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The Payor Bank's Right to Recover Mistaken Payments: Survival of Common Law Restitution Under Proposed Revisions to Uniform Commercial Code Articles 3 and 4

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The Payor Bank's Right to Recover Mistaken Payments: Survival of Common Law Restitution Under Proposed Revisions to Uniform Commercial Code Articles 3 and 4†

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INTRODUCTION

In a case where one person mistakenly pays another person, the courts have traditionally allowed recovery of that payment, at least under circumstances where it would be unjust for the recipient to keep it. This common law restitutionary right is generally available today in a wide range of circumstances. In the context of bank payments, however, the availability of common law restitution is highly problematic, despite there being a number of situations in which a bank might mistakenly pay a customer’s check.1

The perplexing issues generated in this situation revolve around two basic problems. First, the Uniform Commercial Code’s (U.C.C. or Code)2 final payment rule purports to be a limitation on the bank’s restitutionary rights in mistaken payment cases; however, the extent to which this rule bars recovery of such payments is extremely unclear.3 Second, a minority of courts in the nineteenth century developed a warranty theory as an alternative basis for recovery of mistaken bank payments. The drafters of the Code adopted this warranty theory as the primary basis of recovering mistaken payments but failed to address how the warranty scheme relates to and the extent to which it “displaces” common law restitutionary rights.4 Courts continue to be baffled by these seemingly intractable problems. Not surprisingly, legal scholars have generated a tremendous amount of commentary in an effort to find a solution.5 These efforts have been largely disappointing.

1. For a discussion of common law restitution, see infra notes 17-37 and accompanying text. For a discussion of restitution in the context of mistaken payments by a bank, see infra notes 38-65, 84-179 and accompanying text.
3. The final payment rule is found in U.C.C. §§ 3-418, 4-213 and 4-302. See infra notes 100-79 and accompanying text.
4. For a discussion of warranty under pre-Code law, see infra notes 56-63, 72-83 and accompanying text. For a discussion of warranty under the Code, see infra notes 91-179 and accompanying text.
The first major purpose of this Article is to remedy this situation by analyzing the law relating to recovery of mistaken bank payments. In order to avoid the pitfalls encountered by the existing literature on this subject, this analysis will include a consideration of 1) the historical development of common law restitution and alternative theories of recovering bank payments; 2) the application of these theories in the context of the contemporary check collection system; 3) the historical development of the final payment rule; and 4) the current statutory basis of that rule. This analysis will show that the Code sections related to restitutionary rights and the final payment rule ultimately cannot be reconciled. This results from a major conceptual blunder committed by the drafters of the original Code. The solution to the problems related to recovery of mistaken bank payments lies in amending the relevant Code sections.

A major drafting project is currently underway which proposes to extensively revise articles 3 and 4 of the Code.6 This important project presents a rare and valuable opportunity to fashion a permanent statutory solution to the problem of recovering mistaken bank payments. The second major purpose of this Article is to analyze these proposed revisions to see if the drafters have adequately addressed the concerns discussed herein. This analysis will show that the changes embodied in the proposed revisions of articles 3 and 4 are largely superficial. These changes will fail to remedy the problems surrounding the recovery of mistaken bank payments because the present drafting committee unfortunately has committed essentially the same blunder as the drafters of the original version of the Code committed. In the final part of the Article, a new unified theory of recovery will be suggested as a preferable alternative to the present Code as well as the proposed changes.

I. OVERVIEW OF THE PROBLEM

Inasmuch as this Article will consider the extent to which restitution is available to a bank, it is first necessary to briefly describe the ways in

6. The proposed revisions of the Code (R.U.C.C.) attempt, among other things, to spell out more clearly the effect of final payment upon the payor bank's restitutionary rights. The drafting project, entitled "Commercial Code-Current Payment Methods" is sponsored by the National Conference of Commissioners on Uniform State Laws (N.C.C.U.S.L.) and the American Law Institute (A.L.I.). For background on the R.U.C.C. project, see generally Ballen, Baxter, McTaggart, Nyquist & Rubin, Commercial Paper, Bank Deposits and Collections, and Other Payment Systems, 44 Bus. LAW. 1515, 1538-51 (1989). Revisions to article 3 and article 4 are currently under consideration by the N.C.C.U.S.L. References to the R.U.C.C. are to the article 3 draft and number 1 article 4 draft, both dated February 1, 1990. References to the R.U.C.C. Prefatory Note are to that which accompanied a March 1989 draft.

Passage of the Competitive Equality Banking Act of 1987, Pub. L. No. 100-86 (1987), should be noted. The Equality Banking Act granted the Federal Reserve Board ultimate regulatory authority over the nation's check collection process. Id. § 609(c). Pursuant to this authority the Federal Reserve Board has promulgated regulations. See 12 C.F.R. §§ 210, 229 (1989) [hereinafter Reg. CC]. Reg. CC does not have a significant impact on the issues discussed in this Article. Nevertheless, the effect of Reg. CC will be noted where relevant.
which a bank might mistakenly pay a check and the role that restitution would play in that situation. Following presentment of a check to the payor bank, it can be paid in several ways. The most important are (1) the payor bank can pay the item in cash; and (2) the payor bank can fail to return the item and revoke provisional settlements within the time permitted. In a case where the payor has intentionally or inadvertently failed to make a timely return of the item, the U.C.C. provides that the payor is "accountable" for the amount of the item. This is uniformly interpreted by the courts to mean "liable" for the item.

It is in the process of determining whether an item should be paid that the payor bank might make a mistake and pay an item that is not properly payable. The payor may, for example, pay an item bearing a forged

7. "Presentment" is a demand for payment made upon the drawee bank. U.C.C. § 3-504(1).
8. The U.C.C. defines the "payor bank" as "a bank by which an item is payable as drawn or accepted." Id. § 4-105(b). The payor bank is also referred to as the drawee bank. See id. § 3-102 comment 3. The drawee is the entity on which the check or draft is drawn. Id. § 3-503(2); see also R. Braucher & R. Riegert, INTRODUCTION TO COMMERCIAL TRANSACTIONS 64 (1977); D. Whaley, PROBLEMS & MATERIALS ON NEGOTIABLE INSTRUMENTS 2 (2d ed. 1988).
9. Methods of paying an item, which under the Code are referred to as final payment in order to distinguish them from a provisional payment or settlement, are governed by U.C.C. § 4-213.
10. U.C.C. § 4-213(1)(a). This means simply that the payor disburses cash to the presenting party. Note that when the payor pays the item in cash it settles for and finally pays the item at the same time.
11. If the payor bank decides to dishonor the check, it will return the check to the depositary bank and revoke any provisional credit it may have given. Id. § 4-301(1). The payor must exercise its right to revoke any provisional credits within applicable time limits set by statute, agreement, or clearinghouse rule. Id. §§ 4-301(1), 4-302, 4-213. The deadline may be established by agreement pursuant to U.C.C. § 4-103(1). Absent such agreement, the applicable time period is the "midnight deadline" as defined in U.C.C. § 4-104(h). The midnight deadline "is midnight on its next banking day following the banking day on which it receives the relevant item." Id. § 4-104(h).
12. Id. § 4-302. It is surprisingly common for banks to, for example, delay the decision to pay in an effort to ascertain the validity of the item or the sufficiency of funds in the drawer's account, and liability often results. See, e.g., Western Air & Refrigeration, Inc. v. Metro Bank, 599 F.2d 83, 84-85 (5th Cir. 1979); New Ulm State Bank v. Brown, 558 S.W.2d 20, 22 (Tex. Civ. App. 1977).
13. See infra note 122 and accompanying text.
14. The payor bank may take money out of its customer's account to pay an item only if that item is properly payable. U.C.C. § 4-401(1); see, e.g., National Credit Union Admin. v. Michigan Nat'l Bank, 771 F.2d 154, 156 (6th Cir. 1985); Cumis Ins. Soc'y v. Girard Bank, 522 F. Supp. 414, 418 (E.D. Pa. 1981). Items that are not properly payable include: a check containing a forged drawer's signature (see, e.g., Danning v. Bank of Am. Nat'l Trust & Sav. Ass'n, 151 Cal. App. 3d 961, 969, 199 Cal. Rptr. 163, 168 (1984); Fireman's Fund Ins. Co. v. Security Pac. Nat'l Bank, 85 Cal. App. 3d 797, 805 n.7, 149 Cal. Rptr. 883, 889 n.7, 905 (1978)); the absence of a necessary indorsement (see, e.g., Perini Corp. v. First Nat'l Bank, 553 F.2d 398, 403 (5th Cir. 1977); Bank of the West v. Wes-Con Dev. Co., 15 Wash. App. 328, 331, 548 P.2d 563, 566 (1976)); the material alteration of an item (see O'Malley, supra note 5); and the lack of sufficient funds in the drawer's account from which to pay the item. U.C.C. § 4-104(1)(f). The payor bank may, however, choose to pay the check even though doing so creates an overdraft. Id. § 4-401(1).
RECOVERING MISTAKEN PAYMENTS

indorsement or a forged drawer's signature. Such items are not properly payable. If the payor bank pays an item that is not properly payable it must recredit its customer's account, absent customer negligence or other valid defense.\(^5\)

After an item has been paid through any of the possible methods of payment (whether or not the payment was a mistaken one) the payor bank will be in one of two positions with respect to the party who presented the item. The payor will have actually paid the money out as payment for the item, or the payor will still have the money but be "accountable" for it to a presenting party. This latter case would exist when the payor allowed the midnight (or other) deadline to expire without paying cash out for the item or dishonoring it. This is also precisely the situation the payor bank will find itself in when the item was paid by mistake. Unless it can recover the payment from presenting parties or avoid being held liable by presenting parties, it will bear the loss for the mistaken payment.

The fundamental issues examined in this Article are whether, under the first situation, the payor can use common law restitution to recover funds it mistakenly paid out for an item,\(^6\) or whether, under the second situation, the payor can use common law restitution to avoid having to pay the amount of an item for which it is accountable.

The use of common law restitution in this situation is highly problematic. In more than two hundred years of development the courts have created a complicated array of exceptions and limitations on the availability of restitution to recover mistaken payments. Moreover, both article 3 and article 4 of the Code purport to impose statutory limits on the right to restitution of mistaken payments; however, the precise nature of these limits is unclear. Of particular importance is the relationship between a bank's right to common law restitution and its liability under the accountability provisions of article 4. The payor bank may also assert a warranty action in certain cases of mistaken payment; however, while the scope of that action is fairly certain its impact on the bank's restitutionary right is very unclear. Code limitations on the right of restitution will be examined in detail in the later sections of this Article; however, it is first necessary to examine the common law development of restitution and its role in recovery of mistaken bank payments prior to the Code.

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15. See, e.g., G & R Corp. v. American Sec. & Trust Co., 523 F.2d 1164, 1169 (D.C. Cir. 1975); Isaac v. American Heritage Bank & Trust Co., 675 P.2d 742, 744 (Colo. 1984); Bank of the West, 15 Wash. App. at 238, 548 P.2d at 563. Under U.C.C. §§ 3-406 and 4-406 customer negligence can "preclude" the customer from asserting the forgery or alteration, technically making the item a properly payable one. Id. §§ 3-406, 4-406; Fireman's Fund Ins. Co., 85 Cal. App. 3d at 797, 149 Cal. Rptr. at 883.

16. For a discussion of restitution and other potential claims in this situation, see infra notes 38-39, 84-179 and accompanying text.
II. Recovery of Mistaken Payments Under Pre-Code Law
   A. An Overview of Common Law Restitution

Under the common law action for money had and received, which has its origins in early English law, a plaintiff can obtain restitution of money paid to the defendant by mistake.17 Beginning with the leading case of Moses v. MacFerlan,18 decided in 1760, this action was heavily clothed in equitable considerations.19 These considerations, which are typically discussed under the rubric of unjust enrichment, remain paramount today.20

Under present law, the elements of an action to recover mistaken payments can be simply stated; the plaintiff must show that money (a benefit) paid to the defendant was the result of a mistake, and that it would be unjust to allow the defendant to keep it.21 Because the defendant typically received

20. See, e.g., Morgan Guar. Trust Co. v. American Sav. & Loan Ass'n, 804 F.2d 1487, 1492-94 (9th Cir. 1986), cert. denied, 482 U.S. 929 (1987); Northern Trust Co. v. Chase Manhattan Bank, 582 F. Supp. 1380, 1384 (S.D.N.Y. 1984), aff'd, 748 F.2d 803 (2d Cir. 1984); Federal Ins. Co. v. Groveland State Bank, 37 N.Y.2d 252, 333 N.E.2d 334, 336, 372 N.Y.S.2d 18, (1975) (action is “founded upon equitable principles aimed at achieving justice”). For a case in which the court refused to weigh equitable considerations in a quasi-contract action to recover a mistaken payment, see Consumers Power Co. v. County of Muskegon, 346 Mich. 243, 78 N.W.2d 223 (1956), overruled, Spoon-Shacket Co. v. Oakland County, 356 Mich. 151, 97 N.W.2d 25 (1959); see also Restatement of Restitution § 1 (1937) (“A person who has been unjustly enriched at the expense of another is required to make restitution.”) [hereinafter Restatement]; J. Dawson, supra note 17, at 21-26; D. Dobbs, supra note 17, at 227-29; 1 G. Palmer, supra note 17, at 1-8; 2 G. Palmer, supra note 17, at 500-01; Ames, Assumpsit, supra note 17, at 66; Cohen, supra note 19, at 1336.
21. See, e.g., Morgan Guar. Trust Co., 804 F.2d at 1487 (discussing New York law); American Hominy Co. v. Millikin Nat'l Bank, 273 F. 550, 556 (S.D. Ill. 1920); Louisa Nat'l Bank v. Kentucky Nat'l Bank, 239 Ky. 302, 39 S.W.2d 497, 499 (1931); Ellis & Morton v. Ohio Life Ins. & Trust Co., 4 Ohio St. 628, 651 (1855), overruled, Hamden Lodge, I.O.O.F. v. Ohio Fuel Gas Co., 127 Ohio St. 469, 189 N.E. 246 (1934); Bryan v. Citizens Nat'l Bank, 628 S.W.2d 761, 763 (Tex. 1982); W. Keener, supra note 17, at 20, 43, 139; F. Woodward, supra note 17, at 9; Keener, supra note 17, at 218-22; Note, Effect of Bank's Credit to Payee of Check in Misreliance Upon State of Drawer's Account, 21 Colum. L. Rev. 805, 805 (1921) [hereinafter Note, Effect].
the money innocently, the plaintiff generally is required to notify the defendant that the payment was mistaken and demand its return before bringing suit.22

Traditionally, the courts had restricted recovery to cases where the mistake23 was a mistake of fact, not a mistake of law.24 Although this distinction is heavily criticized by commentators,25 and modified by statute in several states,26 it continues to prevail today in a majority of states.27

22. W. Keener, supra note 17, at 140-41; F. Woodward, supra note 17, at 49-51; Keener, supra note 17, at 211, 218-21.
23. Under the Restatement, "mistake means a state of mind not in accord with the facts." Restatement, supra note 20, § 6; 3 G. Palmer, supra note 17, at 458-61 (unilateral mistake a sufficient basis for restitution in cases of the mistaken performance of a contract). For a discussion on various types of mistake, see 2 G. Palmer, supra note 17, at 481-95; 3 G. Palmer, supra note 17, at 458-61; see also Morgan Guar. Trust Co., 804 F.2d at 1493 (discussing New York law) ("It appears that any unintentional result can be categorized as a 'mistake'.").
25. See, e.g., D. Dobbs, supra note 17, at 760-62; W. Keener, supra note 17, at 87-91; 3 G. Palmer, supra note 17, at 11-14, 281-82, 337-43, 337 n.7, 467-77; 13 S. Williston, A TREATISE ON THE LAW OF CONTRACTS §§ 1581-1582 (3d ed. 1970) ("The rule . . . distinguishing mistake of law from mistake of fact is founded on no sound principle." Id. at 536); Corbin, supra note 17, at 543 n.51; Patterson, Improvements in the Law of Restitution, 40 CORNELL L. REV. 667, 676 (1955).
27. See, e.g., W. Keener, supra note 17, at 85; 3 G. Palmer, supra note 17, at 281, 337; Restatement, supra note 20, § 45 (follows general rule); F. Woodward, supra note 17, at 12, 55; Bohannon v. Manhattan Life Ins. Co., 555 F.2d 1205, 1212 (5th Cir. 1977) (discussing Georgia law). Contra, e.g., Morgan Guar. Trust Co., 804 F.2d at 1493 (discussing N.Y. law); St. Paul Fire & Marine Ins. Co. v. Pure Oil Co., 63 F.2d 771, 773 (2d Cir. 1933); Peterson v. First Nat'l Bank, 162 Minn. 369, 375-78, 203 N.W. 53, 55-56 (1925).

It is important to note that a mistake of fact, which may result in restitution, is distinct from what Professor Dobbs calls "conscious ignorance." D. Dobbs, supra note 17, at 718. When a person acts knowing that he is ignorant as to certain facts, he is not mistaken as to those facts. Id. According to the Restatement, "one who knows that he is ignorant is not mistaken since he has no belief as to the existence or non-existence of facts." Restatement, supra note 20, § 6 comment c. For a discussion on the effect of doubt about facts, see 2 G. Palmer, supra note 17, at 511-14; see also Morgan Guar. Trust Co., 804 F.2d at 1494 (discussing New York law) ("conscious ignorance doctrine inapplicable" to case at bar); F. Woodward, supra note 17, at 18. This conscious ignorance must be distinguished from "unconscious disregard" of the facts which would not preclude recovery of the payment. Id. For a discussion of the significance of this concept in the context of the mistaken payment of checks by a bank, see infra note 230 and accompanying text.

There is authority for the point that to be the basis of restitution the mistake must not be as to some collateral or extrinsic fact. W. Keener, supra note 17, at 74; F. Woodward, supra note 17, at 24. For a discussion on the relationship between this idea and recovery of payments on insufficient funds checks, see W. Keener, supra note 17, at 74-77, 79-80; F. Woodward, supra note 17, at 28-30; infra notes 51-52, 115, 210 and accompanying text.
Clearly the most problematic aspect of an action to recover mistaken payments is that of showing it would be unjust for the defendant to retain the money. It is in this regard that the defendant is entitled to assert virtually any legal or equitable argument showing that it would not be unjust to allow him to retain all or part of the money. While an analysis of all such arguments is beyond the scope of this Article, it is necessary to consider those having particular relevance to the context of check collections.

It is generally said that negligence on the part of the plaintiff in making the payment will not preclude restitution of the money. One justification for this is that since the claim for restitution is not based on the negligence of the defendant, the plaintiff's negligence should not preclude it. Moreover, according to the Restatement of Restitution, "we are not penalized for lack of care unless this results in harm to someone else." In a mistaken payment case the defendant would have been benefitted by the plaintiff's negligent act.

A defense that is generally recognized in a mistaken payments case is the so-called change of position or change of circumstances defense. Ordinarily, granting restitution to the plaintiff does not result in a loss to the defendant; it only compels the defendant to give up a benefit received as the result of a mistake. After restoring the benefit to the plaintiff the defendant will be


29. See, e.g., Morgan Guar. Trust Co., 804 F.2d at 1493 (discussing New York law); City Nat'l Bank v. Crocker Nat'l Bank, 150 Cal. App. 3d 290, 197 Cal. Rptr. 721, 725 (1983); Bank of Naperville, 86 Ill. App. 3d at 1008, 408 N.E.2d at 444. There are, on the other hand, many cases where courts have been willing to deny restitution solely on the basis of the plaintiff's negligence. See, e.g., Chase Manhattan Bank v. Burden, 489 A.2d 494, 497 (D.C. Cir. 1985); Northern Trust Co., 582 F. Supp. at 1384-85 (in discussing where "equities lie" court focuses on carelessness of plaintiff); Rohrville Farmers Union Elev. Co. v. Frison, 77 N.D. 235, 238, 408 N.W.2d 354, 356 (1950).

30. See, e.g., Bank of Naperville, 86 Ill. App. 3d at 1009, 408 N.E.2d at 444; D. Dobbs, supra note 17, at 756.

31. Restatement, supra note 20, § 59 comment a; see also 3 G. Palmer, supra note 17, at 462-63.

32. See, e.g., Morgan Guar. Trust Co., 804 F.2d at 1493-94 (discussing New York law); City Nat'l Bank, 197 Cal. Rptr. at 725; Bryan, 628 S.W.2d at 763; D. Dobbs, supra note 17, at 278-80, 766-71; 3 G. Palmer, supra note 17, at 510-29; Restatement, supra note 20, §§ 69, 142; Costigan, supra note 28; Note, Defense of Change of Position in Cases of Payment Under Mistake on a Negotiable Instrument, 42 Harv. L. Rev. 411, 411 n.1 (1929) [hereinafter Note, Defense of Change of Position]. The Restatement formulations typically include this defense in the statement of the basis for recovery. See, e.g., Restatement, supra note 20, § 17. Other defenses such as estoppel may be an expression of the same principle using different terminology. See, e.g., Bank of Naperville, 86 Ill. App. 3d at 1010, 408 N.E.2d at 446 (court refers to estoppel).
back in the position he was in before the benefit was received, but will clearly be no worse off as a result of the restitution. If, however, the defendant has changed his position by losing or passing on the benefit received, restitution will result in an actual loss to the defendant. Under such circumstances it may be unjust to require the defendant to return the benefit, or its equivalent, to the plaintiff. 33 For most courts this will be the case only when the defendant's responsibility for the mistaken payment is no greater than the plaintiff's responsibility. 34 Moreover, the defendant's change of position constitutes a defense in a restitution action only when the change was non-negligent, 35 irrevocable, 36 and in good faith. 37

B. Special Common Law Restitution Rules in a Commercial Paper Context

There are a number of circumstances in which a bank's payment of a check may be mistaken. 38 If we apply the general principles just reviewed

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33. When restitution will not place the defendant back in the position he was in before the payment was received, it may unjustly enrich the plaintiff at the expense of the defendant. The principle that would call for restitution under some circumstances is the same principle that will preclude restitution in others. See D. Dobbs, supra note 17, at 279-80; W. Keener, supra note 17, at 67; Keener, supra note 17, at 222; see, e.g., City Nat'l Bank, 197 Cal. Rptr. at 726; National Bank of Commerce v. National Mechanics' Banking Ass'n, 55 N.Y. 211, 213 (1873).

34. Costigan, supra note 28, at 212-18; Langmaid, Quasi-Contract—Change of Position by Receipt of Money in Satisfaction of a Preexisting Obligation, 21 Calif. L. Rev. 311, 311 (1933). This will be the case where: 1) the defendant is without fault; 2) the parties are equally at fault; and 3) both are at fault but the defendant is less at fault. Cf. W. Keener, supra note 17, at 65, 67, 72; F. Woodward, supra note 17, at 38-41; Note, Effect, supra note 21, at 805.

