

December 1930

## Banks and Banking--Preferred Claim Against Assets of Insolvent Drawee Band for Collections Made by Charging the Drawer's Account

Melville Stewart  
*West Virginia University College of Law*

Follow this and additional works at: <https://researchrepository.wvu.edu/wvlr>



Part of the [Banking and Finance Law Commons](#)

---

### Recommended Citation

Melville Stewart, *Banks and Banking--Preferred Claim Against Assets of Insolvent Drawee Band for Collections Made by Charging the Drawer's Account*, 37 W. Va. L. Rev. (1930).

Available at: <https://researchrepository.wvu.edu/wvlr/vol37/iss1/6>

This Student Note is brought to you for free and open access by the WVU College of Law at The Research Repository @ WVU. It has been accepted for inclusion in West Virginia Law Review by an authorized editor of The Research Repository @ WVU. For more information, please contact [ian.harmon@mail.wvu.edu](mailto:ian.harmon@mail.wvu.edu).

BANKS AND BANKING — PREFERRED CLAIM AGAINST ASSETS OF INSOLVENT DRAWEE BANK FOR COLLECTIONS MADE BY CHARGING THE DRAWER'S ACCOUNT.—In a recent case,<sup>1</sup> the question was presented whether a forwarding bank should have a preferred claim on the assets of an insolvent drawee bank, there being no mutual accounts between the two banks, when the collection was made by charging and closing the account of a depositor in that bank, a cashier's check being mailed in payment of the collection, which did not get back to the drawee bank before its closing. The court held that there was a collection and that the sum so collected, while awaiting the return of the cashier's check was impressed with a trust in favor of the sending bank.<sup>2</sup>

Theoretically, there is difficulty in reconciling the case with the general view concerning the nature and requisites of a trust. The relation between the collecting bank and the depositor was that of debtor and creditor and the bank clearly had a right to mingle the funds. After the collection, there was no particular fund designated, separated or set aside, and consequently no tangible *res* can be found.<sup>3</sup> If there was a chose in action which could be called a *res* in this case, it would have to be one against the collecting bank and it would be logically impossible for this bank to be trustee of a chose in action against itself.<sup>4</sup>

It would seem that under the modern plan of "reifying funds," bookkeeping is all that is necessary to change the relationship of the parties, a setting aside on the books of the bank being the same as a setting aside in fact. It has been said that the funds are held by the collecting bank, where there are no mutual accounts,

<sup>1</sup> Central Trust Company v. Bank of Mullens, 153 S. E. 145 (W. Va. 1930).

<sup>2</sup> The principles of law applicable to the facts were pronounced at length in Central Trust Company v. Bank of Mullens, 108 W. Va. 12, 150 S. E. 137 (1929).

<sup>3</sup> "It is always necessary to a trust that there should be a particular piece of property or a certain fund, to be held or dealt with in a particular manner for the benefit of another. A debtor cannot create a trust out of a debt which he owes without providing a fund to be applied to the payment of the debt. The relation continues to be that of debtor and creditor, so long as he merely owes the debt and has provided no fund for its payment. The relation may be changed but there must be some particular property or certain fund held for the benefit of the *cestui que trust*." *Marble v. Marble Estate*, 304 Ill. 229, 240, 136 N. E. 589, 594 (1922).

<sup>4</sup> "In no case has it ever been held as yet that a party may by transferring his property from one pocket to another, make himself a trustee." *Van Brunt, P. J. in Govin v. Miranda*, 76 Hun. 414, 419, 27 N. Y. S. 1049, 1052 (1894).

<sup>5</sup> "A debtor cannot be a trustee of its obligation to creditor." *Samuels v. E. F. Drew & Co.*, 296 F. 882 (C. C. A. 2d, 1924).

just the same as if separated, sealed and labeled.<sup>5</sup> It is submitted that the general conceptions of trusts formerly held have undergone some radical changes, at least with respect to banking operations.

