

# MAINE STATE LEGISLATURE

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# 115th MAINE LEGISLATURE

## SECOND REGULAR SESSION-1992

Legislative Document

No. 2321

H.P. 1654

House of Representatives, February 11, 1992

Approved for introduction by a majority of the Legislative Council pursuant to Joint Rule 26.  
Reference to the Committee on Judiciary suggested and ordered printed.

EDWIN H. PERT, Clerk

Presented by Representative MARSANO of Belfast.  
Cosponsored by Representative MAYO of Thomaston, Senator CONLEY of Cumberland and  
Senator HOLLOWAY of Lincoln.

STATE OF MAINE

IN THE YEAR OF OUR LORD  
NINETEEN HUNDRED AND NINETY-TWO

An Act to Enact Article 4-A of the Uniform Commercial Code.

Be it enacted by the People of the State of Maine as follows:

2           Sec. 1. 11 MRSA §1-105, sub-§(2), as amended by PL 1977, c.  
4           696, §117, is further amended to read:

6           (2) Where ~~When~~ one of the following provisions of this  
8           Title specifies the applicable law, that provision governs a  
          contrary agreement ~~is-effective~~ only to the extent permitted by  
          the law (including the conflict of laws rules) so specified:

10           Rights of creditors against sold goods. Section 2-402.

12           Applicability of the Article on Bank Deposits and  
14           Collections. Section 4-102.

16           Governing law in the Article on Funds Transfers. Section  
          4-1507.

18           Bulk transfers subject to the Article on Bulk Transfers.  
20           Section 6-102.

22           Applicability of the Article on Investment Securities.  
          Section 8-106.

24           Perfection provisions of the Article on Secured  
26           Transactions. Section 9-103.

28           Sec. 2. 11 MRSA Art. 4-A is enacted to read:

30                           **ARTICLE 4-A**

32                           **FUNDS TRANSFERS**

34                           **PART 1**

36                           **SUBJECT MATTER AND DEFINITIONS**

38                           **§4-1101. Short title**

40                           This Article is known and may be cited as the "Uniform  
42                           Commercial Code - Funds Transfers."

44                           **§4-1102. Subject matter**

46                           Except as otherwise provided in section 4-1108, this Article  
48                           applies to funds transfers defined in section 4-1104.

1991 Uniform Comment

2 Article 4A [Article 4-A] governs a specialized method of  
4 payment referred to in the Article as a funds transfer but also  
6 commonly referred to in the commercial community as a wholesale  
8 wire transfer. A funds transfer is made by means of one or more  
10 payment orders. The scope of Article 4A is determined by the  
12 definitions of "payment order" and "funds transfer" found in  
14 Section 4A-103 [section 4-1103] and Section 4A-104 [section  
16 4-1104].

18 The funds transfer governed by Article 4A [Article 4-A] is  
20 in large part a product of recent and developing technological  
22 changes. Before this Article was drafted there was no  
24 comprehensive body of law - statutory or judicial - that defined  
26 the juridical nature of a funds transfer or the rights and  
28 obligations flowing from payment orders. Judicial authority with  
30 respect to funds transfers is sparse, undeveloped and not  
32 uniform. Judges have had to resolve disputes by referring to  
34 general principles of common law or equity, or they have sought  
36 guidance in statutes such as Article 4 which are applicable to  
38 other payment methods. But attempts to define rights and  
40 obligations in funds transfers by general principles or by  
42 analogy to rights and obligations in negotiable instrument law or  
44 the law of check collection have not been satisfactory.

46 In the drafting of Article 4A [Article 4-A], a deliberate  
48 decision was made to write on a clean slate and to treat a funds  
transfer as a unique method of payment to be governed by unique  
rules that address the particular issues raised by this method of  
payment. A deliberate decision was also made to use precise and  
detailed rules to assign responsibility, define behavioral norms,  
allocate risks and establish limits on liability, rather than to  
rely on broadly stated, flexible principles. In the drafting of  
these rules, a critical consideration was that the various  
parties to funds transfers need to be able to predict risk with  
certainty, to insure against risk, to adjust operational and  
security procedures, and to price funds transfer services  
appropriately. This consideration is particularly important  
given the very large amounts of money that are involved in funds  
transfers.