35. Note, Defense of Change of Position, supra note 32, at 411 n.1. For a discussion on whether accidental loss of the benefit will preclude the change of position defense, see F. Woodward, supra note 17, at 47-48.

36. City Nat'l Bank, 197 Cal. Rptr. at 721; 3 G. Palmer, supra note 17, at 512-14 & n.8; F. Woodward, supra note 17, at 411; Langmaid, supra note 34, at 313-17.

37. 3 G. Palmer, supra note 17, at 511-12. Note that when the change in the defendant's position is the result of consumption of the benefit by the defendant (i.e. he spent the money), the courts generally reject it as a defense. This will be the case where the defendant spends the money to pay personal or business debts, purchase consumer goods or entertainment, or make gifts. This is sometimes referred to as "beneficial consumption." Id.; F. Woodward, supra note 17, at 45. If, on the other hand, in light of the amount of money, the passage of time, and the financial condition of the payee, restitution will be a significant hardship for him, a court may allow it as a defense. D. Dobbs, supra note 17, at 769-70; Restatement, supra note 20, § 142 comment b; F. Woodward, supra note 17, at 45.

There is some support for the idea that when, as a result of receiving a benefit, the defendant changes his life style and/or incurs expenses that would not have been incurred in the absence of the payment, restitution would be unjust. W. Keener, supra note 17, at 59-60. When the change of position defense is available, the burden of proof is on the defendant. Id. at 74.

38. A bank might pay an item that is not properly payable, supra note 14, under the belief that it is genuine and properly payable. Such a payment may be mistaken as that term is used in the cases and commentary on quasi-contract. See supra notes 23-27 and accompanying text. In the event the bank is forced to recredit its customer's account, supra note 14, the bank will, in turn, seek to recover its payment from the presenting bank or another bank or party to whom the payment was forwarded. O'Malley, supra note 5, at 201.
to the context of the mistaken payment of a check, the bank should be able to obtain restitution of the payment under some circumstances unless the defendant has a defense, such as change of position. 39 This was, in fact, the prevailing rule in English common law prior to 1762. 40 That was the year Lord Mansfield decided the case of Price v. Neal, 41 which profoundly unsettled the law of mistaken payments. In that case, a draft on which the year Lord Mansfield decided the case of the prevailing rule in English common law prior to the defendant has a defense, such as change of
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to the context of the mistaken payment of a check, the bank should be able to obtain restitution of the payment under some circumstances unless the defendant has a defense, such as change of position. 39 This was, in fact, the prevailing rule in English common law prior to 1762. 40 That was the year Lord Mansfield decided the case of Price v. Neal, 41 which profoundly unsettled the law of mistaken payments. In that case, a draft on which the year Lord Mansfield decided the case of the prevailing rule in English common law prior to the defendant has a defense, such as change of

39. In addition to an action for money had and received, a warranty action under § 3-417 or § 4-207 is the basis of recovery with certain types of mistaken payments. See, e.g., Bryan, 628 S.W.2d at 762. Moreover, a negligence action is often brought instead of, or in conjunction with, the money action. See, e.g., City Nat'l Bank, 197 Cal. Rptr. at 723-25 (court fails to differentiate liability under negligence with that under a money action).

We should, however, carefully examine the concept of mistake in the context of paying checks in the check collection system. In this context, it is probable that when a bank pays an item in the face of doubts about the genuineness of a signature, for example, it is probably not paying under a mistake of fact. See supra note 27. The same probably can be said in the case of a bank that pays an item without bothering to check a signature. In such a case it can hardly be said that the bank was mistaken as to the genuineness of the signature when it was consciously ignorant of the matter. See also infra note 230 and accompanying text.

40. See generally Corker, Risk of Loss from Forged Indorsements: A California Problem, 4 STAN. L. REV. 24, 34 (1951); Keener, supra note 17, at 212; O'Malley, supra note 5, at 210; Comment, Broader Liability, supra note 5, at 820 n.50; Note, Allocation, supra note 5, at 1086; Note, Doctrine, supra note 5, at 199.


43. Id.

44. See, e.g., South Boston Trust Co. v. Levin, 249 Mass. 45, 49, 143 N.E. 816, 817 (1924); Germania Bank v. Boutell, 60 Minn. 189, 191, 62 N.W. 327, 328 (1895); W. Keener, supra note 17, at 154; 3 G. PALMER, supra note 17, at 291; F. WOODWARD, supra note 17, at 127; Beasley, Liability of Drawee Bank Where a Check or Bill Has Been Materially Altered Before Payment, Acceptance or Certification—Inability of Drawee to Recover Payment From Holder Under Section 62 of the Negotiable Instruments Law, 10 TENN. L. REV. 87, 88 (1931); Langmaid, supra note 34, at 346; Palmer, Negotiable Instruments Under the Commercial Code, 48 Mich. L. Rev. 255, 295 (1950); Note, Relation of Price v. Neal to the Doctrine of Purchaser for Value Without Notice, 26 HARV. L. REV. 634, 634 (1913) [hereinafter Note, Relation]; Note, Allocation, supra note 5, at 1086.
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Given that the rationale for *Price v. Neal* is unclear,


Second, the recipient's *change of position* in reliance on the mistaken payment precludes recovery of the payment by the drawee under this well established defense to a restitutionary action. An early leading case focusing on this rationale is Cocks v. Masterman, 9 B. & C. 902, 908-09 (K.B. 1829). For an example of cases where this rationale is relied on, in part, see Merchants' Nat'l Bank v. National Bank, 139 Mass. 513, 518, 2 N.E. 89, 90 (1885) (without a change of position on the part of the recipient of the payment, the drawee can recover a mistakenly paid insufficient funds item); see also Aigler, *The Doctrine of Price v. Neal*, 24 Mich. L. Rev. 809, 813 (1926) (discussing Cocks); Beasley, *supra* note 44, at 89; Note, *Holder in Due Course: Case Analyzed*, 15 Harv. L. Rev. 451, 458 (1923) [hereinafter Note, *Holder*].

Third, the rule is commonly supported by a *policy of finality*. Promoting certainty in commercial transactions requires an end to the process of check collections at some point. G. Palmer, *supra* note 17, at 291 ("perhaps the most important" among several factors); Aigler, *supra*, at 811, 815, 819 (at least subconscious in Lord Mansfield's opinion and express in later cases); O'Malley, *supra* note 5, at 202, 203 n.84, 227-28 & n.234 ("no expressed support for this theory" in opinion, but by consensus is the "only satisfactory explanation"); Woodward, *The Risk of Forgery or Alteration of Negotiable Instruments*, 24 Colum. L. Rev. 469, 470 (1924). For an example of this rationale being used by courts, see Fireman's Fund Ins. Co., 85 Cal. App. 3d at 797-98, 149 Cal. Rptr. at 904 ("drafters recognize as the only valid basis for the rule ... "). Related rationales are that of maintaining confidence in commercial paper and commercial convenience, see, e.g., Germania Bank, 60 Minn. at 192-93, 62 N.W. at 328-29; Note, *Allocation of Losses from Check Forgeries Under the Law of Negotiable Instruments and the Commercial Code*, 62 Yale L.J. 417, 420 n.17 (1953) [hereinafter Note, *Losses*].

Fourth, some authorities cite the drawee's *negligence* in paying a check as a rationale for the rule. O'Malley, *supra* note 5, at 202; Note, *Losses, supra*, at 420 n.17, 441 n.107 (original justification for rule, but unrealistic under modern banking practices). For an example of a court using negligence as a basis for the rule, see Citizens' Bank v. J. Blach & Sons, 228 Ala. 246, 249, 153 So. 404, 406 (1934). Related to the negligence rationale is the idea that the rule encourages banks to be cautious in examining signatures. Farnsworth, *Insurance Against Check Forgery*, 60 Colum. L. Rev. 284, 302 (1960) [hereinafter Farnsworth, *Insurance*]; Comment, *Broader Liability, supra* note 5, at 825.

Fifth, some commentators, notably Ames, argue that the rule is based on the principle that between two persons having equal equities, the one with legal title should prevail. Ames, *Price v. Neal, supra* note 19, at 299-301; O'Malley, *supra* note 5, at 202, 203 n.85. For an example of a court using this rationale, see Gloucester Bank, 17 Mass. at 41.

Sixth, some courts and commentators suggest that the rule is justified on the basis that the drawee is *bound to know the drawer's signature and is estopped from denying its validity once the item is paid or accepted*. See First Nat'l Bank v. First Nat'l Bank, 151 Mass. 280, 283, 24 N.E. 44, 45 (1890); American Sur. Co. v. Industrial Sav. Bank, 242 Mich. 581, 584, 219 N.W. 689, 690 (1928) ("the duty of the drawee to know the signature of the drawer"); F. Woodward, *supra* note 17, at 129 (strongly suggested by Lord Mansfield's opinion; "favorite explanation"); see also Lawrence, *Misconceptions About Article 3 of the Commercial Code: A Suggested Methodology and Proposed Revisions*, 62 N.C.L. Rev. 115, 132 (1983)
it is difficult to ascertain the relationship between the case and the common law of mistaken payments. Opinions range from the view that the rule is entirely consistent with the general rule governing recovery of mistaken payments\textsuperscript{46} to the view that the rule is an unjustified aberration of the law of mistaken payments.\textsuperscript{47}

Despite these uncertainties, the \textit{Price v. Neal} rule was later adopted by all but a few jurisdictions in the United States.\textsuperscript{48} This pervasive willingness

\begin{flushleft} \textit{"\text{[T]he drawee assumes the risk of payment over the forged signature of the drawer."}}.\textsuperscript{46} \end{flushleft}  

Seventh, one commentator argued that the refusal in \textit{Price v. Neal} to allow recovery resulted from a simple application of the law of mistake in that, under the facts, it was not against good conscience for the defendant to retain the money. Aigler, supra, at 810-11; see also Bernheimer, 2 Minn. at 81-82.

Eighth, Wigmore suggested that the refusal to refund the money in this type of case is based on the idea that there was no mistake with respect to the drawee's duty to the holder. Wigmore, \textit{A Summary of Quasi-Contracts}, 25 Am. L. Rev. 695, 706 (1891). This rationale was more prevalent in insufficient fund cases than in other types of mistaken payments. See, e.g., Boylston Nat'l Bank v. Richardson, 101 Mass. 287, 291 (1869).

Ninth, Keener argued that the denial of recovery ought to be based on the idea that the defendant received money from the plaintiff in \textit{extinguishment of a right} he surrendered for the money and should not be required to return the money. W. Keener, supra note 17, at 157.

Tenth, Professor Farnsworth argues that the rule is justified as a more efficient distribution of losses by placing the loss on the party able to spread the loss through insurance, although he acknowledges that this idea was not part of Lord Mansfield's opinion. Farnsworth, \textit{Insurance}, supra, at 302-03.

Courts typically rely on more than one of these rationales. See, e.g., Commercial & Farmers Nat'l Bank v. First Nat'l Bank, 30 Md. 11 (1869). The confusion over the rationale for the decision may result, in part, from errors in reporting Lord Mansfield's remarks from the bench. The court in \textit{Ellis & Morton}, 4 Ohio St. at 628, remarked that the opinion "is not very clearly reported," and then declined to advance its own views on the rationale for the holding. \textit{Id.} at 653. Professor Palmer suggests that "[s]ome of the disagreement stems from the common error of assuming that the decision rested on a single overriding policy, whereas in fact it probably was a response to several factors." 3 G. Palmer, supra note 17, at 291.

\text{Aigler, supra note 45, at 810-11 ("[U]nder the facts it was not against good conscience for the defendant-holder, to whom the drawee ... had paid the money called for, to retain it."); Beasley, supra note 44, at 91-92.}

\text{First Nat'l Bank v. Bank of Wyndmere, 15 N.D. 229, 305, 108 N.W. 546, 549 (1906) (the court characterizes the doctrine as "unsound"); American Express Co. v. State Nat'l Bank, 27 Okla. 824, 827, 113 P. 711, 712 (1911) (the doctrine is "unsound and illogical"); First Nat'l Bank v. Farmers' & Merchants' State Bank, 146 S.W. 1034, 1035 (Tex. Civ. App. 1912) ("[T]he magic name of Mansfield has not been sufficient to render perpetual the heresy taught by him ...."); W. Keener, supra note 17, at 154 n.1; Beasley, supra note 44, at 89.}

\text{See, e.g., Bank of the United States v. Bank of Ga., 23 U.S. (10 Wheat.) 333, 348-52 (1823) ("The case of \textit{Neal v. Price} [sic] has never since been departed from; and ... it has had the uniform support of the Court, and has been deemed a satisfactory authority."); Commercial & Farmers Nat'l Bank, 30 Md. at 19 ("authority of the case ... has been uniformly and abundently sustained"); Gloucester Bank, 17 Mass. at 43; \textit{Neal v. Coburn}, 92 Me. at 147, 42 A. at 350-51; \textit{American Sur. Co.}, 242 Mich. at 584 ("The great majority of American courts have in the final analysis followed the doctrine of \textit{Price v. Neal} ...."); Germania Bank, 60 Minn. at 191, 62 N.W. at 328 ("This general doctrine is recognized as the law by the courts of every state in the Union except Pennsylvania ...."); National Park Bank, 46 N.Y. at 81; Bank of Williamson v. McDowell County Bank, 66 W. Va. 553, 530, 66 S.E. 761, 764 (1909) (court acknowledges criticism, but adheres to the rule calling it}
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of courts to adopt the *Price v. Neal* rule must be compared, however, with their reluctance to expand the rule beyond the facts of the case. Protection from the drawee's restitutionary action was generally available only to holders who paid value for the draft and who were acting in good faith at the time payment was received. In addition, protection was denied to holders who were negligent in originally obtaining the instrument or the payment. The only notable expansion of the rule was to the mistaken payment of checks drawn on insufficient funds and no account

"indispensable"). *Contra Bank of Wyndmere*, 15 N.D. at 305, 108 N.W. at 546 (court characterizes the doctrine as "unsound"); *American Express Co.*, 27 Okla. at 827, 113 P. at 712 (doctrine is "unsound and illogical"); *Farmers' & Merchants' State Bank*, 146 S.W. at 1035 ("[T]he magic name of Mansfield has not been sufficient to render perpetual the heresy taught by him . . . ."). In both the *Bank of Wyndmere* case and the *American Express Co.* case the courts would allow, under the traditional law of mistake, the recipient's good faith, non-negligent change of position in reliance on the mistaken payment to preclude recovery by the drawee. In 1849, Pennsylvania enacted a statute abolishing the *Price v. Neal* rule. *Pa. Stat. Ann.* tit. 426, § 10 (Purdon 1853); see *Union Nat'l Bank v. Franklin Nat'l Bank*, 249 Pa. 375, 94 A. 1085 (1915); see also 3 G. PALMER, supra note 17, at 292; Aigler, supra note 45, at 816-17; Ames, Price v. Neal, supra note 19, at 297-98; Beasley, supra note 44, at 87 ("well settled rule"); O'Malley, supra note 5, at 202 ("an instantaneous and apparently permanent success"); Steinheimer, *Impact of the Commercial Code on Liability of Parties to Negotiable Instruments in Michigan*, 53 Mich. L. Rev. 171, 209-10 (1954).

49. See, e.g., *Commercial & Sav. Bank Co. v. Citizens' Nat'l Bank*, 68 Ind. App. 417, 425, 120 N.E. 670, 672 (1918); *Bank of St. Albans v. Farmers & Mechanics Bank*, 10 Vt. 141, 147 (1838); see also 3 G. PALMER, supra note 17, at 292; Aigler, supra note 45, at 821-23 (protection should be denied to holders who were in complicity with the forger); Ames, Price v. Neal, supra note 19, at 301; O'Malley, supra note 5, at 204-05.

50. See, e.g., *First Nat'l Bank*, 151 Mass. at 283-84, 24 N.E. at 45; *Germania Bank*, 60 Minn. at 193, 62 N.W. at 329 ("[T]he trend of the modern authorities is to impose upon [the rule] some limitations and modifications."); *Ellis & Morton*, 4 Ohio St. at 652; *People's Bank v. Franklin Bank*, 88 Tenn. 299, 302-03, 12 S.W. 716, 716-17 (1889); *Bank of Williamson*, 66 W. Va. at 550-52, 66 S.E. at 763-65; see also *First Nat'l City Bank v. Altman*, 3 U.C.C. Rep. Serv. (Callaghan) 815, 816-17 (N.Y. Sup. Ct. 1966) (the *Price v. Neal* rule does not apply in a case where the defendant purchaser was negligent in obtaining the instrument). *Contra Bernheimer*, 2 Minn. at 85; *National Park Bank*, 46 N.Y. at 81-82; see also W. Keener, supra note 17, at 154 n.1; Aigler, supra note 45, at 820-21, 823; O'Malley, supra note 5, at 205 & n.93.

In most cases the holder's negligence was the failure to obtain proper identification from a stranger before taking a check. See, e.g., *People's Bank*, 88 Tenn. at 303-04, 12 S.W. at 717. *But see Bank of St. Albans*, 10 Vt. at 147-48 (the failure to obtain proper identification did not preclude protection under the rule); O'Malley, supra note 5, at 205 n.93. The drawee's negligence may excuse the defendant's negligence. See, e.g., *Woods v. Colony Bank*, 114 Ga. 683, 687, 40 S.E. 720, 722 (1902). *Contra People's Bank*, 88 Tenn. at 302-03, 12 S.W. at 717. The plaintiff's negligence was generally not relevant unless it prejudiced the defendant. See, e.g., *First Nat'l Bank*, 151 Mass. at 284, 24 N.E. at 45; *Note, Effect*, supra note 21, at 805 (plaintiff, even if negligent, can recover if his act has not changed the position of an innocent defendant to his detriment).

51. See, e.g., *Manufacturers' Nat'l Bank* v. *Swift*, 70 Md. 515, 518, 17 A. 336, 337 (1889); *Boylston Nat'l Bank*, 101 Mass. at 290-91; *Spokane & Eastern Trust Co. v. Huff*, 63 Wash. 225, 226, 115 P. 80, 81 (1911). *But see Merchants' Nat'l Bank* v. *National Eagle Bank*, 101 Mass. 281, 285 (1869) (the recovery of a mistakenly paid insufficient funds item allowed unless the recipient had changed position in reliance on the payment); see also W. Keener, supra
checks. In these situations, as in the case of a forged drawer's signature, the payment was final and could not be recovered by the drawee so long as the holder was acting in good faith, was not negligent, and had taken the instrument for value. On the other hand, in cases involving other types of mistaken payments, such as payment of an item bearing a forged indorsement, or fraudulent, material alteration, the courts refused to extend Price v. Neal. Accordingly, in such cases restitution remained available to

note 17, at 77; 3 G. PALMER, supra note 17, at 300-01, 300 n.44; Ames, Price v. Neal, supra note 19, at 305; Keener, supra note 17, at 214; Langmaid, supra note 34, at 346 n.124; Woodward, supra note 45, at 474.

The rationale for such an extension is clear. Essentially all of the arguments for finality in a forged drawer situation apply with equal force to an insufficient funds situation. See, e.g., Manufacturers' Nat'l Bank, 70 Md. at 520-21, 17 A. at 337; Germania Bank, 60 Minn. at 193, 62 N.W. at 329; Liberty Trust Co. v. Haggerty, 92 N.J. Eq. 609, 612-13, 113 A. 596, 597-98 (N.J. Ch. 1921), aff'd sub nom. Liberty Trust co. v. Ford, 93 N.J. Eq. 198, 115 A. 926 (1921) (per curiam) (no mistake made and finality of transactions); Spokane & Eastern Trust Co., 63 Wash. at 226-29, 115 P. at 81-82; see also 3 G. PALMER, supra note 17, at 300-01, 300 n.44; Restatement, supra note 20, § 33.


53. See, e.g., Ames, Price v. Neal, supra note 19, at 305; Keener, supra note 17, at 214. The rule was also extended to notes, both as to a forged maker's signature and altered amounts. See, e.g., Bank of the United States, 23 U.S. (10 Wheat.) at 355; Gloucester Bank, 17 Mass. at 43; 3 G. PALMER, supra note 17, at 299 n.40.

The application of the rule to both payment and acceptance does not constitute an expansion of the rule because Price v. Neal involved two drafts, one paid and the other accepted. See, e.g., National Park Bank, 46 N.Y. at 81; First Nat'l Bank v. United States Nat'l Bank, 100 Or. 264, 279-80, 197 P. 547, 552-53 (1921); Levy v. Bank of the United States, 1 Binn. 27, 35 (Pa. 1802); Bank of St. Albans, 10 Vt. at 145.

54. With respect to forged indorsements, see National Park Bank, 46 N.Y. at 81; W. Keener, supra note 17, at 154 n.1; 3 G. PALMER, supra note 17, at 283; Corker, supra note 40, at 24; O'Malley, supra note 5, at 228; Woodward, supra note 45, at 474-76. The same rule applied in cases of a forged indorsement on a note. 3 G. PALMER, supra note 17, at 285 & n.19.

The rationale for refusing to extend the Price v. Neal rule to cases involving forged indorsements is typically that the party dealing with the forger is in the best position to detect that type of forgery. See, e.g., Canal Bank v. Bank of Albany, 1 Hill 287, 293 (N.Y. Sup. Ct. 1841); Bank of the West v. Wes-Con Dev. Co., 15 Wash. App. 238, 241-42, 548 P.2d 563, 566 (1976).

With respect to material alterations, see Espy v. Bank of Cincinnati, 85 U.S. (18 Wall.) 604, 619 (1873); Wells Fargo Bank & Union Trust Co. v. Bank of Italy, 214 Cal. 156, 160, 4 P.2d 781, 783 (1931); Parke v. Roser, 67 Ind. 500, 503 (1879); National Bank of Commerce v. National Mechanics' Banking Ass'n, 55 N.Y. 211, 216-17 (1873); Clewes v. Bank of N.Y. Nat'l Banking Ass'n, 89 N.Y. 418, 422 (1882); see also W. KEENER, supra note 17, at 154 n.1; 3 G. PALMER, supra note 17, at 296; Farnsworth, Insurance, supra note 45, at 309 & n.127 (split of authority); O'Malley, supra note 5, at 261. If a materially altered item was accepted, the drawee was liable only in the original amount. 3 G. PALMER, supra note 17, at 296. If the item was paid, the drawee could recover the difference between the original amount and the altered amount. Id; see also O'Malley, supra note 5, at 261.