Do modern business practices and requirements justify the result in this case, which is reached without regard to the orthodox trust *res* theory?

Until recent years, with but few exceptions, these cases have been decided contrary to the above decision. The trend, however, in the later decisions is toward the view taken in this case.<sup>6</sup> There has been much criticism of these decisions,<sup>7</sup> yet they have increased in number and legislation has been enacted in several states to secure this result.<sup>8</sup>

Banks no longer deal in currency to any great extent.<sup>9</sup> Book credits and commercial paper are employed in place of currency. Payment in collection and remittance transactions is generally made in exchange. Should not this situation be recognized by our courts? By granting preferred claims in collection and remittance cases, commercial paper will circulate more freely and safely, transfer and collection will be more rapid and it would seem to result that business transactions generally are put on a more efficient and settled basis. If refused protection of this kind, to be absolutely secure, forwarding banks will be required to demand remittance in currency, at least where the financial stability of the collecting bank is questioned. In some jurisdictions, collection by debiting accounts is distinguished from collections made in cash or by check on another bank, a trust being said to exist in the latter case.<sup>10</sup> Thus by sending a check to another bank for collection from the bank on which the check is drawn, there may be a

<sup>5</sup> See *Bank of Poplar Bluff v. Frank Millsbaugh*, Commissioner, 313 Mo. 412, 421, 281 S. W. 733, 736 (1926), 47 A. L. R. 754, 759 (1927), quoted in *Central Trust Co. v. Bank of Mullens*, *supra* n. 2, 17.

<sup>6</sup> The cases are collected in notes (1923) 24 A. L. R. 1152; (1926) 42 A. L. R. 754; (1927) 47 A. L. R. 754.

<sup>7</sup> See notes (1923) 72 U. PA. L. REV. 56; (1924) 9 IOWA L. BULL. 134; (1926) 35 YALE L. J. 627; (1926) 75 U. PA. L. REV. 69; (1930) 29 W. VA. L. Q. 297.

<sup>8</sup> Note (1927) 36 YALE L. J. 682, 684; HANDBOOK OF THE NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS AND PROCEEDINGS, (1929) 262, note (1927) 6 N. C. L. REV. 174.

<sup>9</sup> "It has been estimated that from 90% to 95% of all payments made in the United States are made by check rather than in actual money." AMERICAN INSTITUTE OF BANKING, STANDARD BANKING, (1924) 128, quoted from 36 YALE L. J. 683, note.

<sup>10</sup> See *Larabee Flour Mills v. First Nat. Bank*, 13 F. (2d) 330, 47 A. L. R. 764 (C. C. A. 8th, 1926).

preferred claim after collection, if the collecting bank fails. This seems to be a technical distinction and it is thought more desirable that the forwarder be permitted to send his item direct to the drawee bank instead of through a correspondent.<sup>11</sup>

A depositor living in a city in which the bank is located can terminate his relation with the bank by personally presenting his check and receiving currency through the teller's window while the distant depositor must mail his check or place it with another bank for collection. Each account is charged with the amount of the check, but instead of receiving currency, the latter customer is paid with commercial paper, as is customary in present day practice. It would not be illogical to hold that the paper represented so much currency and to treat it as such.

A Uniform Bank Collection Act has been drafted by a committee of the National Commission on Uniform State Laws and Proceedings,<sup>12</sup> and a Bank Collection Code has been recommended by the American Bankers Association<sup>13</sup> for the consideration of Legislatures throughout the country, both presumably developed in the light of present practice and desirability. Each provides that, in the absence of instructions, a payor bank in remitting for an item presented by a customer through the mail, may either send its check or draft upon another bank or the check or draft of any other bank upon any bank other than the drawee or payor of the item.<sup>14</sup> The Collection Code adds that such other method of settlement may be employed as is customary.<sup>15</sup>