Funds transfers involve competing interests -- those of  
banks that provide funds transfer services and the commercial and  
financial organizations that use the services, as well as the  
public interest. These competing interests were represented in  
the drafting process and they were thoroughly considered. The  
rules that emerged represent a careful and delicate balancing of  
those interests and are intended to be the exclusive means of  
determining the rights, duties and liabilities of the affected

parties in any situation covered by particular provisions of the  
Article. Consequently, resort to principles of law or equity  
outside of Article 4A [Article 4-A] is not appropriate to create  
rights, duties and liabilities inconsistent with those stated in  
this Article.

§4-1103. Payment order; definitions

(1) In this Article:

(a) "Payment order" means an instruction of a sender to a receiving bank, transmitted orally, electronically or in writing, to pay, or to cause another bank to pay, a fixed or determinable amount of money to a beneficiary if:

(i) The instruction does not state a condition to payment to the beneficiary other than time of payment;

(ii) The receiving bank is to be reimbursed by debiting an account of, or otherwise receiving payment from, the sender; and

(iii) The instruction is transmitted by the sender directly to the receiving bank or to an agent, funds transfer system or communication system for transmittal to the receiving bank;

(b) "Beneficiary" means the person to be paid by the beneficiary's bank;

(c) "Beneficiary's bank" means the bank identified in a payment order in which an account of the beneficiary is to be credited pursuant to the order or which otherwise is to make payment to the beneficiary if the order does not provide for payment to an account;

(d) "Receiving bank" means the bank to which the sender's instruction is addressed; and

(e) "Sender" means the person giving the instruction to the receiving bank.

(2) If an instruction complying with subsection (1), paragraph (a) is to make more than one payment to a beneficiary, the instruction is a separate payment order with respect to each payment.

2 (3) A payment order is issued when it is sent to the  
3 receiving bank.

4 1991 Uniform Comment

6 This section is discussed in the Comment following Section  
7 4A-104 [section 4-1104].

8 §4-1104. Funds transfer: definitions

10 In this Article:

12 (1) "Funds transfer" means the series of transactions,  
14 beginning with the originator's payment order, made for the  
16 purpose of making payment to the beneficiary of the order. The  
18 term includes any payment order issued by the originator's bank  
20 or an intermediary bank intended to carry out the originator's  
22 payment order. A funds transfer is completed by acceptance by  
24 the beneficiary's bank of a payment order for the benefit of the  
26 beneficiary of the originator's payment order.

28 (2) "Intermediary bank" means a receiving bank other than  
30 the originator's bank or the beneficiary's bank.

32 (3) "Originator" means the sender of the first payment  
34 order in a funds transfer; and

36 (4) "Originator's bank" means:

38 (a) The receiving bank to which the payment order of  
40 the originator is issued if the originator is not a  
42 bank; or

44 (b) The originator if the originator is a bank.

46 1991 Uniform Comment

48 1. Article 4A [Article 4-A] governs a method of payment in  
which the person making payment (the "originator") directly  
transmits an instruction to a bank either to make payment to the  
person receiving payment (the "beneficiary") or to instruct some  
other bank to make payment to the beneficiary. The payment from  
the originator to the beneficiary occurs when the bank that is to  
pay the beneficiary becomes obligated to pay the beneficiary.  
There are two basic definitions: "Payment order" stated in  
Section 4A-103 [section 4-1103] and "Funds transfer" stated in  
Section 4A-104 [section 4-1104]. These definitions, other  
related definitions, and the scope of Article 4A [Article 4-A]

2 can best be understood in the context of specific fact  
3 situations. Consider the following cases:

4 Case #1. X, which has an account in Bank A, instructs that  
5 bank to pay \$1,000,000 to Y's account in Bank A. Bank A carries  
6 out X's instruction by making a credit of \$1,000,000 to Y's  
7 account and notifying Y that the credit is available for  
8 immediate withdrawal. The instruction by X to Bank A is a  
9 "payment order" which was issued when it was sent to Bank A.  
10 Section 4A-103(a)(1) and (c) [section 4-1103(1)(a) and (3)]. X  
11 is the "sender" of the payment order and Bank A is the "receiving  
12 bank." Section 4A-103(a)(5) and (a)(4) [section 4-1103(1)(d) and  
13 (e)]. Y is the "beneficiary" of the payment order and Bank A is  
14 the "beneficiary's bank." Section 4A-103(a)(2) and (a)(3)  
15 [section 4-1103(1)(b) and (c)]. When Bank A notified Y of  
16 receipt of the payment order, Bank A "accepted" the payment  
17 order. Section 4A-209(b)(1) [section 4-1209(2)(a)]. When Bank A  
18 accepted the order it incurred an obligation to Y to pay the  
19 amount of the order. Section 4A-404(a) [section 4-1404(1)].  
20 When Bank A accepted X's order, X incurred an obligation to pay  
21 Bank A the amount of the order. Section 4A-402(b) [section  
22 4-1402(2)]. Payment from X to Bank A would normally be made by a  
23 debit to X's account in Bank A. Section 4A-403(a)(3) [section  
24 4-1403(1)(c)]. At the time Bank A incurred the obligation to pay  
25 Y, payment of \$1,000,000 by X to Y was also made. Section  
26 4A-406(a) [section 4-1406(1)]. Bank A paid Y when it gave notice  
27 to Y of a withdrawable credit of \$1,000,000 to Y's account.  
28 Section 4A-405(a) [section 4-1405(1)]. The overall transaction,  
29 which comprises the acts of X and Bank A, in which the payment by  
30 X to Y is accomplished is referred to as the "funds transfer."  
31 Section 4A-104(a) [section 4-1104(1)]. In this case only one  
32 payment order was involved in the funds transfer. A  
33 one-payment-order funds transfer is usually referred to as a  
34 "book transfer" because the payment is accomplished by the  
35 receiving bank's debiting the account of the sender and crediting  
36 the account of the beneficiary in the same bank. X, in addition  
37 to being the sender of the payment order to Bank A, is the  
38 "originator" of the funds transfer. Section 4A-104(c) [section  
39 4-1104(3)]. Bank A is the "originator's bank" in the funds  
40 transfer as well as the beneficiary's bank. Section 4A-104(d)  
41 [section 4-1104(4)].

42 Case #2. Assume the same facts as in Case #1 except that X  
43 instructs Bank A to pay \$1,000,000 to Y's account in Bank B.  
44 With respect to this payment order, X is the sender, Y is the  
45 beneficiary, and Bank A is the receiving bank. Bank A carries  
46 out X's order by instructing Bank B to pay \$1,000,000 to Y's  
47 account. This instruction is a payment order in which Bank A is  
48 the sender, Bank B is the receiving bank, and Y is the

beneficiary. When Bank A issued its payment order to Bank B, Bank A "executed" X's order. Section 4A-301(a) [section 4-1301(1)]. In the funds transfer, X is the originator, Bank A is the originator's bank, and Bank B is the beneficiary's bank. When Bank A executed X's order, X incurred an obligation to pay Bank A the amount of the order. Section 4A-402(c) [section 4-1402(3)]. When Bank B accepts the payment order issued to it by Bank A, Bank B incurs an obligation to Y to pay the amount of the order (Section 4A-404(a) [section 4-1404(1)]) and Bank A incurs an obligation to pay Bank B. Section 4A-402(b) [section 4-1402(2)]. Acceptance by Bank B also results in payment of \$1,000,000 by X to Y. Section 4A-406(a) [section 4-1406(1)]. In this case two payment orders are involved in the funds transfer.