Although restitution remained available in cases of materially altered drafts, courts followed Price v. Neal in cases of materially altered notes on the rationale that makers were "bound to know [their] own notes." Bank of the United States, 23 U.S. (10 Wheat.) at 351; see also 3 G. PALMER, supra note 17, at 299 & n.40.
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the drawee through an action for money had and received, subject, however, to the traditional defenses such as change of position.55

Looking at the law governing the recovery of mistaken payments of checks and other drafts at the end of the nineteenth century, it is clear that the great weight of authority called for the application of quasi-contract principles to allow restitution in cases of forged indorsements, material alterations, and other circumstances that did not fall within the Price v. Neal rule. At the same time, however, some courts began developing alternative theories of recovery in mistaken payment cases. Some of these were to change fundamentally the law of recovering mistaken payments.

The most significant of these alternative theories of recovery originated in the practice of a few courts implying a warranty of good title from the act of presenting for payment (or acceptance).56 Under this approach, a holder who presented an item bearing a forged indorsement did not have good title and was, therefore, in breach of warranty and obligated to refund the payment. Inasmuch as the presence of a forged drawer's signature did not affect good title to the item,57 the distinction between these types of forgeries that existed under quasi-contract principles was preserved under the implied warranty theory.58 Over the last hundred years commentators

55. 3 G. PALMER, supra note 17, at 283-84, 297; O'Malley, supra note 5, at 228-29, 261; Rogers, The Irrelevance of Negotiable Instruments Concepts in the Law of the Check-Based Payment System, 65 TEX. L. REV. 929, 956 & n.84 (1987) (recovery with respect to forged indorsements rested on a simple restitutionary analysis with a common law action in assumpsit); Steinheimer, supra note 48, at 209-11.

A holder who in good faith changed position in reliance on the payment will not be required to return the payment to the drawee so long as the holder is not more responsible than the drawee for the mistake. See, e.g., National Park Bank v. Seaboard Bank, 114 N.Y. 28, 33-35, 20 N.E. 632, 633-34 (1889) (a change of position precluded the recovery of an altered item mistakenly paid); see also Rogers, supra, at 956 n.84 (disclosed agent defense); Note, Defense of Change of Position, supra note 32, at 411-13.

Following the general common law rule, the negligence of the drawee in paying the instrument typically did not preclude recovery of the payment in a case falling outside of the Price v. Neal rule. F. WOODWARD, supra note 17, at 143. If, however, the drawee is negligent in failing to give prompt notice of the forgery after its discovery, the drawee cannot recover the payment from a defendant who was prejudiced by the delay. Id.

56. See, e.g., Leather Mfrs.' Bank v. Merchants' Bank, 128 U.S. 26, 35 (1888); Merchants' Nat'l Bank v. First Nat'l Bank, 3 F. 66, 67 (C.C.D. Md. 1880); see also 3 G. PALMER, supra note 17, at 283; Corker, supra note 40, at 34; O'Malley, supra note 5, at 228, 261; Rogers, supra note 55, at 956 n.84; Steinheimer, supra note 48, at 209-11.


58. This warranty was sometimes viewed as a warranty of genuineness with respect to signatures, and, for a majority of courts, this warranty did not encompass the drawer's
have heavily criticized this development.59 Despite the criticism, the implied warranty of title persisted in mistaken payment cases, albeit as a minority view.60 In some cases it was relied upon as the sole basis of recovery;61 in other cases it was a basis of recovery in addition to quasi-contract principles.62

There was a parallel development in cases where a fraudulently and materially altered item was mistakenly paid. While the large majority of courts allowed recovery under quasi-contract principles, a few courts allowed recovery under a warranty of genuineness implied in the presentment.63 This development was subject to the same criticism as the development of warranty in cases of forged indorsements.

The end of the nineteenth century brought the formation of the National Conference of Commissioners on Uniform State Laws (N.C.C.U.S.L.) and the organized movement toward uniform state laws.64 The first project of the N.C.C.U.S.L. was the Uniform Negotiable Instruments Law (N.I.L.), promulgated in 1896 and eventually adopted in all states.65 Inasmuch as the
N.I.L. is the statutory predecessor of article 3 of the Code, it is useful to briefly examine how it dealt with the problem of recovering mistaken payments.

C. Recovery of Mistaken Payments Under the Uniform Negotiable Instruments Law

Although the N.I.L. gave no explicit recognition to the *Price v. Neal* rule, the courts in an overwhelming majority of jurisdictions found that the *Price v. Neal* rule was incorporated into the N.I.L. For most courts the vehicle for retaining the rule was section 62 which provided that by accepting the instrument the acceptor admits the genuineness of the drawer's signature. This admission precluded a claim by the drawee that the payment was mistakenly made over a forged drawer's signature, thereby preserving the result in *Price v. Neal*. A few courts brought the *Price v. Neal* rule into the N.I.L. through section 196 as a supplementary common law principle. Through one approach or the other, the rule in *Price v. Neal* became firmly established under the N.I.L., although disputes continued over whether finality of payment was limited to cases where the recipient was a holder in due course and whether a negligent recipient was entitled

66. N.I.L. § 62 (1920); see, e.g., American Hominy Co., 273 F. at 556; National Bank v. First Nat'l Bank, 141 Mo. App. 719, 729-30, 125 S.W. 513, 516 (1910); Banca Commerciale Italiana Trust Co. v. Clarkson, 274 N.Y. 69, 72-73, 8 N.E.2d 281, 282 (1937); United States Nat'l Bank, 100 Or. at 287-88, 197 P. at 552-53; Fidelity & Casualty Co. v. Planenscheck, 200 Wis. 304, 305-06, 227 N.W. 387, 388-89 (1929); see also Aigler, supra note 45, at 818; Beasley, supra note 44, at 91-93; O'Malley, supra note 5, at 202-05; Palmer, supra note 44, at 295. There was, on the other hand, some doubt as to whether N.I.L. § 62 was intended to codify *Price v. Neal*. See Steinheimer, supra note 48, at 207.

67. N.I.L. § 62(1).

68. Notice, however, that according to the language of the section the admission is deemed to be made only in cases of acceptance of an instrument. Most courts simply extended this concept to encompass payment, thereby precluding recovery there as well. See, e.g., Title Guar. & Trust Co. v. Haven, 126 A.D. 802, 804-05, 111 N.Y.S. 305, 307 (1908); Commerce-Guardian Bank v. Toledo Trust Co., 60 Ohio App. 337, 21 N.E.2d 173 (1938) (payment includes acceptance); Fidelity & Cas. Co., 200 Wis. at 305-06, 227 N.W. at 388-89. *But see* Union Nat'l Bank v. Franklin Nat'l Bank, 249 Pa. 375, 94 A. 1085 (1915); see also 3 G. Palmer, supra note 17, at 292; Palmer, supra note 44, at 295 n.147.

69. See, e.g., South Boston Trust Co. v. Levin, 249 Mass. 45, 143 N.E. 816, 817 (1924); see also Aigler, supra note 45, at 818. N.I.L. § 196 provided: "In any case not provided for in this act the rules of [law and equity including] the law merchant shall govern." N.I.L. § 196. This section is the statutory predecessor of U.C.C. § 1-103. U.C.C. § 1-103 Official Comment (Frier Statutory Provision); Hillman, Construction of the Commercial Code: UCC Section 1-103 and "Code" Methodology, 18 B.C. INDUS. & COM. L. REV. 655, 659 n.21 (1977).

to protection.\textsuperscript{71}

With respect to recovery of payments over forged indorsements and material alterations under the N.I.L., an overwhelming majority of courts continued to adhere to quasi-contract principles allowing recovery of the payment unless the recipient changed his position in reliance on the payment or could assert some other affirmative defense;\textsuperscript{72} however, the erosion of the dominant quasi-contract approach accelerated under the N.I.L. The N.I.L. sections 65 and 66 codified the common law transfer warranty of genuineness and good title.\textsuperscript{73} This warranty was, by the terms of the statute, made only in the transfer and negotiation process, and most courts limited the application of the warranty accordingly.\textsuperscript{74} However, a persistent and apparently growing minority of courts extended this warranty from the transfer and negotiation process to the presentment process.\textsuperscript{75} This was heavily criticized as inappropriate on the grounds that a presentment is not a negotiation and a signature by the presenter is not an indorsement.\textsuperscript{76}

Some courts, unwilling to extend the N.I.L. transfer warranties to the presentment process, continued to find a warranty implied in that process as they had done at common law.\textsuperscript{77} Thus, under either an implied warranty theory or the extension of a statutory warranty, the drawee that paid an item bearing a forged indorsement could recover the payment from the recipient.

With respect to the recovery of payments made on altered items, the prevailing view under the N.I.L. was that such payments could be recov-


\textsuperscript{72} See, e.g., United States Nat'l Bank, 100 Or. at 290-92, 197 P. at 556; 3 G. Palmer, supra note 17, at 283.

\textsuperscript{73} N.I.L. §§ 65, 66; Cohen, supra note 19, at 1348 n.45; Note, Defense of Change of Position, supra note 32, at 412.

\textsuperscript{74} See, e.g., American Hominy Co., 273 F. at 555; Louisa Nat'l Bank v. Kentucky Nat'l Bank, 239 Ky. 302, 308-10, 39 S.W.2d 497, 499-500 (1931); see also Corker, supra note 40, at 34 n.27; Rogers, supra note 55, at 956 n.84.

\textsuperscript{75} See, e.g., Security Sav. Bank, 106 F.2d at 545; American Exch. Nat'l Bank v. Yorkville Bank, 122 Misc. 616, 621, 204 N.Y.S. 621, 626 (Sup. Ct. 1924); O'Malley, supra note 5, at 228; Palmer, supra note 44, at 299 n.165 (cites considerable uncertainty as to whom warranties run).

\textsuperscript{76} See, e.g., Security Sav. Bank, 106 F.2d at 545 (acknowledges criticism); United States Nat'l Bank, 100 Or. at 289-90, 197 P. at 555-56; see also Corker, supra note 40, at 34 n.27; Farnsworth, Insurance, supra note 45, at 310; Rogers, supra note 55, at 957 n.84. For a discussion of the presentment warranty under common law, see supra notes 56-63 and accompanying text.

\textsuperscript{77} See, e.g., Clearfield Trust Co., 318 U.S. at 368-69 (discussing federal law); Note, Losses, supra note 45, at 422 n.21; supra notes 56-63 and accompanying text.
For most courts, this result was reached through the application of quasi-contract principles. Some courts, however, allowed for the recovery of altered items under a warranty action.

We can see from this survey of pre-Code law (both common law and the N.I.L.) that recovery of the payment of an item with a forged indorsement was widely available; recovery in a case of material alteration was less so. In cases of a forged drawer's signature, finality of payment under the Price v. Neal rule was nearly universal, but the availability of its protection was restricted. The rule was extended only to items drawn on insufficient funds and no account items. The dominant theory or basis of recovery or its denial was quasi-contract, but the alternative implied warranty theory, which was established at common law, continued under the N.I.L. It was complimented by the extension of the N.I.L. statutory warranty to the presentment process.

It must be emphasized that although quasi-contract and warranty were alternative theories of recovering mistaken payments, as they developed, the similarity between them became increasingly superficial. They both retained the same general treatment of the different types of mistaken payments.


80. The use of an implied warranty of genuineness theory still persisted among some courts. O'Malley, supra note 5, at 261. For an example of a case in which the court finds that the N.I.L. statutory warranties preempt the implied warranties, see Kansas Bankers Sur. Co., 184 Kan. at 536-37, 338 P.2d at 315-16. Other courts were willing to extend the statutory transfer warranty of genuineness to the presentment process and allow for recovery of altered items on that basis. See, e.g., Seaboard Sur. Co. v. First Nat'l City Bank, 15 Misc. 2d 816, 817-18, 180 N.Y.S.2d 156, 157-58 (N.Y. City Ct. 1958).

It should be noted that the tendency of courts to deny recovery of a payment on an altered item was greater under the N.I.L. than under the common law. Under § 62, a drawee who had accepted an altered item was bound to pay it to a holder as accepted; that is, in the altered amount. See, e.g., National City Bank v. National Bank, 300 Ill. 103, 132 N.E. 832 (1921). This view, which some courts limited to acceptance, while others extended it to payment (see, e.g., Kansas Bankers Surety Co., 184 Kan. at 533-34, 537, 338 P.2d at 313, 316) was prevalent among a minority of courts, and received significant support from commentators. See, e.g., National City Bank, 300 Ill. at 108-09, 132 N.E. at 833-34. Contra McClendon, 188 Mo. App. at 426-28, 174 S.W. at 205 (N.I.L. § 62 does not preclude recovery of the mistaken payment of a materially altered item); Beasley, supra note 44, at 93-94. As a result of this section, the implied warranty theory, the extended statutory warranty, and the application of quasi-contract principles, there existed considerable uncertainty under the N.I.L. over the recovery of payments on altered items.

However, under warranty, the plaintiff no longer had to show unjust enrichment on the part of the defendant. In addition, the change of position and other defenses of an equitable nature were discarded under the warranty theory, resulting in it becoming a distinct theory of recovery.

The provisions of the N.I.L. governed the recovery of mistaken payments until the development of the Code in the middle of this century. The next section of this Article will examine recovery of mistaken payments under the Code, focusing on whether and to what extent common law restitution survived the adoption of the Code.

III. RECOVERY OF MISTAKEN PAYMENTS UNDER THE UNIFORM COMMERCIAL CODE

A. Displacement of the Common Law Under U.C.C. Section 1-103

The process of determining the extent to which a common law restitutionary action has survived the enactment of the U.C.C. must begin with section 1-103. It provides in relevant part: "Unless displaced by the particular provisions of this Act, the principles of law and equity, including . . . the law relative to . . . mistake . . . shall supplement its provisions." Under the language of this section, the common law governing cases of mistaken payments, especially the action for money had and received, will supplement the Code provisions (including the Code remedies) unless it has been displaced by the "particular" provisions of the Code. The crucial issue here, of course, is determining the meaning of "displaced." Some courts subscribe to the view that the common law can only be expressly displaced.

82. Steinheimer, supra note 48, at 207; Note, Allocation, supra note 5, at 1080.
83. See Farnsworth, Insurance, supra note 45, at 310; O'Malley, supra note 5, at 263; Note, Defense of Change of Position, supra note 32, at 412. The distinction between restitution and warranty as bases of recovery becomes more apparent under the Code.
84. U.C.C. § 1-103 (1989) (emphasis added). For a discussion on the operation of § 1-103, see generally Hillman, supra note 69; Nickles I, supra note 64, at 47-53; Nickles II, supra note 65; Summers, General Equitable Principles Under Section 1-103 of the Commercial Code, 72 Nw. U.L. Rev. 906 (1978).
Because instances of express displacement of common law are relatively rare under articles 3 and 4 of the Code, the concept of implied displacement becomes central to the issue.

Most of the cases where the courts have found that the Code had impliedly displaced the common law involved inconsistencies between the common law and the language of the Code. For these courts, to the extent that there were such inconsistencies, section 1-103 requires that the Code sections prevail, but otherwise the common law survives. "Implied" in this context operates essentially as a matter of logical necessity in the context of the statutory language. Under this approach, the common law survives so long as that result is not logically inconsistent with the language of the Code.

Some courts hold a much more expansive view of the concept of displacement. For these courts, the focus is on the broader policies and purposes of the Code or of a statutory scheme within the Code. Under this view, the Code may displace the common law rules even though there are no inconsistencies between the common law and the language of the Code. Although this approach entails the difficulty of ascertaining the Code's purposes and policies, it seems to be more consistent with the command of section 1-102 that the Code "shall be liberally construed and applied to promote its underlying purposes and policies."

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86. Those that can be found are in the official comments rather than the Code sections. See, e.g., U.C.C. § 3-418 Official Comment (1978) ("The section rejects decisions under the [N.I.L.] . . ."); id. § 3-415 Official Comment ("Subsection (5) is intended to change the result of such decisions as . . ."); see also id. § 2-206 Official Comment ("Former technical rules as to acceptance, . . . are rejected . . .").


88. In other words, if a particular cause of action existed at common law under particular circumstances and, under the Code, a modified form of the cause of action is available under identical circumstances, one could say that the Code has impliedly changed the common law. On the other hand, in the absence of any logical inconsistencies between the common law and the Code, the common law survives. See, e.g., E.F. Hutton & Co., 149 Cal. App. 3d at 69, 196 Cal. Rptr. at 620. Professor Robert Summers subscribes to a narrow view of displacement, Summers, supra note 84, at 935-39; however, he would allow policy considerations to justify displacement in some cases.


90. U.C.C. § 1-102. The expansive approach also has the support of some commentators. See R. Hillman, J. McDonnell & S. Nickles, COMMON LAW AND EQUITY UNDER THE COMMERCIAL CODE, ¶ 1.04[2] (1985); Hillman, supra note 69; Nickles II, supra note 65, at 225-30 (expansive approach proper when the result is consistent with Code purposes and policies).
Whether and to what extent a common law restitutionary action has survived the enactment of the U.C.C. depends, in large part, on which view of displacement is followed. It also depends, of course, on an analysis of the language of the relevant Code sections and under the expansive view, the underlying policies and purposes of the Code as it relates to check collections and recovery of mistaken payments. Inasmuch as the narrow view of displacement is followed by a majority of courts, the availability of common law restitution under that view will be addressed first.

**B. Restitution Within the Code Under the Narrow View of Displacement**

Neither article 3 nor article 4 expressly adopts or codifies quasi-contract principles as the general basis of recovery of mistaken payments. Instead, a warranty theory, which was the minority view in pre-Code law, is adopted as the basis for recovery under section 3-417\(^9\) and its counterpart in article 4, section 4-207.\(^ {92} \) These sections provide for certain warranties in the presentment of an item for payment or acceptance.\(^ {92} \) The types of mistaken payments that will trigger a breach of warranty and allow recovery of the payment are basically the same as those which, at common law, would allow recovery of the payment under quasi-contract principles.\(^ {94} \) Moreover, the exceptions to the warranty provisions are parallel to the common law as well. Of special significance is the fact that there is no warranty of

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91. U.C.C. § 3-417; see also 3 G. PALMER, supra note 17, at 283; Farnsworth, A General Survey of Article 3 and an Examination of Two Aspects of Codification, 44 Tex. L. Rev. 645, 654-55 (1966) [hereinafter Farnsworth, General Survey]; O'Malley, supra note 5, at 229-30, 262-63.

92. U.C.C. § 4-207; see also North Carolina Nat'l Bank v. Hammond, 298 N.C. 703, 707, 260 S.E.2d 617, 621-22 (1979); Rogers, supra note 55, at 956 (article 4 uses warranty of good title approach); Note, Allocation, supra note 5.

93. The basic warranties are that the presenter and all prior transferors: (1) have good title to the instrument, U.C.C. § 3-417(1)(a); (2) have no knowledge of a forged drawer’s or maker’s signature (with exceptions), id. § 3-417(1)(b); and (3) warrant that the item has not been materially altered, id. § 3-417(1)(c). The warranties set forth in § 4-207 are almost identical. See id. § 4-207(1)(a), (b), and (c). Note that under federal law warranties are also made with respect to items collected through the federal reserve system. Like the Code, such warranties are not dependent upon any express language on the item. 12 C.F.R. §§ 210.5(a)(2), 210.6(b)(i) (1989).


94. The statement in the text refers to the majority approach at common law which allowed recovery under quasi-contract principles in cases of forged indorsements and material alterations. See supra notes 54-55 and accompanying text. Like common law restitution, a warranty action under § 3-417 or § 4-207 is available to the negligent drawee. See Steinheimer, supra note 48, at 207-08; Note, Losses, supra note 45, at 460-62; supra note 50.
genuineness with respect to the drawer's signature. As a result there is no breach of warranty upon the presentment of an item with a forged drawer's signature. Thus, the principal exception to recovery of mistaken payments, which under *Price v. Neal* was an exception to recovery under quasi-contract, is preserved under articles 3 and 4 as an exception to the presentment warranty provisions. The comments to sections 3-417 and 4-207 make it clear that this result was intended by the drafters.

The predominance of warranty in the law governing the recovery of mistaken payments under the Code is unmistakable. The problem is one of ascertaining the effect of this warranty scheme on the survival of a quasi-contract theory of recovery. Although articles 3 and 4 have expressly adopted a warranty theory of recovering mistaken payments, they clearly have not expressly displaced the common law action for money had and received in a wholesale fashion. On the contrary, the comments to the Code make it clear that with respect to the payment of an item over a stop payment order, for example, the drafters intended to retain the common law action for money had and received under the Code, albeit in a modified form.

95. The presenter warrants that he or she has good title to the item, U.C.C. §§ 3-417(1)(a), 4-207(1)(a), but courts have uniformly held that this warranty is not breached by a forged drawer's signature. See, e.g., Bagby v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 491 F.2d 192, 199 (8th Cir. 1974); Sun 'n Sand v. United Cal. Bank, 21 Cal. 3d 671, 684-87, 582 P.2d 920, 929-32, 148 Cal. Rptr. 329, 339-40 (1978).

Under subsection (2) of both § 3-417 and § 4-207 (the so-called transfer warranties) the transferor warrants that all signatures are genuine; however, these warranties run only to transferees and thus will not provide a basis of recovery for the drawee/payor because it is not a transferee under the Code. An item is not transferred to the drawee/payor bank. Instead, it is presented for payment. Since there is no transfer, the drawee/payor is not a transferee. See, e.g., U.C.C. § 4-207 Official Comment 4; North Carolina Nat'l Bank, 298 N.C. at 706-07, 260 S.E.2d at 621.

96. See, e.g., Northern Trust Co. v. Chase Manhattan Bank, 582 F. Supp. 1380, 1386 (S.D.N.Y.), aff'd, 748 F.2d 803 (2d Cir. 1984); Fireman's Fund Ins. Co. v. Security Pac. Nat'l Bank, 85 Cal. App. 3d 797, 807, 149 Cal. Rptr. 883, 889 n.8 (1978). On the other hand, the presenter warrants that he or she has no knowledge of a forged drawer's signature. U.C.C. §§ 3-417(1)(b), 4-207(1)(b). As a result, presentment of an item knowing that the drawer's signature is forged generally will result in warranty liability. See O'Malley, supra note 5, at 206 n.98. Exceptions to liability were made in certain cases when the holder was a holder in due course who obtained acceptance without knowledge of the forgery. U.C.C. § 3-417(1)(a)(iii), 3-417 Official Comment 4.

97. "The warranties prescribed and exceptions thereto follow closely principles established at common law, particularly, those under Price v. Neal . . ." U.C.C. § 3-417 Official Comment 4. "[T]he warranties to payors are less inclusive because of exceptions reflecting the rule of Price v. Neal . . . and related principles." Id. § 4-207 Official Comment 4. These comments suggest that the drafters were unaware of the differences between warranty and restitution as theories of recovery. Although warranty applies to basically the same types of mistaken payments as restitution, it, in fact, does not "follow closely" restitutionary principles. See supra notes 81-83 and accompanying text. The adoption of a warranty theory in the U.C.C. has not been without criticism. See, e.g., Rogers, supra note 55, at 957, 956 n.84; Note, Doctrine, supra note 5, at 212.