---

<sup>11</sup> The following is quoted from an address by PROFESSOR ROSCOE B. TURNER, OF THE YALE LAW SCHOOL, before the National Conference of Commissioners on Uniform State Laws and Proceedings, HANDBOOK OF THE CONFERENCE, *supra* n. 8, 141. "But I think the desirability of sending an item direct to the drawee \* \* \* which is based on a view of the 999 cases rather than the one odd one, should be considered. It will save one day's time in the collection of all paper in circulation, and right today in this country the float, as the banker will call it, that is calculated upon paper in the course of collection is an enormous amount of money. Now if we take the ordinary rule and require that each of these items has to go to a correspondent and then be presented, you have added one more day. That is, you have all the time a million dollars out in circulation for one day more than you would otherwise have if you allowed these items to go direct. But in sending it direct we are subjecting the depositor to a considerable risk. One means of protecting the depositor is to say that if the item has been collected and the proceeds have not been remitted, he is to be allowed a preferred claim out of the assets of the bank which failed."

<sup>12</sup> First Tentative Draft of a Uniform Bank Collection Act, 1929, HANDBOOK, *supra*, n. 8, 253.

<sup>13</sup> Bulletin, Bank Collection Code, Recommended by the American Bankers Association. June 1, 1929. At the time this bulletin went to press, eight States had enacted it into law. Three States have adopted it since that time.

<sup>14</sup> Uniform Collection Act, § 22, HANDBOOK, *supra* n. 8, 261.

<sup>15</sup> Bank Collection Code, § 10, *supra* n. 13, 11.

The Uniform Act further provides that where a payor bank to which an item has been presented by mail for remittance charges the drawer's account or receives payment from him, but closes before making any remittance or made a remittance which has been dishonored upon due presentment, prior parties as their interests may appear will be deemed to have a lien to the amount of the item on the assets of the failed bank other than its previously acquired bank buildings, fixtures and real estate.<sup>16</sup> The Bankers Code differs. It declares that the assets of such drawee or payor shall be impressed with a trust in favor of the owner or owners of such items.<sup>17</sup>

In the instant case, a cashier's check of the payor bank was the medium of payment, while both act and code suggest that the draft or check be drawn on another bank.<sup>18</sup> If the remittance of the drawee bank is to be deemed simply a substitute for currency, where the situation is one for a preference, it would seem immaterial whether a cashier's check or draft is employed.<sup>19</sup>

—MELVILLE STEWART.

---

<sup>16</sup> *Supra* n. 14, § 23.

<sup>17</sup> *Supra* n. 13, § 13, p. 13.

The view expressed in the uniform act seems to be preferable in that there is less theoretical objection to the lien theory.

<sup>18</sup> However, it is to be noted that had the item been charged against the drawer's account and the bank closed before any remittance was made, the drawer would have been deemed to have had a preferred claim. *Supra* notes 16 and 17.

The remitting by collecting bank by cashier's check avails nothing, since it puts the holder in no better condition than he was before and its use is resorted to probably only as a stall.

<sup>19</sup> In the instant case, the court further declares:

"Besides, the drawing and delivery of the cashier's check payable to appellant in payment of the money the bank had collected from Cattaruzza's savings operated as an assignment pro tanto of that sum from the bank's funds."

With this view compare, BRANNAN, NEGOTIABLE INSTRUMENTS LAW, (3d ed. 1920) § 189, p. 407. "When the statute declares that a check of itself does not operate as an assignment, to say that it does in any case is to declare the exact opposite of the statute."

Did the court mean to hold that every holder of a cashier's check has a preferred claim on the assets of an insolvent bank or that it acted as an assignment only when such relation as existed here obtained? The language used by the court in the first Mullens Bank Case, *supra* n. 2, 21, indicates that the court meant to take the latter view and it is submitted that the application of such a doctrine should be confined to cases in which a trust has been declared. Quoting from decision: "Bearing in mind the relationship of the parties, 'the nature of their dealings and attendant circumstances,' it is clear in the instant case that the Bank of Mullens intended a portion of its funds \* \* \* \* should be appropriated to discharge the trust resulting from the proceeds of collection."