Case #3. Assume the same facts as in Case #2 except that Bank A does not execute X's payment order by issuing a payment order to Bank B. One bank will not normally act to carry out a funds transfer for another bank unless there is a preexisting arrangement between the banks for transmittal of payment orders and settlement of accounts. For example, if Bank B is a foreign bank with which Bank A has no relationship, Bank A can utilize a bank that is a correspondent of both Bank A and Bank B. Assume Bank A issues a payment order to Bank C to pay \$1,000,000 to Y's account in Bank B. With respect to this order, Bank A is the sender, Bank C is the receiving bank, and Y is the beneficiary. Bank C will execute the payment order of Bank A by issuing a payment order to Bank B to pay \$1,000,000 to Y's account in Bank B. With respect to Bank C's payment order, Bank C is the sender, Bank B is the receiving bank, and Y is the beneficiary. Payment of \$1,000,000 by X to Y occurs when Bank B accepts the payment order issued to it by Bank C. In this case the funds transfer involves three payment orders. In the funds transfer, X is the originator, Bank A is the originator's bank, Bank B is the beneficiary's bank, and Bank C is an "intermediary bank." Section 4A-104(b) [section 4-1104(2)]. In some cases there may be more than one intermediary bank, and in those cases each intermediary bank is treated like Bank C in Case # 3.

As the three cases demonstrate, a payment under Article 4A [Article 4-A] involves an overall transaction, the funds transfer, in which the originator, X, is making payment to the beneficiary, Y, but the funds transfer may encompass a series of payment orders that are issued in order to effect the payment initiated by the originator's payment order.

In some cases the originator and the beneficiary may be the same person. This will occur, for example, when a corporation orders a bank to transfer funds from an account of the corporation in that bank to another account of the corporation in

that bank or in some other bank. In some funds transfers the first bank to issue a payment order is a bank that is executing a payment order of a customer that is not a bank. In this case the customer is the originator. In other cases, the first bank to issue a payment order is not acting for a customer, but is making a payment for its own account. In that event the first bank to issue a payment order is the originator as well as the originator's bank.

2. "Payment order" is defined in Section 4A-103(a)(1) [section 4-1103(1)(a)] as an instruction to a bank to pay, or to cause another bank to pay, a fixed or determinable amount of money. The bank to which the instruction is addressed is known as the "receiving bank." Section 4A-103(a)(4) [section 4-1103(1)(d)]. "Bank" is defined in Section 4A-105(a)(2) [section 4-1105(1)(h)]. The effect of this definition is to limit Article 4A [Article 4-A] to payments made through the banking system. A transfer of funds made by an entity outside the banking system is excluded. A transfer of funds through an entity other than a bank is usually a consumer transaction involving relatively small amounts of money and a single contract carried out by transfers of cash or a cash equivalent such as a check. Typically, the transferor delivers cash or a check to the company making the transfer, which agrees to pay a like amount to a person designated by the transferor. Transactions covered by Article 4A [Article 4-A] typically involve very large amounts of money in which several transactions involving several banks may be necessary to carry out the payment. Payments are normally made by debits or credits to bank accounts. Originators and beneficiaries are almost always business organizations and the transfers are usually made to pay obligations. Moreover, these transactions are frequently done on the basis of very short-term credit granted by the receiving bank to the sender of the payment order. Wholesale wire transfers involve policy questions that are distinct from those involved in consumer-based transactions by nonbanks.