98. The comments to § 4-403 state that in the event a bank pays an item over its customer's
In addition, a few sections in articles 3 and 4 contain ambiguous language which the courts have interpreted as impliedly incorporating, or at least retaining, the common law action in other specific situations. However, the implied or express retention of a restitutionary action in these situations does not necessarily mean that it was retained in other contexts, particularly that of recovering other types of mistaken payments by the payor bank.

Under section 1-103 the common law is retained unless it has been displaced, and whether it has been displaced depends, under the narrow view, on whether and to what extent it conflicts with the language of the other Code sections. The language of the relevant article 3 Code sections will be examined next.

1. Restitution Under Section 3-418

One of the key Code sections with respect to recovering mistaken payments is section 3-418. The language of the section makes no express reference to restitution or an action for money had and received. Thus, there is no express displacement or retention of them. The section provides, in part, that "payment or acceptance of any instrument is final in favor of a holder in due course, or a person who has in good faith changed his position in reliance on the payment." The phrase "payment is final" could be compatible with subsequent quasi-contract actions by the person who paid to recover a mistaken payment, or, on the other hand, it could mean that stop payment order, the bank "retains common-law rights, e.g., to recover money paid under mistake (Section 1-103) ...." U.C.C. § 4-403 Official Comment 8; see, e.g., Farmers & Merchants State Bank v. Western Bank, 841 F.2d 1433, 1438 (9th Cir. 1988). The comments to § 4-407 similarly provide that "[t]he spelling out of the affirmative rights of the bank in this section [in a case of paying an item over a stop payment order] does not destroy other existing rights (Section 1-103) .... [including] rights to recover money paid under a mistake." U.C.C. § 4-407 Official Comment 5; see also id. § 4-407 ("to prevent unjust enrichment"); Bryan, 628 S.W.2d at 761.

99. For example, § 4-212(5) provides that the failure of a bank to effect a charge-back against its customer "does not affect other rights of the bank against the customer or any other party." U.C.C. § 4-212(5) (emphasis added). Relying on this language, at least one court held that charge-back is not a collecting bank"s exclusive remedy against its customer, thereby allowing an action for money had and received. Great W. Bank & Trust, 138 Ariz. at 260, 674 P.2d at 323.

In addition, § 3-419(3) provides that a bank who has in good faith and in accordance with the reasonable commercial standards ... dealt with an instrument or its proceeds on behalf of one who was not the true owner is not liable in conversion or otherwise to the true owner beyond the amount of any proceeds remaining in his hands. U.C.C. § 3-419(3) (emphasis added). Relying on this language, some courts have held that the conversion action provided in § 3-419 did not displace the common law action for money had and received. See, e.g., Peerless Ins. Co. v. Texas Commerce Bank, 791 F.2d 1177 (5th Cir. 1986); Citizens State Bank v. National Sur. Corp., 199 Colo. 497, 612 P.2d 70 (1980) (en banc).

100. U.C.C. § 3-418.
such actions are barred. A review of pre-Code case law and the relevant commentary shows that under the dominant quasi-contract theory as well as under the minority warranty theory, the payment is final concept meant that subsequent recovery of the payment was barred. Under this interpretation, the final payment rule will displace common law restitution when the rule applies. It thus becomes necessary to consider the circumstances under which the final payment rule applies.

Under common law, the protection provided by this finality rule was not available to all defendants. It was not available to defendants who were not acting in good faith as well as to those who had not paid value for the item. By using the holder in due course concept in section 3-418, the Code has retained these two restrictions without significant change. Moreover, under common law, a defendant who had not paid value could nevertheless retain the payment if he could prove that he had changed his position in reliance on the payment, at least under the dominant quasi-contract theory. This defense has also been retained in section 3-418. One significant change with respect to the scope of protection under section 3-418 is in the effect of the defendant’s negligence on the finality of the payment. At common law the defendant’s negligence would typically preclude protection under the rule. Under the Code, the protection of the finality rule is not precluded by the defendant’s negligence unless the negligence amounts to a lack of good faith.

101. Comment 8 to § 4-303 states that a party “retains common law rights to recover money paid by mistake in cases where payment is not made final by 3-418.” U.C.C. § 4-303 Official Comment 8. This language shows that the drafters saw § 3-418 as cutting off common law restitutionary rights. This interpretation is widely held by courts. See, e.g., Morgan Guar. Trust Co., 804 F.2d at 1494-98 (discussing New York law); Northern Trust Co., 582 F. Supp. at 1385-86. But see Demos, 151 N.J. Super. 489, 376 A.2d 1352, 1355 (court appears to employ a more narrow view of “payment is final,” one allowing restitution under some circumstances). It is also supported by commentators. See, e.g., R. Hillman, J. McDonnell & S. Nickles, supra note 90, at ¶ 1.06[2][c]; Lawrence, supra note 45, at 142 (“may not be recovered by the payor, nor the acceptance avoided”); O’Malley, supra note 5, at 227-28; Note, Allocation, supra note 5, at 1086-87 (“final—not recoverable”; “irrevocable”).


103. See, e.g., Mid-Continent Nat’l Bank v. Bank of Independence, 523 S.W.2d 569 (Mo. Ct. App. 1975). Relatively few cases rest solely on the change of position defense. For an example of a case that does, see First Nat’l City Bank v. Altman, 3 U.C.C. Rep. Serv. (Callaghan) 815 (N.Y. Sup. Ct. 1966). For criticism of this decision, see, e.g., J. Winn & R. Summers, supra note 57, at 611-14; Comment, Broader Liability, supra note 5, at 826-28. For a discussion of the change of position concept under the common law, see supra notes 32-37 and accompanying text.

104. See U.C.C. § 3-418 Official Comment 4; Fireman’s Fund Ins. Co., 85 Cal. App. 3d
If these two restrictions were the only restrictions on the finality rule, it would represent a substantial expansion of the rule under the Code. This is because under pre-Code law, finality of payment was limited in the first instance to payment or acceptance of items containing forged drawer's signatures and those drawn on insufficient funds or no account. It did not bar recovery in cases of forged indorsements or material alterations. These limitations on the Code's finality rule are not expressed in the language of section 3-418; instead, they are preserved in the warranty provisions of section 3-417 which is incorporated by reference into section 3-418 as an exception to the operation of the rule. We have already seen that the warranty provisions of section 3-417 are tailored to allow recovery of basically the same types of mistaken payments as under the common law quasi-contract theory, while preserving principal exceptions to recovery. By incorporating these warranty provisions into section 3-418 as an express exception to the finality rule, the rule is limited to essentially the same types of mistaken payments under article 3 as it was under pre-Code law. The official comments to section 3-418 make it clear that the drafters intended the section to follow the rule in Price v. Neal. Moreover, both courts and commentators find that the section modifies or embodies the rule.

The finality rule in section 3-418 prohibits recovery of a mistaken payment, and this is obviously incompatible with the availability of a common law restitutionary action. It is clear then that with respect to those mistaken payments that are final under section 3-418, common law restitution is

at 823, 149 Cal. Rptr. at 901; Payroll Check Cashing v. New Palestine Bank, 401 N.E.2d 752, 759 (Ind. Ct. App. 1980); see also O'Malley, supra note 5, at 206; Steinheimer, supra note 48, at 208. Note, however, that the holder in due course concept under § 3-418 includes a requirement of good faith, U.C.C. § 3-302(1)(b), and good faith for a merchant includes an objective standard of adherence to reasonable commercial standards. Id. § 2-103(1)(b). Thus, a merchant's negligence will preclude protection of the finality rule under the Code as under common law. Note, Losses, supra note 45, at 465. For a discussion of negligence under the common law, see supra notes 29-31, 50 and accompanying text.

105. "[E]xcept for liability for breach of warranty on presentment under [§ 3-417] . . . ." U.C.C. § 3-418. For a discussion of the common law final payment rule, see supra notes 38-63 and accompanying text.

106. In other words, it imposes finality on the mistaken payment in cases of forged drawer's signature. It also imposes finality with the mistaken payment of insufficient funds and no account items.

107. U.C.C. § 3-418 Official Comment 1.

108. See, e.g., Morgan Guar. Trust Co., 804 F.2d at 1495 (discussing New York law); Fireman's Fund Ins. Co., 85 Cal. App. 3d at 822, 149 Cal. Rptr. at 900; Payroll Check Cashing, 401 N.E.2d at 755; Mid-Continent Nat'l Bank, 523 S.W.2d at 575; First City Bank, 675 S.W.2d at 319; 3 G. PALMER, supra note 17, at 290-91; Cooter & Rubin, A Theory of Loss Allocation for Consumer Payments, 66 Tex. L. Rev. 63, 105 (1987); Farnsworth, General Survey, supra note 91, at 654-55; Lawrence, supra note 45, at 132; O'Malley, supra note 5, at 201-06; Steinheimer, supra note 48, at 208.

The courts often ignore the real differences that exist between common law restitution and the Code warranty provisions. As a result, they are unaware of the problems these differences create in the Code scheme. See supra notes 81-83, 96-97 and accompanying text.
logically inconsistent and is therefore displaced. However, the operation of
the rule is severely limited by the section 3-417 warranty exception and by
the holder in due course and good faith reliance restrictions of section 3-
418. In cases where the rule is not available, common law restitution would
not, under the narrow view, be displaced—at least not unless it is displaced
by some other Code provision.

Under this approach, common law restitution survives, but only in those
situations where payment is not final under section 3-418. This will, as a
practical matter, limit the availability of a restitutionary action to certain
types of mistaken payment cases. In cases where an item containing a forged
indorsement or material alteration is paid, recovery of the payment is clearly
available under the section 3-417 statutory presentment warranty as an
express exception to the final payment rule. \textsuperscript{109} Availability of a warranty
action would render the restitutionary claim superfluous in most cases, but
restitution is not logically inconsistent with the warranty claim. Under the
narrow view, therefore, the restitutionary claim would not be displaced. \textsuperscript{110}
Instead, the two theories of recovery exist as alternative claims in these
types of mistaken payment cases. By comparison, no presentment warranty
is typically breached in a case involving a forged drawer's signature, or an
item drawn on insufficient funds or a closed account, \textsuperscript{111} but the final
payment rule under section 3-418 will displace a restitutionary action if the
recipient of the payment is a holder in due course of the item or changed
his position in good faith reliance on the payment. It is only when we have
payment of an item containing a forged drawer's signature or of an item

\textsuperscript{109} Professor Palmer takes the view that a warranty action “should not exclude the use
of quasi contract.” 3 G. PALMER, supra note 17, at 283. He suggests circumstances where
restitution may be preferable to warranty. \textsuperscript{111} With respect to insufficient funds items, see, e.g., Lowe's of Sanford, Inc. v. Mid-
South Bank & Trust Co., 44 N.C. App. 365, 260 S.E.2d 801 (1979). With respect to forged
signatures, see, e.g., Payroll Check Cashing, 401 N.E.2d at 757; see also O'Malley, supra note
5, at 193 n.30; Steinheimer, supra note 48, at 207; Note, Losses, supra note 45, at 457; Note, Allocation, supra note 5,
at 1081, 1087; Comment, Broader Liability, supra note 5, at 821.
drawn on insufficient funds or a closed account where the recipient is not a holder in due course or did not rely on the payment that a restitutionary action would be available as a sole cause of action. This is not, however, to suggest that such an action, if brought against the recipient of the payment, would be successful for the plaintiff. Recall that at common law, restitution was generally not available in cases where an insufficient funds item or no account item was paid by mistake.\textsuperscript{112}

The analysis of section 3-418 up to this point has focused on the degree to which it has displaced the common law action for money had and received. This focus is logical given that the starting point of the Code analysis was section 1-103. There is, however, another perspective on section 3-418 that should be considered. While most courts see the function of section 3-418 as imposing limits on recovering payments under restitution and not as a source of a right to recover a payment,\textsuperscript{113} there is authority for the view that section 3-418 embodies or creates a right to recover payments as well as sets forth restrictions on that right.\textsuperscript{114}

\begin{footnote}
112. See supra notes 51-53, 81 and accompanying text. Compare Central Bank & Trust Co. v. General Fin. Corp., 297 F.2d 126 (5th Cir. 1961) (restitution denied in case of mistaken payment of insufficient fund item) with Manufacturers Trust Co. v. Diamond, 17 Misc. 2d 909, 186 N.Y.S.2d 917 (N.Y. Sup. Ct. 1959) (restitution allowed with no account check unless change of position); see also Town & Country State Bank v. First State Bank, 358 N.W. 2d 387 (Minn. 1984) (court suggests that even if the payor could show that the defendant was not a holder in due course, it would still have to establish a right to restitution, e.g., based on fraud or mistake, and may not be able to do so); Demos, 151 N.J. Super. at 496, 500, 376 A.2d at 1355, 1357-58 (court characterizes this as a “waiver” of restitutionary rights).

113. See, e.g., Farmers & Merchants State Bank, 841 F.2d at 1438; Perini Corp., 553 F.2d at 416-17; Northern Trust Co., 582 F. Supp. at 1385-86; Town & Country State Bank, 358 N.W.2d at 394-95. For commentary supporting this view, see, e.g., Lawrence, supra note 45, at 142-43 (under both the Code and the N.I.L. payor’s right to recover must rest on common law restitution); O’Malley, supra note 5, at 201, 227-28; Comment, Broader Liability, supra note 5, at 834 n.129.

114. This view is typically based on two arguments. First, the official comment to § 3-418 states that the section is intended to follow “the rule of Price v. Neal.” U.C.C. § 3-418 Official Comment 1. That case was a restitution case and, therefore, by codifying the “rule” of the case, the section creates a right of restitution or recovery. The problem with this argument is that the language found in that comment is ambiguous. The rule of Price v. Neal is one of precluding recovery, or put another way, one of making payment final in certain circumstances. It is questionable to argue that codifying a rule making certain payments final entails a rule allowing recovery of payments. Moreover, the result of Price v. Neal, which was nonrecovery of a mistaken payment, is compatible with a warranty theory of recovery as was seen under the minority approach at common law and under the N.I.L. After all, the official comments to § 3-417 contain a nearly identical statement that the section—entailing a system of warranty recovery—follows the rule in Price v. Neal. Id. § 3-417 Official Comment 4.

Second, the view that § 3-418 creates a right to recover some mistaken payments is also supported by a negative inference drawn from the language of the section. The section provides that “payment is final” in certain circumstances. This implies that payment is not final, i.e. can be recovered, in those circumstances not covered by the rule. This argument is plausible when § 3-418 is looked at in isolation; however, to suggest that a restitutionary right is implied in the language of the section clearly overlooks the express mandate of § 1-103 that the common law of mistake is to supplement the provisions of the Code. Moreover, the inference
\end{footnote}
The significance of the distinction between these two views of the function of section 3-418, one of creating a limited right to recover mistaken payments and the other of selectively displacing common law restitution, is made apparent when one asks whether a payor bank can obtain restitution of a payment under the Code under circumstances where restitution would be denied at common law. This is the key issue in any case where a bank mistakenly pays an insufficient fund or no account item and the recipient of the money is not a holder in due course and did not change his position in reliance on the payment. If we consider section 3-418 as the source of restitutionary rights, then restitution should be available. Even though typically no warranty is breached with insufficient fund or no account items, payment is not final under section 3-418 and a right of recovery is inferred. If, on the other hand, we consider section 3-418 as merely selectively displacing common law restitution, then restitution will generally not be available because it was generally not available at common law. The results, however, under this latter approach will differ depending on what state law is applied in the case because the common law rule was not uniform.

The analysis up to this point has proceeded from the narrow view of displacement under section 1-103, focusing on the extent to which article 3 displaces common law restitution. Displacement here depends on whether a restitutionary action would be inconsistent with the language of the article 3 sections. The next step is to consider those Code sections dealing with "recovery of bank payments," the other express exception to the final payment rule under section 3-418. The next section of this Article will consider the provisions of article 4 related to the recovery of bank payments and analyze their impact on common law restitution.

under § 3-418 that payments can be recovered under certain circumstances is at least equally compatible with a warranty theory which is the predominant theory of recovering payments in both article 3 and article 4. For an example of a court that views § 3-418 as both embodying a right to recover payments and setting forth restrictions on that right, see Blake v. Woodford Bank & Trust, 555 S.W.2d 589, 601-02 (Ky. Ct. App. 1977).

115. For an example of a court's reliance on common law restitution under state law, see National Sav. & Trust Co. v. Park Corp., 722 F.2d 1303 (6th Cir. 1983), cert. denied, 466 U.S. 939 (1984); see also Comment, Broader Liability, supra note 5; cf. Demos, 151 N.J. Super. at 500-01, 376 A.2d at 1357-58.

In saying that common law restitution was generally not available in insufficient funds and closed account cases one must distinguish between two possible reasons for that result. One could be a simple extension of Price v. Neal with its supporting rationale, but, if so, the restrictions on Price v. Neal would go along as well, namely, requiring good faith payment of value or good faith change of position. On the other hand, the result of non-recovery could be based on the theory that in insufficient funds cases and no account cases there is no mistake sufficient to justify restitution. This makes the issues of good faith, value, and change of position irrelevant. As a result, the consideration of common law restitution needs to account for this distinction, especially if we consider § 3-418 as a source of recovery rather than merely restricting common law restitution.
2. Restitution Under Article 4 Sections

In examining article 4 to determine if common law restitution has been displaced by the U.C.C., two sections deserve particular attention: section 4-213 and section 4-302. Subsection (1) of section 4-213 describes the ways in which final payment may occur. The two most significant ways specified are payment of the item either in cash or by posting, and failure to revoke the provisional credits before the midnight deadline. Subsection (1) further provides that when final payment occurs through posting or by failure to revoke provisional credits, the payor bank shall be accountable for the amount of the item.116 Section 4-302 also specifies bank accountability.117 It provides, in part, that except for where there is a breach of a presentment warranty, "or the like," the payor bank is "accountable" for the amount of any item it retains beyond the midnight deadline without paying the item or dishonoring it.118 Accountability is broader in scope under section 4-302 than under section 4-213 because section 4-302 provides that the payor bank which retains the item is accountable regardless of whether or not the item is properly payable.119 Neither section defines the meaning of the term "accountable." According to comment 7 to section 4-213, accountability imposes upon the payor "a duty to account, which duty is met if and when a settlement for the item satisfactorily clears."120 This definition does not adequately describe the exact nature of this duty to account. In spite of this ambiguity under the Code, there has been a high degree of uniformity in the courts' interpretation of this term. Beginning with the Rock Island Auction Sales, Inc. v. Empire Packing Co.121 case in 1965, courts have interpreted the term "accountable" as synonymous with liable and have held the payor to a strict standard of

116. U.C.C. § 4-213(1).
117. The redundant treatment of this subject is curious. No differences can be discerned between the two sections. Professor Leary asserts that the clause should not have been included in § 4-213 since it provides a penalty for nonaction and should have more appropriately been included in §§ 4-301 and 4-302. Leary, A Proposal for the Automation of Returns of Cash Items, 19 U.C.C. L.J. 47, 52 (1986).
118. U.C.C. § 4-302 (emphasis added). Section 4-302 specifies payor bank accountability where the bank has failed to act within specified time limits. This failure is sometimes referred to as "undue retention" or "delayed return." For a historical treatment of the undue retention doctrine, see Blake, 555 S.W.2d at 589. See generally Note, Retention of a Check: Payor Bank's Liability Under Section 4-302, 10 B.C. INDUS. & COM. L. REV. 116 (1968) [hereinafter Note, Retention of a Check].
119. U.C.C. § 4-302(a). The payor bank is, in addition, liable for the face amount of the item rather than for any actual damages which resulted from the payor bank's inaction. Rock Island Auction Sales, Inc. v. Empire Packing Co., 32 Ill. 2d 269, 204 N.E.2d 721 (1965); Note, Retention of a Check, supra note 118, at 117. For cases equating the term accountable with liable, see infra note 122 and accompanying text.
120. U.C.C. § 4-213 Official Comment 7.
121. 32 Ill. 2d at 269, 204 N.E.2d at 721.
liability for retaining the item past the midnight deadline.\textsuperscript{122} The practical effect of accountability is, however, unclear. Inasmuch as the "accountable" language under both sections applies only to noncash final payments, it has been suggested that the term merely imposes an affirmative duty on the payor bank to disburse money for the item.\textsuperscript{123} Comment 7 to section 4-213 suggests that accountability is designed, at least in part, to put noncash final payment, such as that which occurs through undue retention, on a par with cash final payment. This is consistent with the interpretation of accountability as merely requiring disbursement. This interpretation does not, however, address the question of the payor's common law right to restitution following mistaken payment.\textsuperscript{124}

\textsuperscript{122} For cases equating the term accountable with liable, see, e.g., Houston Contracting Co. v. Chase Manhattan Bank, 539 F. Supp. 247 (S.D.N.Y. 1982); Universal C.I.T. Credit Corp. v. Farmers Bank, 358 F. Supp. 317 (E.D. Mo. 1973); Farmers Coop. Livestock Mkt., Inc. v. Second Nat'l Bank, 427 S.W.2d 247 (Ky. 1968); Sun River Cattle Co. v. Miners Bank, 164 Mont. 237, 521 P.2d 679 (1974); Berman v. United States Nat'l Bank, 197 Neb. 268, 249 N.W.2d 187 (1976). Often courts fail to define the term accountable, holding only that the payor is accountable for the face amount of the item. Such courts, by implication, interpret the term accountable as meaning liable. See, e.g., Ashford Bank v. Capital Preservation Fund, Inc., 544 F. Supp. 26 (D. Mont. 1982); Bank of Wyandotte v. Woodrow, 394 F. Supp. 550 (W.D. Mo. 1975); Capital City First Nat'l Bank v. Lewis State Bank, 341 So. 2d 1025 (Fla. Dist. Ct. App. 1977); Reynolds-Wilson Lumber Co. v. Peoples Nat'l Bank, 699 P.2d 146 (Okla. 1985). It should be noted that in the cases cited above, the holding pertains to the accountable language found in § 4-302. No reported case was found interpreting the term accountable in § 4-213. This could be explained if the role § 4-213 plays in the statutory scheme is to describe when final payment occurs rather than to explain its consequences. See infra notes 143-46 and accompanying text.

\textsuperscript{123} Note, \textit{Commercial Code—Articles 3 and 4—Bank Required to Disburse Funds After Final Payment}, 64 MARQ. L. REV. 408, 411 (1980).