3. Further limitations on the scope of Article 4A [Article 4-A] are found in the three requirements found in subparagraphs (i), (ii), and (iii) of Section 4A-103(a)(1) [section 4-1103(1)(a)]. Subparagraph (i) states that the instruction to pay is a payment order only if it "does not state a condition to payment to the beneficiary other than time of payment." An instruction to pay a beneficiary sometimes is subject to a requirement that the beneficiary perform some act such as delivery of documents. For example, a New York bank may have issued a letter of credit in favor of X, a California seller of goods to be shipped to the New York bank's customer in New York. The terms of the letter of credit provide for payment to X if

documents are presented to prove shipment of the goods. Instead of providing for presentment of the documents to the New York bank, the letter of credit states that they may be presented to a California bank that acts as an agent for payment. The New York bank sends an instruction to the California bank to pay X upon presentation of the required documents. The instruction is not covered by Article 4A [Article 4-A] because payment to the beneficiary is conditional upon receipt of shipping documents. The function of banks in a funds transfer under Article 4A [Article 4-A] is comparable to the role of banks in the collection and payment of checks in that it is essentially mechanical in nature. The low price and high speed that characterize funds transfers reflect this fact. Conditions to payment by the California bank other than time of payment impose responsibilities on that bank that go beyond those in Article 4A [Article 4-A] funds transfers. Although the payment by the New York bank to X under the letter of credit is not covered by Article 4A [Article 4-A], if X is paid by the California bank, payment of the obligation of the New York bank to reimburse the California bank could be made by an Article 4A [Article 4-A] funds transfer. In such a case there is a distinction between the payment by the New York bank to X under the letter of credit and the payment by the New York bank to the California bank. For example, if the New York bank pays its reimbursement obligation to the California bank by a Fedwire naming the California bank as beneficiary (see Comment 1 to Section 4A-107 [section 4-1107]), payment is made to the California bank rather than to X. That payment is governed by Article 4A [Article 4-A] and it could be made either before or after payment by the California bank to X. The payment by the New York bank to X under the letter of credit is not governed by Article 4A [Article 4-A] and it occurs when the California bank, as agent of the New York bank, pays X. No payment order was involved in that transaction. In this example, if the New York bank had erroneously sent an instruction to the California bank unconditionally instructing payment to X, the instruction would have been an Article 4A [Article 4-A] payment order. If the payment order was accepted (Section 4A-209(b) [section 4-1209(2)]) by the California bank, a payment by the New York bank to X would have resulted (Section 4A-406(a) [section 4-1406(1)]). But Article 4A [Article 4-A] would not prevent recovery of funds from X on the basis that X was not entitled to retain the funds under the law of mistake and restitution, letter of credit law or other applicable law.

4. Transfers of funds made through the banking system are commonly referred to as either "credit" transfers or "debit" transfers. In a credit transfer the instruction to pay is given by the person making payment. In a debit transfer the instruction to pay is given by the person receiving payment. The

purpose of subparagraph (ii) of subsection (a)(1) of Section 4A-103 [section 4-1103(1)(a)(ii)] is to include credit transfers in Article 4A [Article 4-A] and to exclude debit transfers. All of the instructions to pay in the three cases described in Comment 1 fall within subparagraph (ii). Take Case #2 as an example. With respect to X's instruction given to Bank A, Bank A will be reimbursed by debiting X's account or otherwise receiving payment from X. With respect to Bank A's instruction to Bank B, Bank B will be reimbursed by receiving payment from Bank A. In a debit transfer, a creditor, pursuant to authority from the debtor, is enabled to draw on the debtor's bank account by issuing an instruction to pay to the debtor's bank. If the debtor's bank pays, it will be reimbursed by the debtor rather than by the person giving the instruction. For example, the holder of an insurance policy may pay premiums by authorizing the insurance company to order the policyholder's bank to pay the insurance company. The order to pay may be in the form of a draft covered by Article 3, or it might be an instruction to pay that is not an instrument under that Article. The bank receives reimbursement by debiting the policyholder's account. Or, a subsidiary corporation may make payments to its parent by authorizing the parent to order the subsidiary's bank to pay the parent from the subsidiary's account. These transactions are not covered by Article 4A [Article 4-A] because subparagraph (ii) is not satisfied. Article 4A [Article 4-A] is limited to transactions in which the account to be debited by the receiving bank is that of the person in whose name the instruction is given.