\textsuperscript{124} It is unclear whether the strict liability imposed works only to deny defenses in a suit against the payor bank to account for the amount of the item, or whether it would also deny relief by the bank in a suit to recover the funds once disbursed. In by far the majority of cases equating the term accountable with liable, this question arose in a suit to account against the payor bank. See, e.g., Catalina Yachts v. Old Colony Bank & Trust Co., 497 F. Supp. 1227 (D. Mass. 1980); National City Bank v. Motor Contract Co., 119 Ga. App. 208, 166 S.E.2d 742 (1969); Available Iron & Metal Co. v. First Nat'l Bank, 56 Ill. App. 3d 516, 371 N.E.2d 1032 (1977); Templeton v. First Nat'l Bank, 47 Ill. App. 3d 443, 362 N.E.2d 33 (1977); Kane v. American Nat'l Bank & Trust Co., 21 Ill. App. 3d 1046, 316 N.E.2d 177 (1974). The issue of restitution was not discussed in the above cases. This could be true, of course, for a variety of reasons. It might not have been raised by the payor bank; circumstances might not have existed justifying restitution; it could have been raised but rejected by the court without discussion. Alternatively, this might be seen as support for the argument that § 4-302 imposes a strict duty to disburse funds regardless of the equities involved. See infra notes 128-40 and accompanying text where this argument is advanced in more detail.

Similarly, most cases in which restitution was discussed was arose where funds had already been disbursed. See, e.g., Peerless Ins. Co., 791 F.2d at 1177; Ashford Bank, 544 F. Supp. at 26; Bank Leumi Trust Co., 528 F. Supp. at 349; Maplewood Bank & Trust Co., 142 N.J. Super. at 434, 262 A.2d at 44; First Nat'l City Bank, 3 U.C.C. Rep. Serv. at 815. In these cases the payor bank was suing to recover the money paid by mistake, with court attention focusing upon § 3-418. This could support the view that article 4 requires disbursement of funds, while article 3 determines restitutionary rights. See infra notes 143-46 and accompanying text where this view is discussed.
The relationship between final payment in article 3 and accountability in article 4 is unclear. If the accountable language found in article 4 merely requires the payor bank to disburse funds, to, in effect, put itself in the same position as if it had paid the item in cash, no restrictions on common law restitutionary rights would be created. The payor bank under article 4 would possess whatever restitutionary rights a drawee bank had under article 3. Recall that section 3-418 provides for final payment, but with the significant restrictions of holder in due course and good faith reliance. If, on the other hand, the accountable language operates to prohibit restitution once final payment under section 4-213 has occurred, it would appear to entail an absolute prohibition on restitution because the restrictions found in section 3-418 are not found in either section 4-213 or section 4-302. In other words, neither section 4-213 nor section 4-302 specifies that the payor is accountable only to a holder in due course or to a party who changed his position in reliance on the payment. Each, thus, appears to provide for final payment, but with virtually no restrictions. If the accountable language in section 4-213 and section 4-302 establishes a final payment rule, it is in marked contrast with that of section 3-418.

The problem can be illustrated by examining it in the context of a situation where the payor bank pays an instrument containing a forged drawer's signature. The key issue in such an instance is the availability of restitution. It is here that the apparent conflict between the language of section 3-418 and the article 4 sections comes into focus. Under section 3-418, in addition, it does not except the breach of warranty situation. Whether this was based on drafter oversight or was intentional is unclear. Commentators seem in agreement that breach of warranty offers relief to the payor bank even if final payment has occurred under § 4-213. See e.g., Griffith, *Final Payment and Warranties on Presentment Under the Commercial Code—Some Aspects*, 23 Drake L. Rev. 34, 35, 37 (1973); Note, Allocation, *supra* note 5, at 1089 n.78.


Recall that the question of restitution arises most frequently in the forged drawer's signature or insufficient funds situation. Where the payor has paid over a forged indorsement, a breach of warranty claim would more easily enable the payor to recover the payment. See supra notes 91-98 and accompanying text. In a forged drawer's signature case, the payor bank is typically unable to assert a breach of warranty claim. See supra notes 95-97, 107-08 and accompanying text.
418, payment of an item with a forged drawer's signature is final in favor of a holder in due course or someone who relied in good faith on the payment. As a result, the payor's or drawee's restitutionary rights are limited to cases where there is no holder in due course or good faith reliance. The conflict arises when one attempts to apply the accountable language from article 4. The language of sections 4-213 and 4-302 purport to make the payor accountable and do not limit accountability to cases where there is a holder in due course or good faith reliance. The problem arises when the party making presentment of an item on which the drawer's signature was forged is not a holder in due course and cannot show good faith reliance. Restitution might be available to the drawee under article 3, but restitution would be barred under article 4 unless the holder in due course and good faith reliance restrictions from section 3-418 are read into article 4.

There are three alternative interpretations which have been offered to resolve the apparent conflict between Code sections. It is useful to examine and evaluate each proposed construction.

a. Article 4 Prevails

Advocates of the first approach assert that the language, "except for recovery of bank payments" found in section 3-418, recognizes that article 4 provides different rules with respect to final payment. Further, in the case of a conflict between articles, article 4 prevails when the case involves check collection.\textsuperscript{128} Under this approach, once a check has entered the check collection system, all restitutionary rights would be cut off. Finality of payment would not be limited to a holder in due course or good faith reliance because these section 3-418 limitations would not be read into article 4. The only restriction that would be incorporated into the operation of article 4 would be a requirement of good faith on the part of the presenting party and prior transferors.\textsuperscript{129}

This view has support from courts and commentators.\textsuperscript{130} In addition, the drafting history of the Code, including an examination of prior statutes and

\textsuperscript{128} U.C.C. § 4-102.

\textsuperscript{129} Although there is no provision excepting bad faith presenters from the protections of article 4, there is near unanimous agreement that payment made to one acting in bad faith is not final. \textsuperscript{Id.} § 3-418 comment 3; see, e.g., \textit{Perini Corp.}, 553 F.2d at 398; \textit{Bartlett}, 218 Va. at 247, 237 S.E.2d at 115; First Wyoming Bank v. Cabinet Craft Distrubs., Inc., 624 P.2d 227 (Wyo. 1981).

\textsuperscript{130} See, e.g., \textit{Ashford Bank}, 544 F. Supp. at 26; \textit{Kirby v. First & Merchants Nat'l Bank}, 210 Va. 88, 168 S.E.2d 273 (1969); B. \textit{CLARK}, supra note 126, § 6.2[1], at 6-7; J. \textit{WHITE & R. SUMMERS}, supra note 57, § 16-2, at 617-18. There is, however, evidence that in the next edition of the White and Summers treatise the authors will change their position on this issue. \textit{See D. EPSTEIN & J. MARTIN, BASIC COMMERCIAL CODE 514 (2d ed. 1983).} Here is found the
commentary at the time of enactment, supports this position. While admit-
ning that "no good reason is apparent for the fundamental differences" be-
tween section 3-418 on the one hand and section 4-213 on the other, Pro-
fessors White and Summers cite the New York Law Revision Commission
Report as support for their view that:

It appears . . . that the very difference with which we are concerned
was pointed out to the draftsmen in 1954. They answered that the
difference was intended and that those who could not claim the protec-
tion of 3-418, because they had not changed their position in reliance
or because they were not holders in due course, might nevertheless claim
the protection of 4-302 and 4-213.\textsuperscript{131}

The rationale for this distinction can, to some extent, be uncovered by an
examination of pre-Code statute and practice. Prior to World War II, payor
banks customarily processed items, as they were received, before two or
three o'clock in the afternoon of the day of presentment.\textsuperscript{132} Wartime
personnel shortages led to the practice of deferred posting.\textsuperscript{133} This practice,
however, imposed risks upon the payor bank. Under the provisions of the
N.I.L., the drawee bank had only twenty-four hours within which to decide
whether or not to honor a check.\textsuperscript{134} If the drawee failed to return a check
within the time period specified, it was deemed to have accepted the item.\textsuperscript{135}
Despite this potential liability, the practice of deferred posting became
increasingly popular. Several pre-Code statutes authorizing deferred posting

\textsuperscript{131} J. \textsc{White} & R. \textsc{Summers}, \textit{supra} note 57, § 16-2, at 615-16 n.22 (citing 2 \textsc{N.Y. State
Law Revision Comm'n}, 1955 Report 1075 (1955)); \textit{see also id.} § 16-2, at 614 & n.17 (citing
\textsc{U.C.C.}, 1953 Official Draft of Text and Comments 142-43 (Supp. No. 1, 1955)).

\textsuperscript{132} \textsc{Leary}, \textit{Deferred Posting and Delayed Returns—The Current Check Collection
Problem}, 62 \textsc{Harv. L. Rev.} 905, 915-16 (1949) [hereinafter \textsc{Leary, Deferred Posting}]. This practice is
referred to as dribble posting. \textsc{Id.} at 916.

\textsuperscript{133} \textsc{Deferred posting refers to the practice of sorting and proving items on the day that}
they are received but not posting the item until the day following the day of presentment.
\textsc{U.C.C.} § 4-301 Official Comment 1. For a discussion of this process, see \textsc{Leary, Deferred
Posting, supra} note 132, at 917.

\textsuperscript{134} \textsc{N.I.L.} § 136; \textit{see also} \textsc{Leary, Deferred Posting, supra} note 132, at 918; \textsc{Note, Retention
of a Check, supra} note 118, at 119.

\textsuperscript{135} \textsc{Central Bank} \& \textsc{Trust Co.}, 297 F.2d at 126 (liability for delayed retention); \textsc{College
Station State Bank v. Fulcher}, 296 S.W.2d 953 (Tex. Civ. App. 1956); \textsc{Note, Retention of a
Check, supra} note 118, at 119-20. Moreover, the majority rule was that mere retention
constituted implied refusal to return the item for which the drawee would be liable as an
acceptor. \textsc{Leary, Deferred Posting, supra} note 132, at 918-19; \textsc{Note, Retention of a Check,
supra} note 118, at 120; \textit{see, e.g.}, \textsc{State Bank v. Weiss}, 46 Misc. 93, 91 \textsc{N.Y.S.} 276 (1904);
\textsc{Wisner v. First Nat'l Bank}, 220 Pa. 21, 68 \textsc{A.} 955 (1908). The rule was later abrogated by
statute in Pennsylvania. \textsc{Leary, Deferred Posting, supra} note 132, at 918. \textsc{Contra} \textsc{Womack v.
Durrett}, 24 S.W.2d 463 (Tex. Civ. App. 1930) (§ 137 only applicable where the item was
presented for acceptance not payment).
were promulgated to diminish the risks to payor banks of deferred posting; none was widely enacted.\(^{136}\) The Code provided a compromise solution. In exchange for codification of deferred posting practices, the Code provided a penalty\(^{137}\) for delay, namely, accountability. A primary goal of article 4, to insure speedy bulk processing of items,\(^{138}\) was furthered by the accountability requirement.\(^{139}\) Accountability under this interpretation would entail strict liability with no restitution possible.\(^{140}\)

In spite of its initial attractiveness, this alternative has several flaws. First, it would elevate section 4-213 (and section 4-302) over section 3-418 in importance since most disputes over forgeries and insufficient funds checks arise within the check collection system. Section 3-418 would be relegated to cases involving promissory notes and drafts collected outside the bank collection system. Court decisions have certainly not supported this interpretation. In fact, in the instance of forged drawer's signatures, for example, courts have typically ignored the conflict between section 3-418 and article

\(^{136}\) The Bank Collection Code, supported by the American Bankers Association, was one of the most widely adopted, with passage in 19 states. Leary, *Deferred Posting, supra* note 132, at 919 n.23; Leary & Schmitt, *Some Bad News and Some Good News from Articles Three and Four*, 43 Ohio St. L.J. 611, 617 (1982). In 1948 the American Bankers Association drafted the Model Deferred Posting Statute as an amendment to the Bank Collection Code. The Model Deferred Posting Statute, a forerunner to *U.C.C.* § 4-302, gave payor banks until midnight of the banking day following presentment of the item within which to act. This was adopted in few states. *Id.* at 121-22. For a discussion of various pre-Code legislative solutions, see generally Leary, *Deferred Posting, supra* note 132, at 926-28.

\(^{137}\) Leary & Schmitt, *supra* note 136, at 623; see also Leary, *Deferred Posting, supra* note 132, at 929 (describing accountability as the "sanction compelling decision"). Professor Leary states that contrary to the theory of pre-Code statutes, "the theory of the Code is that payment by the payor bank has been made, but can be recovered." *Id.* at 930; see also *supra* notes 155-66 and accompanying text. The compromise was accepted by the bankers and the Federal Reserve. For a description of the compromise, see Leary & Schmitt, *supra* note 136, at 623; Leary & Tarlow, *Reflections on Articles 3 and 4 for a Review Committee*, 48 Temp. L.Q. 919, 941 n.46 (1975).

\(^{138}\) Starcraft Co. v. C.J. Heck Co., 748 F.2d 982, 986 (5th Cir. 1984); Chrysler Credit Corp. v. First Nat'l Bank & Trust Co., 582 F. Supp. 1436, 1438 (W.D. Pa.), aff'd, 746 F.2d 200 (3d Cir. 1984).

\(^{139}\) To the extent that finality is an underlying policy consideration in article 4, it has been argued that accountability requires strict liability. *Starcraft Co.*, 748 F.2d at 986; *Town & Country State Bank*, 358 N.W.2d at 395; B. Clark, *supra* note 126, § 3.6[3], at 3-40; J. White & R. Summers, *supra* note 57, § 1, at 3; Note, *Mistaken Payment, supra* note 126, at 1094.

\(^{140}\) See e.g., B. Clark, *supra* note 126, § 6.2[1], at 6-7; J. White & R. Summers, *supra* note 57, § 16.2, at 613-18. Professor White explains:

> [M]y sources among the drafters of Article 4 tell me that the "accountable" language in 4-302 was intended to cut off any restitutionary claim that a tardy bank might have. He tells me that section 4-302 is the banker's concession made in return for the right to hold a check for a day and a half before final payment has occurred (in contrast to pre-Code shorter deadlines.) It was understood that if a banker held a check (without "paying" or "returning" it) beyond the midnight deadline, that check could not be sent back even if it was NSF and even if the party receiving it did not qualify under 3-418.

4 and have applied section 3-418 even where the check is clearly in the check collection system. 141

Second, while this alternative can be justified by reference to pre-Code law and by viewing the Code as a compromise (imposing strict liability under article 4 in exchange for a longer period of time within which to post items), imposition of strict liability is not justified in cases where the bank paid the item by actually disbursing the funds. Recall that where final payment has been effected by paying cash for the item, the payor bank is not accountable for the item under the language of sections 4-213 and 4-302. Whether or not restitution would be available in such a situation is not considered under this approach. Similarly, where final payment has occurred by posting the item, the payor bank is also accountable; however, strict liability, which is imposed to penalize the dilatory bank in cases of undue retention, is uncalled for in that instance.

Third, article 4 is itself inconsistent in its approach. For example, while section 4-213 makes no exception to accountability even for breach of warranty, section 4-302 expressly excepts breach of warranty. This alternative does not accommodate these differences.

Last, neither section 4-213 nor section 4-302 limits applicability of the accountability provisions by a requirement of good faith on the part of the presenting party or prior transferor. Although article 4 nowhere specifies lack of good faith as a defense to accountability, there is nearly uniform consensus that where the payee receives payment in bad faith, the payor bank should be permitted to recover its payment. 142

b. Section 4-213 Specifies Only the Time and Not the Effect of Final Payment

The second alternative for resolving the apparent conflict between the Code sections is to offer an alternative construction of section 4-213. Under this interpretation, section 4-213 is viewed as establishing rules for determining when final payment occurs, rather than governing the legal consequences of final payment. 143 The legal consequences of final payment would

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142. See supra note 129 and accompanying text; see, e.g., J. White & R. Summers, supra note 57, § 16-2, at 613-18.

143. Under this construction, § 4-213 is thought to refer primarily to the timing of final payment. Note, Allocation, supra note 5, at 1088 n.75. The use of the term "final" in U.C.C. § 4-213 is thought only to distinguish final from provisional payments. Final payment under
be governed by section 3-418 and the common law as applied through section 1-103. Under this construction, the accountability language of section 4-213 would put noncash payments on a par with cash payment by requiring that the payor disburse money for all items on which noncash final payment was made. It would, however, have no effect on the payor's right to restitution when such final payment was made by mistake. Payment of a check would be final, even under article 4, only in favor of a holder in due course or other party who in good faith relied on the payment.

This interpretation is supported in part by reference to some Code official comments. Comment 5 to section 3-418 refers to final payment "as defined in section 4-213." Comment 3 to section 4-213 describes the section as "fixing the point of time" at which final payment occurs. Support for this alternative can also be found in both court opinion and commentary. Unlike the first alternative, which renders section 3-418 applicable only where the item has not entered the check collection process, the second alternative gives effect to both section 3-418 and section 4-213.

There are, on the other hand, major problems with this alternative interpretation that cannot be ignored. It is based upon a construction of the purposes of sections 3-418 and 4-213; however, it ignores entirely section 4-302. The language and operation of sections 3-418 and 4-213 must be compared with that of section 4-302, as interpreted by the courts. Recall that section 4-302 provides that the payor bank is accountable for the amount of any item it retains beyond the midnight deadline without paying the item or dishonoring it. The term accountable here has been widely interpreted to impose strict liability upon the payor bank. The only defenses recognized to this strict liability under section 4-302 are breach of warranty and lack of good faith. While the time limits under section 4-302 may be extended under the operation of section 4-108, that excuse section has been construed very narrowly. The key question in construction of section 4-

§ 3-418, on the other hand, "deprives a drawee who has finally paid off a cause of action for the recovery of payment except as provided by the Code for breach of presentment warranty." Finan, supra note 126, at 28. The author continues:

If payment is final under both sections, no recovery may be had by a bank except as specifically provided by the Code. If payment is final only under § 4-213(1) however, resort may be had not only to the breach of warranty provisions of the Code, but also to supplementary principles of law and equity.

Id. at 28-29 (footnote omitted); see also Griffith, supra note 125, at 34.

144. U.C.C. § 3-418 Official Comment 5 (1977) (emphasis added).
145. Id. § 4-213 Official Comment 3.
146. See, e.g., Park, 722 F.2d at 1303; Blake, 555 S.W.2d at 589; R. Braucher & R. Riegert, supra note 8, at 128-29; Comment, Broader Liability, supra note 5, at 828-37.
147. Most commentators who have considered this conflict have, likewise, ignored § 4-302. See, e.g., Hill, supra note 126; Note, Easy Come, Easy Go, supra note 126; Comment, Broader Liability, supra note 5.
148. See, e.g., Bank Leumi Trust Co., 499 F. Supp. at 1022 (error in encoding computer
302 is whether a payor bank who by mistake retained an item beyond the midnight deadline is entitled to restitution. Courts attaching strict liability to the payor under section 4-302 have not limited this liability to cases where the presenting party or prior transferor was a holder in due course or showed good faith reliance.149 In fact, few undue retention cases even mention a restitution claim.150 Even in those cases in which restitution is discussed, nearly all courts refuse to allow it.151

If section 4-302 provides an absolute rule of liability subject only to the limited number of defenses discussed, this creates a conflict with both section 4-213 and section 3-418. In addition to accountability under section 4-302, the payor bank is accountable under section 4-213 when final payment has occurred through any of the noncash methods. If these terms are construed consistently so that the strict liability rule of section 4-302 is applied in section 4-213, the result is a major conflict between section 4-
213 and section 3-418.\textsuperscript{152} If, on the other hand, the alternative construction of section 4-213 is accepted so that section 4-213 is construed consistently with section 3-418 and the restrictions under section 3-418 apply in the article 4 context,\textsuperscript{153} the term "accountable" in section 4-213 will mean something different than it means in section 4-302. In other words, "accountable" in section 4-213 would accommodate restitution when the presenting party was neither a holder in due course, nor changed his position in reliance on the payment, while "accountable" in section 4-302 would not. In addition to attaching two different meanings to the same term, this would result in the availability of restitution by the payor bank being dependent upon the way in which final payment occurred.\textsuperscript{154} When final payment was made by undue retention, the absolute liability of section 4-302 would be imposed; when final payment occurred by other means, restitution would be allowed. Under this view, a payor bank, uncertain as to the proper course of action with respect to a check, would be advised to pay the check, thereby preserving the possibility of subsequent restitution. The alternative of dishonoring the item or holding it past the applicable deadline while deciding whether to pay it would create risks of liability to the customer-drawer for wrongful dishonor,\textsuperscript{155} or to the presenting party for undue retention.

c. Section 4-302 Provides for Restitution

There is a third alternative interpretation of the Code sections at issue that should be considered. This alternative is a variation of the second alternative just discussed. As in the second alternative, section 4-213 is read as providing when final payment occurs. The use of the word "final" in section 4-213 distinguishes payment made under the provisions of section 4-213 from provisional settlement. The use of the term "accountable" in

\textsuperscript{152} For a discussion of this conflict, see supra notes 125-26 and accompanying text. Under this construction, the restrictions found in § 3-418 apply only in an article 3 situation, and do not apply under § 4-213 or § 4-302. For cases refusing to read the § 3-418 restrictions into article 4, see, e.g., Ashford Bank, 544 F. Supp. at 26-27; Kirby v. First & Merchants Nat'l Bank, 210 Va. 88, 168 S.E.2d 273 (1969); Northwestern Nat'l Ins. Co., 96 Wis. 2d at 155, 292 N.W.2d at 591.

\textsuperscript{153} For cases holding that the § 3-418 restrictions should be read into § 4-213, see, e.g., Park, 722 F.2d at 1303; Demos, 151 N.J. Super. at 489, 376 A.2d at 1352.

\textsuperscript{154} Courts appear to be applying this double standard presently without articulating the method of payment as a determinative factor. Most of the cases in which a payor bank has successfully raised the issue of restitution are cases in which the item was paid rather than retained. See, e.g., Park, 722 F.2d at 1303; Ashford Bank, 544 F. Supp. at 26; First Nat'l City Bank, 3 U.C.C. Rep. Serv. (Callaghan) at 815; Manufacturers Trust Co., 17 Misc. 2d at 909, 186 N.Y.S.2d at 917; Valley Bank, 74 Misc. 2d at 195, 343 N.Y.S.2d at 191.

\textsuperscript{155} If the dishonor was wrongful, the payor bank could face liability to the customer for wrongful dishonor under § 4-402. See generally Dow, Damages and Proof in Cases of Wrongful Dishonor: The Unsettled Issues Under U.C.C. Section 4-402, 63 WASH. U.L.Q. 237 (1985).
section 4-213 merely puts noncash payments on the same footing as cash payments. Where payment has become final under any of the noncash methods of final payment, the payor has a duty to remit cash. The payor has a duty to, in effect, put himself in the position that he would have been in had payment been made in cash. Accountability would have no effect upon the payor's rights to recover payments made by mistake.

In order to determine the effects of final payment, one looks to section 3-418 which allows restitution except against a holder in due course or one who in good faith changed his position in reliance upon the payment. This construction has support from courts and commentators, as discussed above. More importantly, each section is construed as an important component of the Code, playing a useful role in determining the rights and liabilities of the parties. The function of section 3-418 would be to limit the restitutonary rights of the parties. While one objection to this approach might be the language "[e]xcept for recovery of bank payments" in section 3-418, it is argued that this clause applies only to the situation where the payor bank was not accountable under section 4-213.

The next step in the analysis is to question the role that section 4-302 plays in this construction. Under this third alternative, the accountability provision of section 4-302, in effect, mirrors the accountability provision of section 4-213. Section 4-302 provides, accordingly, that the payor bank which retains an item beyond the time limits specified without dishonoring it, incurs the same liability as a payor bank that pays the item. The term "accountability" is given the same interpretation under section 4-213 and section 4-302. Under either section a payor bank which is accountable for the item has a duty to account—to disburse funds for the item. Whether or not the payor bank might be able to recover upon restitutonary principles the funds disbursed is not dealt with in either article 4 section 1. That issue is governed by section 3-418.

One major objection to this approach, discussed above, was the fact that, for more than twenty years, courts have interpreted the accountability

156. See generally Finan, supra note 126; Note, Allocation, supra note 5; Comment, Broader Liability, supra note 5.

157. One interpretation of this clause has been to exclude § 3-418 from applicability in all cases of bank collections. See supra notes 128-40 and accompanying text. Under this interpretation, § 3-418 applies only where the funds have been disbursed. Edwards, supra note 126, at 351.

158. Professor Leary states: "Thus, Section 4-302 must be interpreted as saying that the effect of a late return falling in either of the two categories referred to in the section is just as if the item had been finally paid, and case law is in agreement." Leary & Tarlow, supra note 137, at 937 (footnote omitted) (citing Rock Island Auction Sales v. Empire Packing Co., 32 Ill. 2d 269, 204 N.E.2d 721 (1965)).

159. Professor Leary asserts that such defenses would be available in a common law action for an accounting and, therefore, should be available under article 4. See Leary, Reflections of a Drafter, 43 Ohio St. L.J. 557, 563 (1982); Leary & Schmitt, supra note 136, at 622.
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provision of section 4-302 as imposing a form of absolute liability. If the term accountability in section 4-213 was interpreted to allow restitution (by reference to section 3-418) and the same term in section 4-302 does not allow restitution (absolute liability), the absurd result discussed above would be reached. First, the same term "accountability" would be given one interpretation in one section and a different interpretation in the other section. Second, the situation might result where the payor bank's restitutionary rights were solely dependent upon the manner in which final payment occurred. Where final payment occurred by paying out funds, restitution might be allowed, but where final payment occurred by undue retention, no restitution would be permitted.

Bank accountability should create the same rights and obligations under both Code sections. This result can be reached by a literal reading of section 4-302 which expressly allows for defenses to the absolute liability commonly imposed by the courts. The section begins with an exception to accountability: "In the absence of a valid defense such as breach of a presentment warranty . . ., settlement effected or the like . . ." There is no doubt that the payor bank can escape liability where there has been a breach of presentment warranty. The use of the phrase "such as" in the introductory language indicates, however, that the list of defenses is not an exhaustive list. Exception from accountability is made for breach of warranty, settlement effected, "or the like." What exactly "or the like" entails is not specified. It has been suggested that this clause refers to restitution. This is a reasonable interpretation of the statutory language. Given the general acceptance of restitution that existed prior to N.I.L. and Code enactment, limited only by the restrictions of Price v. Neal, it seems unlikely that the drafters would have dramatically changed the common law treatment without even mentioning the change in the comments.

This third interpretation attempts to reconcile the apparent inconsistencies between statutory sections. If section 4-302 is interpreted to allow restitution, the apparent inconsistencies between accountability under section 4-213 and

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160. U.C.C. § 4-302 (emphasis added). It is not clear why a similar provision does not appear in § 4-213. This can be explained if § 4-213 merely specifies the time final payment occurs without specifying the effect of final payment. See supra notes 143-55 and accompanying text. It is, however, difficult to read the accountability provision without concluding that at least to some extent accountability is the effect of final payment. If the absence of any defenses in § 4-213 supports a conclusion that an absolute duty to remit funds is created by final payment (not necessarily a denial of subsequent restitution), why does § 4-302 seem to allow for defenses to this duty to remit? This inconsistency is impossible to resolve satisfactorily.


162. Id.


164. See Note, Allocation, supra note 5, at 1099. The author considers only the conflict between §§ 3-418 and 4-213. No consideration is given to § 4-302. This is not uncommon. See supra note 147.
accountability under section 4-302, discussed above, are resolved. This reconciliation is achieved in accordance with general Code principles and objectives. Article 4 and, in particular, section 4-302 was designed to promote the rapid processing of checks. Payor banks were placed under a duty to act promptly in deciding whether or not to pay, and were penalized for failure to do so by requiring disbursement of the funds. This principle is not, however, inconsistent with allowing subsequent restitution.

Inasmuch as this interpretation of section 4-302 is inconsistent with the case law imposing absolute liability under section 4-302, one must conclude that those cases were incorrectly decided. A careful reading of the majority of undue retention cases reveals, however, that few of them directly address the restitution issue. Most cases in which accountability has been equated with absolute liability were cases in which the payor bank was being sued to require disbursement of funds. Creation of an absolute duty to remit funds is not necessarily inconsistent with allowing subsequent restitution. Moreover, it is possible that, although the court did not discuss the fact, in many undue retention cases the person receiving payment was a holder in due course.

In a variation on this approach, it could be asserted that section 4-213 provides when final payment occurs. In order to determine the effect of final payment, one must look to one of two places. If the item was finally paid by undue retention, section 4-302 specifies that the payor bank should be accountable for the item, subject to the defense provisions. If the item was paid in any other manner, section 3-418 specifies final payment subject to restitution. Neither final payment under section 3-418 nor accountability under section 4-302 would eliminate restitutionary rights except where there is a holder in due course or where there has been good faith reliance. The need for a separate provision detailing the results of undue retention is more easily understood in light of the fact that the concept of undue retention was a new concept that had been the subject of some confusion under the N.I.L.

While both variations reconcile the conflicting Code sections in a fairly logical manner, they are not without problems. Most importantly, even if one accepts the general premise that restitution should be available to a payor bank which by mistake finally pays an item in the bank collection process, it is unclear when restitution should be raised. In other words, can

165. U.C.C. § 4-101 Official Comment; Edwards, supra note 126, at 355; Hill, supra note 126, at 299; Note, Retention of a Check, supra note 118, at 116.

166. Whether restitution should be allowed as a defense in a suit to account or restricted to a subsequent action to recover monies paid is unclear. To the extent, however, that finality is an objective to be achieved by the final payment rule, see infra note 174 and accompanying text, allowing restitution would be inconsistent with that objective.

167. See supra note 149.
a payor bank assert restitution as a defense in a suit by the presenting party
to compel disbursement of funds, or is restitution limited to a suit by the
payor bank subsequent to disbursement? The answer is not apparent.
Interpreting the introductory language of section 4-302 as providing for
restitution would seem to permit its defensive use. There are, however, two
arguments against allowing defensive assertion of restitution. First, by its
very nature restitution generally seeks "restoration" of money paid by
mistake. Allowing restitution to be asserted in a defense would be inconsis-
tent with common law treatment. Second, under this approach the term
"accountable" is rendered almost meaningless. If the term does not even
require disbursement of funds, what does it require?

Alternatively, restitution could be limited to a subsequent lawsuit by the
payor bank to recover the funds disbursed. This would protect the expec-
tations of the parties in the bank collection process, and it is supported by
a literal reading of the term "accountable." Where final payment has
occurred without funds disbursement, the payor bank could best be put in
the same position as if it had, in fact, finally paid the item in cash by
creating an absolute duty on the part of the payor bank to disburse funds.168
It would, in addition, penalize the payor bank for its delay in the case of
undue retention.169

There are, however, three arguments against this interpretation. First, it
is inefficient to require two lawsuits where one would suffice. Second, if
an absolute duty to remit funds is required by the term accountable, what
is the function of the introductory language to section 4-302 providing for
certain defenses? Third, it is unclear whether a payor bank which was
forced to remit funds following a mistaken undue retention, but which
turned the funds over to the presenting party (plaintiff) with full knowledge
of the facts, would qualify for restitution. Under those circumstances the
payment would not have been made by mistake.

It is the conclusion of this Article that these sections, despite a number
of attempts, cannot be satisfactorily reconciled. Any satisfactory approach
must interpret the function of each Code section to create a logical, cohesive
scheme. In addition to the difficulty in statutory interpretation, court
treatment has added to, rather than resolved, the confusion. Indeed, the
conflicts between Code sections can, perhaps, best be illustrated by an

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168. See U.C.C. § 4-213 Official Comment 7 (drafters specify that there is no need for
accountability where the payor "has paid the item in cash because such payment is itself a
sufficient accounting").

169. See supra notes 132-37 and accompanying text where the statutory history is recounted.
The accountable language was designed to impose a penalty upon the dilatory payor bank in
the case of undue retention. Even though a subsequent action for restitution would be allowed,
the payor bank would be penalized by the costs of litigating the second action. See Comment,
Broader Liability, supra note 5, at 825, where the author asserts that this expense would
encourage care on the part of the payor bank.
examination of court treatment in the context of specific situations. Because of the availability of warranty relief, the issue of restitution is unlikely to arise in the context of forged indorsements. The issue is, instead, more likely to be litigated in the instance of a forged drawer's signature or where there are insufficient funds from which the check can be paid.

In the case where a check has been mistakenly paid over a forged drawer's signature, courts typically ignore the conflict between Code sections and apply section 3-418 even where the check has clearly entered the check collection system. This results in allowing restitution where there is neither a holder in due course nor good faith reliance. Those courts that do recognize the conflict are split as to its resolution; some read the section 3-418 restrictions into section 4-213 and some refuse to do so.

Additional problems arise in the process of applying the final payment rule to the payment of insufficient funds checks. At common law, the majority rule precluded restitution by the payor who paid an insufficient funds check even if the check was paid by mistake. Given this common law background, the conflict between Code sections takes on a new dimension. Even if the section 3-418 limitations are read into article 4, allowing the assertion of restitution, its actual availability is dependent upon applicable state law. Restitution would only be available to the payor bank where it would be available at common law. In most cases where the payor bank has delayed return of an insufficient funds check, even through mistake, the accountability language of section 4-302 has operated to impose absolute liability and preclude restitution. It is, thus, evident that the U.C.C. scheme fails to adequately address the question of whether or not restitution is available in the bank collection context.

170. Perini Corp., 553 F.2d at 398; Fireman's Fund Ins. Co., 85 Cal. App. 3d at 797, 149 Cal. Rptr. at 883; Payroll Check Cashing, 401 N.E.2d at 752; Maplewood Bank & Trust Co., 142 N.J. Super. at 480, 362 A.2d at 44; Richardson Co., 504 S.W.2d at 812.


172. See, e.g., Park, 722 F.2d at 1303 (restitution permitted after mistaken payment of an insufficient funds check since the common law in Ohio permitted restitution). The Park court's emphasis on the language of § 3-418, which clearly applies to overdrafts (see U.C.C. § 3-418 Official Comment 2) has been misinterpreted as allowing restitution when permitted by § 3-418 without reference to state law. Note, Easy Come, Easy Go, supra note 126, at 689-90.

173. This creates the anomalous situation in which the availability of restitution depends upon whether the payor bank paid out the money for the item or retained it beyond the midnight deadline. Restitution would be virtually nonexistent if the item was retained beyond the midnight deadline, but might be possible if the item was paid. This, obviously, encourages the payor to pay the item when in doubt and hope that the applicable state law allows restitution. Whether or not restitution was available, even where the insufficient funds item was paid, often depends upon whether restitution was available at common law in insufficient funds situations in that particular state. Whether or not the payor is entitled to restitution, therefore, might differ depending upon how the item was paid, and the common law of the state where the item was paid.
3. Summary of Article 4 Sections Under the Narrow View of Displacement

It is clear that neither article 3 nor article 4 expressly displaces the availability of restitution. Whether or not there has been implied Code displacement, on the other hand, depends, in most instances, on whether one adopts the narrow or expansive view of displacement. With respect to the narrow view of displacement, restitution has been displaced by the language of section 3-418 only with respect to payments made to a holder in due course or to one who changed his position in reliance upon the payment. The key question is whether restitution has been further displaced under the language of article 4. It is not clear whether the language of article 4 is inconsistent with restitution because the language itself is unclear. Article 4 provides that upon final payment the payor bank is accountable for the amount of the item, but the extent to which article 4 is inconsistent with restitution depends upon the interpretation one gives to the term accountable. If accountable is interpreted as absolutely liable, then this would preclude restitution. If, however, the term accountable is interpreted as requiring only that the payor bank disburse the funds (to, in effect, put itself in the position that it would have been in had it effected final payment in cash), restitution might be available. The extent to which restitution is displaced is, therefore, unclear under the narrow view of displacement.

C. Restitution Within the Code Under the Expansive View of Displacement

The unsettling result of Code analysis under the narrow view of displacement is the primary reason for looking to the expansive view which considers whether common law restitution is at odds with the broad purposes and policies of the Code. Within the context of the check collection system, as governed by articles 3 and 4, one important purpose or policy is finality of commercial transactions, which entails the view that commerce requires an end to commercial transactions.\textsuperscript{174} Restitution of a mistaken payment obviously conflicts with the policy of finality in that restitution allows a transaction to be opened up at a time subsequent to the payment. This could not, however, constitute sufficient justification to abolish restitution from the Code scheme of check collections because both the transfer and presentment warranties, which are expressly provided for in both article 3 and article 4, also clearly conflict with the policy of finality.

\textsuperscript{174} U.C.C. § 3-418 Official Comment 1.
Another broad purpose of the Code is to promote certainty in matters of commercial law.\textsuperscript{175} The parties to a transaction should be able to ascertain relevant law with a fairly high degree of certainty. With respect to recovering mistaken payments it is clear that restitution is at odds with this policy. First, there is significant disagreement among the states on several important issues of restitution, particularly with respect to the mistaken payment of insufficient fund and no account items. Supplementing the Code provisions with this unsettled body of common law creates less certainty in transactions governed by the Code. These variations among the states, when used to supplement Code provisions, also conflict with the important Code policy of uniformity.\textsuperscript{176} Moreover, with respect to those matters over which there might be uniform agreement under common law, restitution, which is based on concepts of justice and fairness, is inherently uncertain and unpredictable in its application. We have already seen that a defendant in a restitution case may assert essentially any argument to show that it would not be unjust to allow him to keep the mistaken payment. Delving into such things as the relative financial worth of the parties hardly promotes certainty in the law.

Up to this point, it appears that a consideration of Code policies points to displacement of restitution; however, another policy within the Code scheme of check collections must be considered—that of avoiding unjust enrichment. It is clear that the drafters saw this as playing some role under the Code. In fact, restitution is specifically called for under some circumstances.\textsuperscript{177}

We can see from the above discussion that the statutory language is deficient with respect to delineating the availability and scope of common law restitution. It should also be apparent that the problem is more fundamental than mere language deficiencies. The broad purposes and policies of the Code, as evidenced by the statutory language and official comments, simultaneously support and reject the availability of common law restitution.

It is submitted that the root of the problems relating to recovering mistaken payments under the Code lies in a substantive blunder made nearly forty years ago by the drafters of the original articles 3 and 4. The blunder was adopting a warranty theory of recovery while at the same time retaining

\textsuperscript{175} Great W. Bank & Trust Co., 138 Ariz. at 265, 674 P.2d at 328; R. Hillman, J. McDonnell & S. Nickles, supra note 90, at ¶ 1.06(2)[a] and [c]; Gedid, U.C.C. Methodology: Taking a Realistic Look at the Code, 29 WM. & MARY L. REV. 341, 354-59 (1988); Hillman, supra note 69, at 655, 678-79.

\textsuperscript{176} U.C.C. § 1-102(2)(c); General Comment of N.C.C.U.S.L. and the A.L.I., I.U.L.A. xv, (1989); see also Gedid, supra note 175, at 379; Hillman, supra note 69, at 655, 678-79; Nickles I, supra note 64, at 13.

\textsuperscript{177} See U.C.C. § 4-407 (establishes certain rights “to prevent unjust enrichment”); supra notes 98-99 and accompanying text.
common law restitution. Evidence for this assertion is found by first looking at pre-Code law.

Early in their common law development restitution and warranty functioned as competing theories of recovering mistaken payments. As these theories developed, however, they clearly diverged to the extent that they would support different results in some cases even while generally adhering to the *Price v. Neal* rule. The reason for this divergence is easy to see. Freed from the change of position defense and the doctrinal baggage of unjust enrichment, warranty became a much more streamlined basis of recovery, which typically favored the plaintiff. As a result of these substantive differences, principally with respect to defenses, warranty and restitution claims sometimes lead to different results under the same circumstances. Yet, the Code (both article 3 and article 4) expressly adopts warranty as a basis of recovering mistaken payments while at the same time retains common law restitution.

Incorporating these two distinct and potentially conflicting theories of recovery results in a number of undesirable consequences. First, it greatly complicates the body of law governing recovery of mistaken payments. Two separate and independent bases of recovery exist with identical objectives, namely, recovering mistaken payments. Instead of a unified theory of recovery, courts must presently consider both bodies of law in each mistaken payment case and face inconsistencies between the two.

Second, the presence of restitution invites uncertainty and lack of uniformity in the law of recovering mistaken payments. The uniformity that is achieved through the detailed provisions of sections 3-417 and 4-207 is considerably diminished by the interplay with restitution. This is due both to the variations among the states as well as the inherent uncertainty of restitution.

The third consequence relates to the policy rationale behind the warranty provisions. In sections 3-417 and 4-207 the drafters went to great lengths to delineate carefully and specifically the warranties that are given on presentment and to fashion numerous specific exceptions thereto. According to the official comments, the purpose behind these provisions, both in allowing recovery and in denying recovery, was to follow the rule in *Price v. Neal*. The apparent comprehensiveness of this section is lessened considerably when we see that a plaintiff who is unable to recover the mistaken payment in a warranty action can pursue a restitutionary claim, sometimes successfully. The policy behind denying warranty recovery under certain circumstances is obviously frustrated by simultaneously allowing the plaintiff another chance to achieve the same objective (recovering the payment) under

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178. See 3 G. PALMER, *supra* note 17, § 16.8; *supra* notes 81-83, 97, 112, and accompanying text.
an entirely different theory. This same problem can be considered from the perspective of restitution as well. The policy behind denying restitution under certain circumstances is frustrated by allowing the plaintiff, who is unable to obtain restitution, to pursue a warranty action in order to recover the payment.

The presence of two alternative and inconsistent theories of recovery inevitably results in ambiguities within the article 4 provisions relating to the accountability concept and mistaken payments. As a consequence of the ambiguous relationship between warranty and restitution, the relationship between restitution and the accountability concept of article 4 is ambiguous as well. The language of section 4-302 expressly excepts breach of warranty from the operation of the accountability concept in cases of undue retention, but the section ignores the matter of how accountability relates to a restitutionary claim through section 1-103. It has been argued that the phrase "or the like" in section 4-302 encompasses a restitutionary claim, but a significant number of courts and commentators have rejected this interpretation.\(^{179}\)

A review of the drafting history of the Code fails to clearly establish why the drafters adopted a warranty theory of recovery while retaining common law restitution. The confusion may be at least partly due to the drafters’ failure to analyze and synthesize pre-Code, especially pre-N.I.L., case law. It may be also partly due to the drafters simultaneously embracing conflicting policies with respect to recovering mistaken payments without adequately addressing the interplay between these policies and the resolution of such conflicts. With this background in mind it is now appropriate to consider the proposed changes to articles 3 and 4 and see how, if at all, these problems have been addressed.

IV. AN ANALYSIS OF THE PROPOSED CHANGES TO ARTICLE 3 AND 4 PROVISIONS RELATING TO MISTAKEN PAYMENTS

The drafting project to revise articles 3 and 4 presents a rare and valuable opportunity to correct drafting errors in the present versions of these articles and fashion a permanent statutory solution to the problem of recovering mistaken bank payments. The proposed revisions include a limited number of substantive changes in the sections that relate to recovering mistaken payments. These will be analyzed and discussed in this section.

Like the current Code, the R.U.C.C. retains warranty as the primary basis of recovering mistaken payments. For clarity, the R.U.C.C. drafters

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179. See supra notes 160-64 and accompanying text; see also Rogers, supra note 55, at 945 n.54 (the author also finds fault with “parallel systems” of liability in the check collection system).
have separated transfer warranties and presentment warranties into two
different sections, R.U.C.C. sections 3-416 and 3-418, have
distinguished presentment warranties made to drawees of unaccepted drafts from
those made to acceptors of drafts and makers of notes. These changes
are proposed in order to avoid the complicated exceptions to the presentment
warranty found in current sections 3-417 and 4-207; however, the overall
structure and substance of both types of warranties are unchanged. Just
as under section 3-417 of the current Code, the presenter warrants under
R.U.C.C. section 3-418 that all indorsements necessary to pass title are
genuine and that there are no material alterations. With respect to
presentment of unaccepted drafts to drawees, the R.U.C.C. follows the
current Code in excluding a warranty of a genuine drawer's signature by
warranting only that the presentor has no knowledge that the drawer's
signature is forged. Although the R.U.C.C. warranty provisions embody
no significant substantive changes from the Code provisions, one must
consider the role that restitution will play in recovering mistaken payments
under the R.U.C.C.