If the beneficiary of a funds transfer is the originator of the transfer, the transfer is governed by Article 4A [Article 4-A] if it is a credit transfer in form. If it is in the form of a debit transfer it is not governed by Article 4A [Article 4-A]. For example, Corporation has accounts in Bank A and Bank B. Corporation instructs Bank A to pay to Corporation's account in Bank B. The funds transfer is governed by Article 4A [Article 4-A]. Sometimes, Corporation will authorize Bank B to draw on Corporation's account in Bank A for the purpose of transferring funds into Corporation's account in Bank B. If Corporation also makes an agreement with Bank A under which Bank A is authorized to follow instructions of Bank B, as agent of Corporation, to transfer funds from Customer's account in Bank A, the instruction of Bank B is a payment order of Customer and is governed by Article 4A [Article 4-A]. This kind of transaction is known in the wire-transfer business as a "drawdown transfer." If Corporation does not make such an agreement with Bank A and Bank B instructs Bank A to make the transfer, the order is in form a debit transfer and is not governed by Article 4A [Article 4-A]. These debit transfers are normally ACH transactions in which Bank

2 A relies on Bank B's warranties pursuant to ACH rules, including  
the warranty that the transfer is authorized.

4 5. The principal effect of subparagraph (iii) of subsection  
6 (a) of Section 4A-103 [section 4-1103(1)(iii)] is to exclude from  
8 Article 4A [Article 4-A] payments made by check or credit card.  
10 In those cases the instruction of the debtor to the bank on which  
12 the check is drawn or to which the credit card slip is to be  
14 presented is contained in the check or credit card slip signed by  
16 the debtor. The instruction is not transmitted by the debtor  
18 directly to the debtor's bank. Rather, the instruction is  
20 delivered or otherwise transmitted by the debtor to the creditor  
22 who then presents it to the bank either directly or through bank  
24 collection channels. These payments are governed by Articles 3  
26 and 4 and federal law. There are, however, limited instances in  
28 which the paper on which a check is printed can be used as the  
30 means of transmitting a payment order that is covered by Article  
32 4A [Article 4-A]. Assume that Originator instructs Originator's  
34 Bank to pay \$10,000 to the account of Beneficiary in  
36 Beneficiary's Bank. Since the amount of Originator's payment  
38 order is small, if Originator's Bank and Beneficiary's Bank do  
not have an account relationship, Originator's Bank may execute  
Originator's order by issuing a teller's check payable to  
Beneficiary's Bank for \$10,000 along with instructions to credit  
Beneficiary's account in that amount. The instruction to  
Beneficiary's Bank to credit Beneficiary's account is a payment  
order. The check is the means by which Originator's Bank pays  
its obligation as sender of the payment order. The instruction  
of Originator's Bank to Beneficiary's Bank might be given in a  
letter accompanying the check or it may be written on the check  
itself. In either case the instruction to Beneficiary's Bank is  
a payment order but the check itself (which is an order to pay  
addressed to the drawee rather than to Beneficiary's Bank) is an  
instrument under Article 3 and is not a payment order. The check  
can be both the means by which Originator's Bank pays its  
obligation under §4A-402(b) [section 4-1402(2)] to Beneficiary's  
Bank and the means by which the instruction to Beneficiary's Bank  
is transmitted.

40 6. Most payments covered by Article 4A [Article 4-A] are  
42 commonly referred to as wire transfers and usually involve some  
44 kind of electronic transmission, but the applicability of Article  
46 4A [Article 4-A] does not depend upon the means used to transmit  
the instruction of the sender. Transmission may be by letter or  
other written communication, oral communication or electronic  
communication. An oral communication is normally given by  
telephone. Frequently the message is recorded by the receiving  
bank to provide evidence of the transaction, but apart from  
problems of proof there is no need to record the oral

2 instruction. Transmission of an instruction may be a direct  
4 communication between the sender and the receiving bank or  
6 through an intermediary such as an agent of the sender, a  
8 communication system such as international cable, or a funds  
transfer system such as CHIPS, SWIFT or an automated  
clearinghouse.