U.C.C. section 3-418, one of the key Code sections dealing with restitution,
have been replaced by R.U.C.C. section 3-419. At first glance, it

180. R.U.C.C §§ 3-416, 3-418. According to § 4-304 these warranties apply in a case
otherwise governed by article 4. Id. § 4-304(1). For a discussion of warranties under the Code,
see supra notes 91-97 and accompanying text.
181. R.U.C.C. § 3-418(a); see also id. § 3-418 Official Comment 1.
182. Id. The drafters acknowledge that the R.U.C.C. presentment warranties duplicate the
substance of the current Code warranties by stating in the prefatory note that the "warranties
are restated but they do not change existing law." See id. § 3-418 Official Comment 2; id.
Prefatory Note vi.
183. R.U.C.C. § 3-418(a)(1), (a)(2). Like the current Code, this part of R.U.C.C. § 3-418
does not refer to genuineness of indorsements. Instead, it refers to being "entitled to enforce
the draft or authorized to obtain payment . . . ." Id. § 3-418(a)(1). Inasmuch as such entitlement
or authority is dependent upon the genuineness of indorsements necessary to pass title, the
warranty under this subsection is essentially a warranty that these indorsements are genuine.
184. Id. § 3-418(a)(3). The only substantive change is the addition in article 4 of a warranty
with respect to M.I.C.R. encoding. Id. § 4-208(1). The warranty is one of accuracy in encoding
and subjects the warrantor to liability for loss caused by overencoding or underencoding. This
warranty appears only in article 4 because problems with encoding are unique to the check
collection process. For a discussion of the use of M.I.C.R. in the check collection system, see
Bank Leumi Trust Co. v. Bally's Park Place, 528 F. Supp. 349 (S.D.N.Y. 1981); R.U.C.C. § 4-208
Official Comments 1 & 2; N. PENNY & D. BAKER, THE LAW OF ELECTRONIC FUND
TRANSFER SYSTEMS § 1.02, at 1-19 to 1-29 (1980).
185. Section 3-419 states:
(a) Except as provided in subsection (c), if the drawee of a draft pays or
accepts the draft and the drawee acted on the mistaken belief that (i) payment
of the draft had not been stopped under Section 4-403, (ii) the signature of the
purported drawer of the draft was authorized, or (iii) the balance in the drawer's
account with the drawee represented available funds, the drawee may recover the
amount paid from the person to whom or for whose benefit payment was made
or, in the case of acceptance, may revoke the acceptance. Rights of the drawee
under this subsection are not affected by negligence of the drawee in paying or
appears to entail a number of changes from U.C.C. section 3-418. Determining whether these changes are substantive, however, requires closer analysis.

R.U.C.C. section 3-419, entitled "Payment or Acceptance By Mistake," deals with mistaken payment or acceptance of an instrument. Subsection (a) governs mistaken payment or acceptance by a drawee of three types of drafts: 1) those paid over a stop payment order, 2) those containing a forged drawer's signature, and 3) those drawn on insufficient funds. Subsection (b) governs all other types of mistaken payment or acceptance cases. This arrangement raises four related issues. First, why did the drafters establish this division between types of mistake cases rather than treat all mistaken payments and acceptances under one provision? Second, to what extent is the right of recovery under subsection (a) different from that under subsection (b)? Third, what types of mistaken payments or acceptances fall within subsection (b)? Fourth, on what basis were these types of mistake cases relegated to subsection (b) coverage?

The comments to R.U.C.C. section 3-419 state that subsection (a) "applies to the most common cases in which the problem is presented." The "problem" referred to here is presumably that of mistaken payments and acceptances. It is likely, however, that the most common type of mistaken payment is a payment over a forged indorsement, but this type of case is not among those enumerated in subsection (a). The drafters may have intended the subsection to cover the most common types of mistake cases not included under the R.U.C.C. section 3-418 presentment warranty provisions. This interpretation, however, is questionable because forged draw-

(b) Except as provided in subsection (c), if an instrument has been paid or accepted by mistake and the case is not covered by subsection (a), the person paying or accepting may recover the amount paid or revoke acceptance to the extent allowed by the law governing mistake and restitution.

(c) The remedies provided by subsection (a) or (b) may not be asserted against a person having rights of a holder in due course of the instrument or a person that in good faith changed position in reliance on the payment or acceptance of the instrument. This subsection does not limit remedies provided by Section 3-418 for breach of warranty.

R.U.C.C. § 3-419.
186. Id. § 3-419(a).
187. Id. § 3-419(b).
188. Id. § 3-419 Official Comment 1.
189. Although insufficient fund and no-account checks make up a large majority of "bad checks," they constitute a minor part of checks mistakenly paid because, as Professor Farnsworth states, they are "almost invariably detected by the drawee and dishonored." Farnsworth, Insurance, supra note 45, at 297 (footnote omitted). Because the payor bank has no effective means of detecting a forged or otherwise unauthorized indorsement prior to payment, they probably are the most common type of mistaken payment.
190. Those warranty provisions deal with forged indorsements, knowledge of a forged drawer's signature, and material alteration. R.U.C.C. § 3-418(a)(1), (a)(2), (a)(3).
ers' signatures, which are referred to in subsection (a), are also included in those warranty provisions.\textsuperscript{191}

It is most likely that the reasoning behind covering three types of mistake cases in subsection (a) and leaving the rest covered by subsection (b), was to take what the drafters perceived as the most common types of mistake cases and fashion specific rules as to when recovery is allowed and when it is precluded. This would clarify the law of mistake in these types of cases by avoiding the uncertainty and diversity of common law restitutionary doctrine which through U.C.C. section 1-103 has resulted in myriad problems in mistake cases under the current Code. The other types of mistake cases not included in subsection (a) were deemed relatively unimportant. They were left to be resolved under common law restitutionary doctrine despite the substantial risks of uncertainty and diversity. This interpretation makes sense, however, only if the recovery right under subsection (a) is reasonably definite and the nature of that right is different from that under subsection (b).

The text of the proposed statute suggests that the recovery right under subsection (a) is different from that under subsection (b). Subsection (a) provides that in the specified types of mistake cases the drawee "may recover" the payment.\textsuperscript{192} This right is limited only by the holder in due course and change of position defense provided in subsection (c).\textsuperscript{193} Subsection (b) provides that in mistake cases "not covered by subsection (a)" the person paying "may recover" the payment. This latter right of recovery is subject, however, not only to the holder in due course and change of position defenses under subsection (c); it is also available only "to the extent allowed by the law governing mistake and restitution."\textsuperscript{194} The use of the different language in each subsection supports the notion that the nature of the right in each subsection is also different. If the drafters intended the recovery rights in both subsections to be identical it is reasonable to suppose that they would have used identical language. Moreover, having identical recovery rights in both subsections would vitiate the need for distinct subsections.

There is, on the other hand, language in the comment to R.U.C.C. section 3-419 that suggests the recovery rights in subsections (a) and (b) may be the same. The comment provides that "[p]roposed Section 3-419 specifically states the right of restitution in subsection (a) and (b)."\textsuperscript{195} On one level this suggests that the recovery rights in both subsection (a) and (b) are the same. The comment makes no distinction between "the right of restitution?" stated

\textsuperscript{191} Id. § 3-418(a)(3).
\textsuperscript{192} Id. § 3-419(a).
\textsuperscript{193} Id. §§ 3-419(a), (c).
\textsuperscript{194} Id. § 3-419(b); see also id. § 3-419 Official Comment 2.
\textsuperscript{195} Id. § 3-419 Official Comment 1.
in subsection (a) from that stated in subsection (b). Read on another level, however, this portion of the comment is compatible with viewing the recovery right in subsection (a) as distinct from that in subsection (b). The use of the term "restitution" in the comment probably is not used to denote the body of common law rules and principles examined in Part II of this Article. Rather, it appears to be used in a more general sense of recovering or restoring a payment. This more general use is in contrast with how the term "restitution" appears to be used in subsection (b). Assuming that the recovery right in subsection (a) is different from that in subsection (b), we must next examine the nature of those rights and see how they compare with each other and with restitution under the present Code.

The nature of the recovery right under subsection (b) of R.U.C.C. section 3-419 is relatively clear. In the comment to that section the R.U.C.C. drafters describe the majority view that U.C.C. section 3-418 does not create a right of restitution in mistaken payment cases. Instead, that right is found in the common law and incorporated into the Code through section 1-103. Section 3-418 limits that right primarily through the use of the holder in due course and change of position defenses. In comment 1 to R.U.C.C. section 3-419 the drafters then indicate that, in contrast to the present Code, that section "specifically states the right of restitution in subsection (a) and (b)." Looking at the language of subsection (b), it is apparent that the right of restitution stated there exists only "to the extent allowed by the law governing mistake and restitution." The law referred to here could be nothing other than the common law. Moreover, in comment 2 to R.U.C.C. section 3-419 the drafters state that subsection (b) "directs courts to deal with those cases under the law governing mistake and restitution." This body of law to which the courts are directed could be nothing other than common law restitution. It is, therefore, fairly clear that the subsection states the right of restitution but does not change the nature of that right from the common law. In this way subsection (b) expressly incorporates common law restitution. With respect to limits on restitution we see that (as under present section 3-418) recovery under subsection (b) is expressly subject to the holder in due course and change of position defenses under subsection (c). Moreover, by allowing recovery only to the extent that recovery would be allowed under common law restitution, the defendant may assert a potentially large array of equitable and legal arguments in order to show that restitution of the payment should not be granted.

In contrast to subsection (b), ascertaining the nature of the recovery right in subsection (a) is much more problematic. The comment to section 3-419

196. Id. For a discussion of present § 3-418, see supra notes 100-15 and accompanying text.
197. R.U.C.C. § 3-419 Official Comment 1.
198. Id. § 3-419(b).
199. Id. § 3-419 Official Comment 2.
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specifies that the "right of restitution" is stated not only in subsection (b) but in subsection (a) as well.\textsuperscript{200} The right of restitution stated in subsection (b) is common law restitution expressly incorporated into the subsection. This suggests that the recovery right in subsection (a) is a common law restitutionary right as well. It is clear, however, that the language of subsection (a) is very different from that found in subsection (b). Unlike subsection (b) which allows recovery only "to the extent allowed by the law governing mistake and restitution,"\textsuperscript{201} the right of recovery in subsection (a) is not similarly limited. It provides that if the drawee mistakenly pays a draft over a stop payment order, a draft with a forged drawer's signature, or a draft drawn on insufficient funds, the drawee "may recover the amount paid."\textsuperscript{202} It is expressly limited only by the holder in due course and change of position defenses of subsection (c). A critical question is whether this recovery right is modified or limited by anything else. This depends on whether the recovery right in subsection (a) displaces common law restitution or codifies common law restitution. If it displaces common law restitution, then the right in subsection (a) should be considered a statutory right created by the language of the subsection and limited only by the defenses specified in subsection (c) or other Code provisions. If, on the other hand, it codifies common law restitution, then the drawee's recovery right is subject not only to the statutory defenses in subsection (c), but also to other defenses under common law restitution. This includes any legal or equitable argument that the defendant can assert to show that it is not unjust to retain the mistaken payment. As the following analysis of section 3-419 shows, the answer to this question is far from certain.

In the comment to R.U.C.C. section 3-419, the drafters state that the section "specifically states the right of restitution in subsection (a) and (b)."\textsuperscript{203} Using the term "restitution" rather than a more general term such as "recovery" supports the notion that both subsection (a) and (b) embody common law restitution rather than a newly created statutory recovery right. Moreover, the comment implies that the recovery right in subsection (a) is the same as that in subsection (b). From the analysis of the statutory language of section 3-419 and its comments, it is fairly clear that the right embodied in subsection (b) is common law restitution. The recovery right embodied in subsection (a) would, therefore, be common law restitution as well. The comment to section 3-419 and the Prefatory Note both refer to \textit{Price v. Neal}. The comment states that subsections (a) and (c) "incorporate the rule of \textit{Price v. Neal}."\textsuperscript{204} Notwithstanding the two centuries of debate

\textsuperscript{200} Id. § 3-419 Official Comment 1.
\textsuperscript{201} Id. § 3-419(b).
\textsuperscript{202} Id. § 3-419(a).
\textsuperscript{203} Id. § 3-419 Official Comment 1.
\textsuperscript{204} Id.; id. Prefatory Note vi.
over that case, one thing is clear: Price v. Neal was a common law restitution case. This suggests that the recovery right in subsection (a) is common law restitution. Finally, subsection (a) states that the "[r]ights of the drawee under this subsection are not affected by negligence of the drawee in paying or accepting the instrument." If subsection (a) does not embody common law restitution, why is it necessary for the statute to address the effect of the drawee's negligence on the recovery right? A plaintiff's negligence is recognized by only a minority of courts as a defense to a restitution claim in mistaken payment cases. It seems that if subsection (a) embodies a new statutory right which is both created as well as limited by the terms of section 3-419, there is no need to specify things that do not affect the plaintiff's recovery right. Moreover, it infers that things not mentioned in the statutory language, such as other defenses in a common law restitution case, may affect that right.

There are, on the other hand, several arguments that support interpreting subsection (a) as embodying a new statutory right. The first is, of course, the language of the statute. The difference between the language of subsection (a) and section 3-419 is clear: subsection (a) states that the "[r]ights of the drawee under this subsection are not affected by negligence of the drawee in paying or accepting the instrument." If subsection (a) does not embody common law restitution, why is it necessary for the statute to address the effect of the drawee's negligence on the recovery right? A plaintiff's negligence is recognized by only a minority of courts as a defense to a restitution claim in mistaken payment cases. It seems that if subsection (a) embodies a new statutory right which is both created as well as limited by the terms of section 3-419, there is no need to specify things that do not affect the plaintiff's recovery right. Moreover, it infers that things not mentioned in the statutory language, such as other defenses in a common law restitution case, may affect that right.

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205. Id. § 3-419(a).
206. This language raises another troublesome issue. The drawee's recovery right under subsection (a) is not available when there is a holder in due course of the mistakenly paid item. In Official Comment 1 to this section, the drafters state that in most cases there will be a holder in due course of the mistakenly paid item, and, therefore, in most cases the drawee will be unable to recover. By raising the matter of the effect of the drawee's negligence on recovery the drafters are raising an issue that, according to their comment, is not very important. The effect of the drawee's negligence is not addressed in present § 3-418 or its comments. Those comments, however, do address the issue of the effect of the defendant's negligence. The comments clarify an issue under the N.I.L. by stating that the defendant's negligence will not preclude protection under the final payment rule unless the negligence amounts to a lack of good faith. U.C.C. § 3-418 Official Comment 4 (1987); see supra notes 102-04 and accompanying text. The R.U.C.C. drafters have dropped this issue completely from the R.U.C.C. The effect of the defendant's negligence is not dealt with in R.U.C.C. § 3-419 or its comments.

We can expect that this will be a source of problems in cases litigated under the R.U.C.C. Dropping this comment from the R.U.C.C. may (at least for some courts) infer that the R.U.C.C. drafters intended to change this rule, making the defendant's negligence preclude holder in due course status under § 3-419. If, as the drafters suggest, there will usually be a holder in due course of the mistakenly paid item, the effect of negligence on holder in due course status is very pertinent. It should be addressed by the R.U.C.C. drafters. Although a majority of pre-Code cases made the negligence of the defendant (recipient of the mistaken payment) preclude protection under the rule, one commentator noted that the cases are in "hopeless conflict" over establishing uniform standards of negligence. O'Malley, supra note 5, at 205 n.93. The R.U.C.C. drafters may be inviting a return of this conflict. For a case discussing some problems created by making the recipient's negligence relevant, see First Nat'l Bank v. Bank of Wyndmere, 15 N.D. 299, 303, 108 N.W. 546, 548 (1906); supra notes 50, 71, 104.

Another issue relating to the defendant's negligence is raised when we consider the change of position defense which is also provided in subsection (c). At common law the change of position must be, inter alia, non-negligent to constitute a defense in a restitutionary action. See supra note 35 and accompanying text. Because a change of position is a defense under R.U.C.C. § 3-419, the drafters should address the issue of negligence in this context as well.
tion (b), which allows recovery only "to the extent" allowed under common law restitution, and subsection (a), which limits the recovery right only by the holder in due course and change of position defenses in subsection (c), strongly suggests that the recovery right in subsection (a) is not common law restitution. Second, the language of comment 2 to section 3-419 states that subsection (b) "directs the courts" to apply common law restitution. The comment contains no language of similar import with respect to subsection (a). This also suggests that the recovery right embodied in subsection (a) is not common law restitution. Third, with respect to the reference to the rule of Price v. Neal, we have already seen that even though the case was a restitution case, the rule of the case is compatible with other bases of recovery. The rule is compatible with warranty, and presumably, with other theories of recovery as well. Perhaps the most compelling reason for concluding that the recovery right in subsection (a) is a statutory right rather than common law restitution is that if the recovery rights in these two subsections are the same, it vitiates the reason for treating mistake cases in two different subsections. The R.U.C.C. drafters must be faulted for failing to clarify the statutory language, or at least failing to clarify this issue in the comments to section 3-419. Nevertheless, we believe that the language of subsection (a) should be construed as creating a new statutory right of recovery while subsection (b) codifies common law restitution.

207. With respect to the reasoning behind the distinction between subsections (a) and (b), in both the comments to § 3-419 and the Prefatory Note the drafters focus on the idea that subsection (a) covers specific types of mistake cases, but there is clearly inadequate attention given to the issue of how the recovery right in subsection (a) differs from that in subsection (b). R.U.C.C. § 3-419 Official Comments; id. Prefatory Note vi.

208. Replacing present § 3-418 with R.U.C.C. § 3-419 creates a potential problem with respect to the concept of final payment. Under the majority interpretation of the Code, the right of recovery is that found in common law restitution. Present § 3-418 makes a mistaken payment final by limiting those restitutionary rights under certain circumstances. See R.U.C.C. § 3-419 Official Comment 1; supra notes 100-15 and accompanying text. The R.U.C.C. drafters state that § 3-419 replaces present § 3-418. It is, however, not clear that the function of § 3-418 has been replaced by R.U.C.C. § 3-419 because the purpose of § 3-418 is very different than that of present § 3-418. In § 3-419 the R.U.C.C. drafters have created a statutory right of recovery in subsection (a) and expressly codified common law restitution in subsection (b). In this sense § 3-419 has replaced the need to look to the common law through § 1-103 to find a right to recovery, but it has not replaced the function of § 3-418 which is to limit that right. This makes it necessary to ask what makes payment final under the R.U.C.C. Subsection (c) of § 3-419 specifies that the recovery rights under subsections (a) and (b) "may not be asserted against" a holder in due course or one who changed position in reliance on the payment. This subsection (c) limitation limits the recovery rights under subsections (a) and (b). The subsection clearly states that it does not limit recovery under warranty; however, it may be read as not limiting a recovery right from some other source. By specifying the circumstances in which recovery is available one can obviously infer from the statutory language that recovery is not available (i.e. payment is final) in other circumstances. Nevertheless, in order to avoid potentially inconsistent interpretations by the courts, the R.U.C.C. drafters should specify in the statutory language or the comment that in cases where a mistaken payment cannot be recovered pursuant to subsections (a) and (c) the payment is final.
The next matter to be addressed is that of ascertaining what types of mistake cases fall within the coverage of subsection (b).

The language of subsection (a) is very clear with respect to the types of mistake cases that fall within its coverage. It applies when the drawee mistakenly pays or accepts a draft on which payment has been stopped, or which contains a forged drawer's signature, or which was drawn on insufficient funds. The comments to section 3-419 resolve some confusion that exists under the present Code by elaborating on the concept of "mistake" that is employed by the statute. As described by the drafters, this concept is similar to that found in common law restitution. It does, however, expand the scope of recovery. Although comment 2 to section 3-419 elaborates at great length on the nature of mistake within the context of insufficient funds cases, the drafters do not address numerous other aspects of the concept. Some of these can be adequately dealt with by using the discussion on insufficient funds cases as an analogy. Nevertheless, many questions will remain. When a court confronts such a question, to what body of law or principles should the court look for guidance? The most obvious choice is common law restitution which provides a well-developed doctrine on the concept of mistake. Thus, even though the recovery right in subsection (a)

209. R.U.C.C. § 3-419 Official Comment 1. The confusion is generated not by U.C.C. § 3-418, but by differences among the courts over what constitutes a mistake sufficient to justify common law restitution read into the Code through § 1-103.

210. The statement in the text is made with some qualification. Case #1 mentioned in Official Comment 1 deals with a situation where the drawee pays an item drawn on insufficient funds, intending to pay it as an overdraft, and subsequently seeks reimbursement from its customer, the drawer of the draft. By concluding that no mistake sufficient to trigger recovery under the statute is made under these circumstances the drafters are in agreement with common law restitution. It should be noted, however, that even if the drawee makes a deliberate decision not to check the state of the account, this is characterized as conscious ignorance which, at common law, is not considered a mistake sufficient to trigger restitution. Case #2 deals with a situation where the drawee negligently fails to ascertain whether the drawer's account contains sufficient funds to pay the draft. By concluding that a mistake triggering recovery is made under these circumstances the drafters are not in agreement with the majority view at common law. Although negligence, in general, did not preclude recovery at common law, Case #2 conflicts with the common law because it allows recovery of a mistakenly paid insufficient funds item. See supra notes 50-53 and accompanying text.

It appears that Case #3 also represents somewhat of a departure from common law restitution. Although common law doctrine does not address current funds availability legislation, it does deal with cases where the drawee expects items deposited by the customer to be collected, but such items are instead dishonored. The drafters state that "if the bank mistakenly believed that the credit balance represented available funds," there is a mistake sufficient to trigger recovery. This result appears contrary to the position taken by courts on this issue. See, e.g., Lowe's of Sanford, Inc. v. Mid-So. Bank & Trust Co., 44 N.C. App. 365, 260 S.E.2d 801 (1979); Demos v. Lyons, 151 N.J. Super. 489, 376 A.2d 1352 (N.J. Super. Ct. Law Div. 1977). Nevertheless, because recovery in this circumstance is subject to the holder in due course and change of position defenses, the result should be in line with common law restitution. Note that the use of the concept of mistake from common law restitution supports the argument that the recovery right in subsection (a) is common law restitution rather than a statutory right.
is a statutory one rather than common law restitution, common law restitution will be relevant in ascertaining the contours of that right.

The next step is obviously one of determining what types of mistake cases fall within subsection (b). The statutory language of section 3-419, the comments to that section, and the Prefatory Note all indicate that subsection (b) covers mistaken payment or acceptance cases "not covered by subsection (a)."211 Under a literal reading of this language, subsection (b) would include any type of mistaken payment of a note as well as any mistaken payment or acceptance of a draft other than the three types enumerated in subsection (a). The critical question here is whether this includes those types of mistake cases covered by the presentment warranty provisions of R.U.C.C. section 3-418. A literal reading of the statutory language suggests that it does. Mistake cases "not covered by subsection (a)" would include items mistakenly paid or accepted on a forged indorsement as well as a material alteration.

Such a reading would settle the matter were it not for ambiguous statements in the first comment of section 3-419. After discussing subsection (a) and the way in which it relates to subsection (c), the drafters state that 
"[t]he remedy of a drawee to recover funds paid on bad checks is principally found in Section 3-418," which, of course, is the presentment warranty provision.212 This statement raises several issues. First of all, the reference here to "bad checks" is unclear. It is nowhere defined in the R.U.C.C., nor is it defined in the U.C.C. Presumably, it is distinct from the term "forged checks," which is also used but not defined in the same comment. It is troublesome to encounter such an ambiguous term in the comment, the purpose of which is to clarify statutory language and intent. Nevertheless, it is reasonable to assume that the term "bad check" encompasses all checks that for a variety of reasons, such as forgeries, material alterations, and insufficient funds, are mistakenly paid.213 By saying that the "principal" remedy in bad check cases is found in section 3-418 the drafters infer that section 3-419 provides a secondary or complementary remedy in bad check cases. The problem here is to ascertain the extent to which these remedial sections overlap.

211. R.U.C.C. § 3-419(b); id. Official Comment 2; id. Prefatory Note vi.
212. Id. § 3-419 Official Comment 1.
213. A number of writers and courts use the term "forged check" to refer to a check containing a forged drawer's signature, and the drafters appear to follow this usage. In the portion of comment 1 discussing the results of suits under § 3-418, the drafters distinguish between forged indorsement cases, alteration cases, and forged check cases. It would be inappropriate to equate "bad check" with checks that are not "properly payable" as that phrase is used in the Code. The drafters apparently include insufficient fund items within the concept of "bad checks," yet insufficient fund items are clearly properly payable as the concept is used under U.C.C. § 4-401. U.C.C. § 4-401.
Comment 1 to section 3-419 states that the "drawee wins in forged indorsement cases," citing a section 3-418 warranty provision, and in "alteration cases," citing another section 3-418 warranty provision.\textsuperscript{214} It then states that the drawee "loses in forged check [forged drawer's signature?] cases unless the warrantor had knowledge of the forgery," citing another section 3-418 warranty provision.\textsuperscript{215} We know, however, that the drawee does \textit{not} "lose" if the defendant is not a holder in due course or did not change his position in reliance on the payment or acceptance because in such a case recovery is available under subsection (a) of section 3-419. It is fairly clear, therefore, that at least with one type of mistake case, namely forged drawer's signature, both section 3-418 and section 3-419 apply. Accordingly, the drawee could assert either section depending on the circumstances. A section 3-418 warranty could be asserted if the defendant had knowledge of the forgery. Section 3-419 subsection (a) could be asserted if the defendant is not a holder in due course and can show no change of position. Under this interpretation, both section 3-418 presentment warranty and subsection (a) statutory recovery right exist within the R.U.C.C. as independent and potentially conflicting bases of recovery. There is no reason to assume that other types of mistake cases (such as forged indorsements and material alterations) which fall within the section 3-418 warranty provisions do not also fall within subsection (b) of section 3-419. A drawee who for some reason cannot prevail in a section 3-418 presentment warranty action can assert, perhaps successfully, a restitutionary claim under section 3-419. From this analysis we can conclude that subsection (b) covers any type of mistaken payment of a note as well as any mistaken payment or acceptance of a draft other than the three types enumerated in subsection (a), even though it may also be covered under the section 3-418 presentment warranty provisions.

As a result of this interplay between sections 3-418 and 3-419, the R.U.C.C. rules on the recovery of mistaken payments are unnecessarily complex. It appears that, in this regard, the R.U.C.C. suffers from basically the same problem as the U.C.C. Instead of a unified theory of recovery in mistaken payment cases, the R.U.C.C. drafters have followed the original Code drafters by adopting different theories of recovery that are independent and potentially conflicting. More than one theory may be applicable to a particular mistake case. One effect of this is to undermine the policy rationale behind each theory. In this regard, the R.U.C.C. may be worse than the U.C.C. because the R.U.C.C. has three, rather than two, independent theories of recovery, namely warranty under section 3-418, common law restitution under section 3-419(b), and a statutory recovery right under

\textsuperscript{214} R.U.C.C. § 3-419 Official Comment 1 (citing R.U.C.C. § 3-418(a)(1), (a)(2)).
\textsuperscript{215} \textit{Id.} (citing R.U.C.C. § 3-418(a)(3)).
section 3-419(a). One could avoid some of the potential conflicts between sections 3-418 and 3-419 by construing subsection (b) of 3-419 as not covering the types of mistake cases that are covered by the section 3-418 warranty provisions. With three independent theories of recovery, however, the R.U.C.C. scheme would remain unnecessarily complex.

Leaving certain types of mistake cases out of subsection (a) creates new problems in the R.U.C.C. Although the drafters state that the cases in subsection (a) are the most common types of mistake cases, we have already seen that these are probably not the most common types. Forged indorsements are probably the most common type. This error suggests that the drafters are not sufficiently aware of the common law background on these issues. The drafters took what they thought were the most common types of cases not covered in the warranty provisions, put them into a separate section, and created specific rules on when recovery of the mistaken payment is allowed. Making this distinction between types of mistaken payments on the basis of frequency of occurrence creates a significant problem.

The problem created by this type of distinction is that no account cases were left out of subsection (a), presumably because they are not a common type of mistake case. However, doing so opens the possibility that courts will treat no account cases differently than insufficient fund cases even though they were treated the same at common law and should, on policy grounds, be treated the same under the Code. Leaving the rest of the mistake cases under subsection (b) invites courts to take approaches conflicting with the common law and with each other. Diversity on these matters is inevitable.

Inasmuch as the R.U.C.C. constitutes a major revision of the Code, perhaps the drafters should take the time to analyze the other types of mistake cases, such as no account cases, and put them under subsection (a) where appropriate. If a type of case does not fit within the subsection (a) rules, they should fashion new language in another subsection to set forth the circumstances under which recovery is allowed. As it stands, the way the drafters dealt with this matter suggests that they have not taken the time to follow through on some of the less common types of mistake cases. To the extent that these other types of mistake cases should be treated differently than the subsection (a) types, such treatment should be based on a rational policy or set of policies regarding recovery of mistaken payments rather than on the frequency of their occurrence.

It is not clear what the drafters’ rationale was in fashioning these R.U.C.C. sections. It may be that they were not cognizant of the common law background of mistaken payments and the tension between the restitution and warranty theories, or how this tension manifests itself in the Code. The comments to the relevant R.U.C.C. sections suggest that the drafters may not have adequately considered the relationship between R.U.C.C. sections 3-418 and 3-419. For example, in comment 1 to section
3-419 the drafters state that the "section covers payment or acceptance by mistake and replaces present Section 3-418." It is obvious, however, that section 3-418 also covers mistaken payment and acceptance. Likewise, in the Prefatory Note the drafters point out that the rationale for the structure of section 3-419 is "the doctrine of Price v. Neal." This offers little guidance in resolving the issues we have raised. As discussed above, there are at least ten different rationales for that case, and several of them are conflicting. Holding up Price v. Neal as a rationale for the changes proposed in section 3-419 confuses rather than clarifies the issues.

Perhaps as a result of the drafters' failure to resolve adequately the problems with respect to restitution and warranty in mistaken payment cases, the R.U.C.C. also fails to resolve adequately the problems with respect to the relationship between the R.U.C.C. section 3-419 recovery rights and the provisions of article 4. The R.U.C.C. proposes to eliminate the provisional settlement, final settlement, and final payment terminology. Instead, payment would occur upon "settlement" by the payor bank. In the typical bank collection case, settlement (and thus payment) would occur when the credit entry was made accompanying an item's physical presentment to the payor bank.

R.U.C.C. section 4-301 specifies the procedure by which the payor bank can dishonor the item after payment by returning the item before its midnight deadline. Section 4-302, retaining the present accountability concept, applies only if settlement has not been made. Revised article 4 fails, however, to address the question of whether restitution might be used by a payor bank to recover mistaken payments after the midnight deadline. A payor bank would be entitled to recover where there has been a breach of presentment warranty. The question the R.U.C.C. drafters have not

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216. Id. § 3-419 Official Comment 1.
217. Id. Prefatory Note vi.
218. Id. § 4-215(1).
219. Id. § 4-213(2)(d). Settlement might also occur, with respect to settlement by credit in an account in a Federal Reserve Bank, when the credit becomes final. Id. § 4-213(2)(b).
220. Id. § 4-301(1). The return of the item under R.U.C.C. § 4-301 is theoretically different from present § 4-301. Under present § 4-301, the payor bank that returns the item by its midnight deadline is permitted to revoke its provisional settlement and avoid liability. Under R.U.C.C. § 4-301, the payor bank that returns the item by its midnight deadline is entitled to a settlement from the bank to which the return is made. Practically, this makes very little difference. Compare id. § 4-301 with U.C.C. § 4-301.
221. R.U.C.C. §§ 4-302(1)(a), 4-302(1)(b). The drafters reasoned that there is no need to make a bank accountable for an item when it has already settled for the item. Id. § 4-302 comment 1. The drafters recognized the inconsistencies between present Code sections. See id. § 4-215 Official Comment 4.
222. Id. § 4-302. Section 4-302 retains the language excepting breach of presentment warranty from accountability. It is unclear why the drafters feel the need to expressly provide an exception for presentment warranty in § 4-302, which covers the unusual situation where no settlement has been made, but not in § 4-301, which covers the typical situation where a settlement has been made. Id. § 4-302(3). The presentment warranties are found in §§ 3-418 and 4-305.
addressed is whether the recovery rights under proposed section 3-419 would provide a similar defense. No mention is made in proposed article 4 of the role that section 3-419 would play. Section 4-302 provides that in addition to the situation where there is a breach of presentment warranty, accountability is inapplicable where "the person seeking enforcement of the liability presented or transferred the item for the purpose of defrauding the payor bank." This is a much narrower defense than is specified in present U.C.C. section 4-302 which allows defenses "such as" breach of warranty "or the like." R.U.C.C. section 4-302 provides only for the defenses of breach of presentment warranty and fraud. The drafters, however, make clear in the official comments to section 4-302 that this language is intended to reject decisions holding that a bank's liability under the accountability provision is absolute. The extent of this rejection is unclear. If the drafters had intended restitution from section 3-419 to offer a means of relief for the payor bank, they should have so specified. Instead, it is unclear from the statutory language what role, if any, section 3-419 plays in check collections.

The drafters make clear by comment in article 3 that their intent is to allow the availability of section 3-419 relief even where the item has been paid through the check collection process. This language is a substantial improvement over present Code treatment; however, addressing this matter in a comment fails to adequately address the concerns raised in this Article. First, the statutory language in article 4 fails to provide allowance for restitution. While the comments are evidence of legislative intent, they might not control over the plain meaning of the statute. It is unclear why the drafters would explicitly provide for recovery in the instance of breach of warranty but not mention restitution. Second, if restitution is allowed, the questions raised about the nature of accountability remain unanswered.

223. Id. § 4-302(3).
224. The example given in the comments would permit a payor bank to escape liability to the defrauder operating a check kiting scheme. Id. § 4-302 Official Comment 4.
225. See id. This is opposed to the absolute liability found by many courts interpreting present § 4-302. See supra notes 121-22, 148-54 and accompanying text.
226. R.U.C.C. § 3-419 Official Comment 3. Comment 3 provides:
   The right of the drawee to recover a payment or to revoke an acceptance under Section 3-419 is not affected by the rules under article 4 that determine when an item is paid. Even though a payor bank may have paid an item under proposed Section 4-215, it may have a right to recover the payment under Section 3-419. National Sav. & Trust Co. v. Park Corp., 722 F.2d 1303 (6th Cir. 1983), cert. denied, 466 U.S. 939 (1984), correctly states the present law on the issue.
   Id. It is unclear why the drafters chose the Park case to cite with approval. The Park case was an insufficient funds case. While the common law in Ohio allows for recovery of mistaken payments in an insufficient funds situation, it has traditionally not been allowed in a majority of states. See supra notes 51-53, 81, 112 and accompanying text. Reference to Park illustrates the difficulties inherent in proposed § 3-419. See supra notes 185-217 and accompanying text.
227. See supra notes 167-69 and accompanying text.
Third, the proposed changes create another problem. If one reads proposed article 4 to allow the payor bank to obtain restitution of the mistaken payment under section 3-419, it is unclear whether the payor bank could assert only common law restitution or the restitutionary right created under subsection (a) of section 3-419. In this way, the R.U.C.C. may have in fact worsened the situation because proposed section 3-419 embodies not one, but two independent theories of recovery: common law restitution under subsection (b) and a statutory recovery right under subsection (a). It is not clear how either one relates to the article 4 provisions.

An additional concern is that defenses are available to the payor bank only under section 4-302, but this section is only applicable where neither a settlement nor a dishonor has been made by the payor bank. This situation would be highly unusual. In the far more typical situation, the payor bank settles for the item promptly. The R.U.C.C. treats this settlement as payment under section 4-215. Section 4-301 specifies the circumstances under which a payor bank that has already settled for the item is entitled to undo the payment and obtain payment by returning the item by its midnight deadline. No mention is made in sections 4-213, 4-215, or 4-302 of any other defenses that the payor bank might assert to undo the payment. Thus, R.U.C.C. article 4 does not solve the problems present in article 4 of the U.C.C. In addition, the R.U.C.C. fails to resolve adequately the apparent conflicts between articles 3 and 4.

The problems encountered under the present Code relating to the recovery of mistaken payments are complex and seemingly intractable. The current drafting project, which proposes a major revision of the Code, offers an opportunity to correct and clarify the many problems with the present Code. However, the current version of the R.U.C.C. fails to offer workable solutions. The next section sets forth a proposed solution that the drafting committee should consider in the next R.U.C.C. draft.

V. TOWARD A UNIFIED THEORY OF RECOVERY

The foregoing analysis of the proposed changes in U.C.C. articles 3 and 4 shows that not only does the R.U.C.C. perpetuate the original drafting blunder, it compounds it. The R.U.C.C. embodies not two, but three, independent and potentially conflicting theories of recovering mistaken payments. The first and most predominant is warranty under R.U.C.C. section 3-418. The second is common law restitution expressly incorporated under subsection (b) of section 3-419. The third is the newly created statutory right of recovery under subsection (a) of section 3-419. Multiple theories of

228. R.U.C.C. § 4-302(1)(a).
229. Id. § 4-301(1).
recovery will be the source of numerous problems under the R.U.C.C. in the same way that they have been under the Code. Instead of using the R.U.C.C. project as an opportunity to resolve the many problems that relate to recovering mistaken payments under the Code, the drafters have created the potential for a number of new problems.

The solution to the problems highlighted in this Article is one that apparently has not been considered by the R.U.C.C. drafters. The solution is basically one of rectifying the original drafting blunder. Recovery of mistaken payments under the Code should be based on a unified theory of recovery. The R.U.C.C. drafters should either establish a warranty basis of recovery and at the same time abolish any vestige of common law restitution, or establish a restitutionary basis of recovery and at the same time abolish any related warranty action. Either theory is adequate to accomplish the goal of establishing a rational and comprehensive system of rules and principles for recovering mistaken payments.

In one respect, a restitutionary basis of recovery is most appropriate given that recovering mistaken payments has traditionally been (and to a significant extent still is) equitable in nature. The inherent weakness of a restitutionary theory of recovery is its uncertainty and unpredictability. To be consistent with the nature of the action, the recipient of the mistaken payment should be allowed to assert virtually any argument in order to show that it would not be unjust to keep the payment. Moreover, the concept of mistake in common law restitution is perhaps too narrow to fit within modern banking practices. In view of the common law, when a bank pays an item in the face of doubts about the genuineness of a signature, for example, it is probably not paying under a mistake of fact. The same probably can be said in the case of a bank that pays an item without bothering to check a signature.230 In such a case it can hardly be said that

230. For a discussion of the concept of mistake under common law restitution, see supra notes 23-27 and accompanying text. Although conventional wisdom suggests that banks, especially large banks, typically do not verify the drawer's signature on items presented for payment, recent empirical research on this issue indicates that most payor banks do check the drawer's signature on all or a substantial number of checks. Murray, Price v. Neal in the Electronic Age: An Empirical Survey, 87 BANKING L.J. 686, 698-701 (1970). Professor Murray reported that "only one bank out of 91 large American banks has 'adopted the practice of not checking signatures on checks below a certain amount.'" Id. at 701. The authors of this Article are not aware of any further empirical research on this question since the publication of Professor Murray's work in 1970. Nor do the authors have any evidence, other than anecdotal evidence (such as reports of banks paying items without any drawer's signature), that contradicts the basic findings of Professor Murray's empirical research. The anecdotal evidence, however, is sometimes compelling. For example, according to a brief filed over ten years ago in a case before a federal appeals court, Morgan Guaranty Trust examines signatures only on checks of $10,000 or more. Note, Allocation, supra note 5, at 1090 n.90; see also O'Malley, supra note 5, at 209. Nevertheless, in view of the very large number of items processed each day by some large banks (approximately 36 billion checks are collected through the Federal Reserve each year, Cooper, Checks Held Hostage—The Funds Availability Con-
the bank was mistaken as to the genuineness of the signature when it was consciously ignorant of the matter. In light of modern banking practices, a restitutionary action will often not be available to the bank that pays an item bearing forgeries or alterations. These problems may make restitution unacceptable as the basis of recovering mistaken payments under the Code.

On the other hand, warranty is susceptible to the same criticism today as it was when it first emerged as a minority theory of recovery. It may be, however, too late to abandon warranty. It has become an integral part of not only the U.C.C., including article 2, but of modern commercial law in general. The relative certainty and predictability of warranty encouraged this development.

The recovery of mistaken payments should be governed by a unified warranty theory of recovery. This can be accomplished by first incorporating into the warranty provisions the situations where recovery is currently based on restitution. Some courts used a similar technique in originally fashioning warranty as a minority theory of recovery at common law. The categories of mistaken payment cases allowing for recovery, as well as those precluding recovery, were retained under an entirely different theory.

The R.U.C.C. drafters have demonstrated, perhaps unwittingly, how the same result can be accomplished under different theories. Looking at the newly created warranty provisions dealing with M.I.C.R. check encoding problems in the check collection system, for example, the problems of overencoding and underencoding have been specifically addressed by a new warranty. M.I.C.R. errors are essentially part of a broader problem of mistaken payments. Analysis of the recent cases and commentary dealing with M.I.C.R. errors shows that they can be resolved either under common law, with restitution or negligence, or warranty. While few cases are reported, a common law approach is favored. There is no need to use

troversy, 102 Banking J.L. 532, 535 (1985)), it has become increasingly difficult to believe that most banks continue to verify the signatures on most items. The authors believe that while small banks may continue to verify the signature on most or all items, large banks verify signatures only on large items. As a result, on a majority of items processed through the check collection system today, the drawer's signature is not verified by the payor bank. For a case in which the drawee's doubts about the genuineness of the drawer's signature were a basis for denying recovery of the payment, see National Bank v. First Nat'l Bank, 141 Mo. App. 719, 125 S.W. 513 (1910).

231. See, e.g., U.C.C. §§ 2-312, 2-313, 2-314, 2-315 (1987); 12 C.F.R. § 210.6 (1989) (Regulation J). Regulation CC has created a warranty to be made upon the return of an item. Under § 229.34 the payor bank warrants that the item was returned within the applicable deadline and that there is no material alteration. Id. § 229.34(a), (b). This provision demonstrates how the warranty theory can be used to deal with situations that have been handled traditionally under non-warranty approaches such as undue retention.

232. R.U.C.C. § 4-208(1); see supra note 183.

both theories. The R.U.C.C. drafters have fashioned a specific warranty to achieve the result that most courts achieve through common law. Our proposal is to follow this approach with respect to the remaining types of mistake cases presently dealt with by restitution. These, of course, are found in R.U.C.C. section 3-419.

The outline of the warranty provisions needed to achieve the objective proposed here is fairly simple. Instead of providing for restitution in certain cases, the drafters can provide for a breach of warranty action in those same cases. The warranty provisions can also incorporate the holder in due course and change of position defenses. It is true that incorporating these defenses will generate some degree of uncertainty in the warranty scheme, but it creates no more uncertainty than exists under the present U.C.C. warranty sections 3-417 and 4-207, which incorporate the holder in due course concept. On balance, the overall treatment of mistake cases will be clarified because the uncertainty that results from doctrinal baggage that comes with a restitutionary claim will be avoided. Care in drafting the warranty provisions will avoid most of the difficulty encountered in reading present U.C.C. sections 3-417 and 4-207. The second step in achieving a unified theory of recovery is abolishing restitution as an alternative theory of recovery in any mistaken payment case governed by the Code. This can be accomplished by specifying that warranty is the exclusive means of recovering any mistaken payment governed by the Code. In other words, restitution should be expressly displaced.

The unified warranty theory of recovery proposed will not only avoid the conflicts between restitution and warranty, it will finally resolve the conflict between the recovery of mistaken payments under restitution and the accountability concept of article 4. U.C.C. section 4-302 and R.U.C.C. section 4-302 both expressly allow a payor bank to assert breach of warranty as a defense in an action based on undue retention. By making warranty the exclusive basis of recovering all mistaken payments, the potential conflict with any restitutionary rights of the payor is eliminated.

234. Adding the change of position defense to the warranty action would change current law. See supra notes 82-83, 91-97, 178 and accompanying text. For cases involving the mistaken payment of a materially altered item, the change is justified. The payee or recipient of a check bearing a material alteration is, unlike a forged indorsement, not in the best position to detect the wrongdoing. Obviously, neither is the payor bank in a good position to detect the alteration. However, once the materially altered item is paid by the payor and the recipient changes his or her position in good faith reliance on the payment, who should bear the loss when the alteration is discovered? As between the payor bank and the recipient of the payment, the equities favor the recipient after the good faith change of position. The few jurisdictions that rejected Price v. Neal nevertheless recognized that a good faith change of position in reliance on the mistaken payment would preclude its recovery by the drawee. See supra note 48 and accompanying text. For an example of a case taking this approach, see First Nat'l Bank v. Bank of Wyndmere, 108 N.W. 546, 549 (N.D. 1906).
CONCLUSION

In the prefatory note to the R.U.C.C., the drafters criticize the Code for following prior law too closely.\textsuperscript{235} The analysis of the R.U.C.C. set forth in Part IV of this Article shows that this same criticism can be leveled against the R.U.C.C. The R.U.C.C. drafters have made essentially the same blunder as the drafters of the Code—incorporating independent and potentially conflicting theories of recovering mistaken payments. As a result, the R.U.C.C. drafters have also failed to clarify adequately the relationship between the article 3 recovery rights and the accountability concept of article 4. The changes they propose are at best superficial, and may actually have worsened the situation by providing for three independent theories of recovery.

The approach outlined in this Article, a unified theory of recovery, can provide a basis for finally resolving the present problems under the Code relating to the recovery of mistaken payments. It will provide a single basis of recovery under article 3. The basis we propose is warranty. At the same time, it will finally provide a way to clarify the relationship between article 3 recovery rights and the accountability concept of article 4. Thus, the current draft of the R.U.C.C. should not be adopted unless the rules for recovering mistaken payments are reconsidered and substantially revised.

\textsuperscript{235} R.U.C.C. Prefatory Note i (July/August Draft, as amended March 15, 1989).