#### 8 §4-1105. Other definitions

##### 10 (1) In this Article:

12 (a) "Authorized account" means a deposit account of a  
14 customer in a bank designated by the customer as a  
16 source of payment of payment orders issued by the  
18 customer to the bank. If a customer does not so  
20 designate an account, any account of the customer is an  
22 authorized account if payment of a payment order from  
24 that account is not inconsistent with a restriction on  
26 the use of that account.

28 (b) "Bank" means a person engaged in the business of  
30 banking and includes a savings bank, savings and loan  
32 association, credit union and trust company. A branch  
34 or separate office of a bank is a separate bank for  
36 purposes of this Article.

38 (c) "Customer" means a person, including a bank,  
40 having an account with a bank or from whom a bank has  
42 agreed to receive payment orders.

44 (d) "Funds transfer business day" of a receiving bank  
46 means the part of a day during which the receiving bank  
is open for the receipt, processing and transmittal of  
payment orders and cancellations and amendments of  
payment orders.

(e) "Funds transfer system" means a wire transfer  
network, automated clearing house or other  
communication system of a clearing house or other  
association of banks through which a payment order by a  
bank may be transmitted to the bank to which the order  
is addressed.

(f) "Good faith" means honesty in fact and the  
observance of reasonable commercial standards of fair  
dealing; and

(g) "Prove" with respect to a fact means to meet the burden of establishing the fact (section 1-201, subsection (8)).

(2) Other definitions applying to this Article and the sections in which they appear are:

"Acceptance"	Section 4-1209
"Beneficiary"	Section 4-1103
"Beneficiary's bank"	Section 4-1103
"Executed"	Section 4-1301
"Execution date"	Section 4-1301
"Funds transfer"	Section 4-1104
"Funds transfer system rule"	Section 4-1501
"Intermediary bank"	Section 4-1104
"Originator"	Section 4-1104
"Originator's bank"	Section 4-1104
"Payment by beneficiary's bank to beneficiary"	Section 4-1405
"Payment by originator to beneficiary"	Section 4-1406
"Payment by sender to receiving bank"	Section 4-1403
"Payment date"	Section 4-1401
"Payment order"	Section 4-1103
"Receiving bank"	Section 4-1103
"Security procedure"	Section 4-1201
"Sender"	Section 4-1103

(3) The following definitions in Article 4 apply to this Article:

"Clearing house"	Section 4-104
"Item"	Section 4-104
"Suspends payments"	Section 4-104

(4) In addition, Article 1 contains general definitions and principles of construction and interpretation applicable throughout this Article.

#### 1991 Uniform Comment

1. The definition of "bank" in subsection (a)(2) [subsection (1)(b)] includes some institutions that are not commercial banks. The definition reflects the fact that many financial institutions now perform functions previously restricted to commercial banks, including acting on behalf of customers in funds transfers. Since many funds transfers involve payment orders to or from foreign countries the definition also

covers foreign banks. The definition also includes Federal Reserve Banks. Funds transfers carried out by Federal Reserve Banks are described in Comments 1 and 2 to Section 4A-107 [section 4-1107].

2. Funds transfer business is frequently transacted by banks outside of general banking hours. Thus, the definition of banking day in Section 4-104(1)(c) cannot be used to describe when a bank is open for funds transfer business. Subsection (a)(4) [subsection (1)(d)] defines a new term, "funds transfer business day," which is applicable to Article 4A [Article 4-A]. The definition states, "is open for the receipt, processing, and transmittal of payment orders and cancellations and amendments of payment orders." In some cases it is possible to electronically transmit payment orders and other communications to a receiving bank at any time. If the receiving bank is not open for the processing of an order when it is received, the communication is stored in the receiving bank's computer for retrieval when the receiving bank is open for processing. The use of the conjunctive makes clear that the defined term is limited to the period during which all functions of the receiving bank can be performed, i.e., receipt, processing, and transmittal of payment orders, cancellations and amendments.

3. Subsection (a)(5) [subsection (1)(e)] defines "funds transfer system." The term includes a system such as CHIPS which provides for transmission of a payment order as well as settlement of the obligation of the sender to pay the order. It also includes automated clearing houses, operated by a clearing house or other association of banks, which process and transmit payment orders of banks to other banks. In addition the term includes organizations that provide only transmission services such as SWIFT. The definition also includes the wire transfer network and automated clearing houses of Federal Reserve Banks. Systems of the Federal Reserve Banks, however, are treated differently from systems of other associations of banks. Funds transfer systems other than systems of the Federal Reserve Banks are treated in Article 4A [Article 4-A] as a means of communication of payment orders between participating banks. Section 4A-206 [section 4-1206]. The Comment to that section and the Comment to Section 4A-107 [section 4-1107] explain how Federal Reserve Banks function under Article 4A [Article 4-A]. Funds transfer systems are also able to promulgate rules binding on participating banks that, under Section 4A-501 [section 4-1501], may supplement or in some cases may even override provisions of Article 4A [Article 4-A].

4. Subsection (d) [subsection (4)] incorporates definitions stated in Article 1 as well as principles of construction and



2 interpretation stated in that Article. Included is Section  
3 1-103. The last paragraph of the Comment to Section 4A-102  
4 [section 4-1102] is addressed to the issue of the extent to which  
5 general principles of law and equity should apply to situations  
6 covered by provisions of Article 4A [Article 4-A].

7 **§4-1106. Time payment order received**

8 (1) The time of receipt of a payment order or communication  
9 cancelling or amending a payment order is determined by the rules  
10 applicable to receipt of a notice stated in section 1-201,  
11 subsection 27. A receiving bank may fix a cut-off time or times  
12 on a funds transfer business day for the receipt and processing  
13 of payment orders and communications cancelling or amending  
14 payment orders. Different cut-off times may apply to payment  
15 orders, cancellations or amendments, or to different categories  
16 of payment orders, cancellations or amendments. A cut-off time  
17 may apply to senders generally or different cut-off times may  
18 apply to different senders or categories of payment orders. If a  
19 payment order or communication cancelling or amending a payment  
20 order is received after the close of a funds transfer business  
21 day or after the appropriate cut-off time on a funds transfer  
22 business day, the receiving bank may treat the payment order or  
23 communication as received at the opening of the next funds  
24 transfer business day.

25 (2) If this Article refers to an execution date or payment  
26 date or states a day on which a receiving bank is required to  
27 take action, and the date or day does not fall on a funds  
28 transfer business day, the next day that is a funds transfer  
29 business day is treated as the date or day stated, unless the  
30 contrary is stated in this Article.

31 **1991 Uniform Comment**

32 The time that a payment order is received by a receiving  
33 bank usually defines the payment date or the execution date of a  
34 payment order. Section 4A-401 [section 4-1401] and Section  
35 4A-301 [section 4-1301]. The time of receipt of a payment order,  
36 or communication cancelling or amending a payment order is  
37 defined in subsection (a) [subsection (1)] by reference to the  
38 rules stated in Section 1-201(27). Thus, time of receipt is  
39 determined by the same rules that determine when a notice is  
40 received. Time of receipt, however, may be altered by a cut-off  
41 time.

42 **§4-1107. Federal reserve regulations and operating circulars**

2 Regulations of the Board of Governors of the Federal Reserve  
3 System and operating circulars of the Federal Reserve Banks  
4 supersede any inconsistent provision of this Article to the  
5 extent of the inconsistency.

6 **1991 Uniform Comment**

7 1. Funds transfers under Article 4A [Article 4-A] may be  
8 made, in whole or in part, by payment orders through a Federal  
9 Reserve Bank in what is usually referred to as a transfer by  
10 Fedwire. If Bank A, which has an account in Federal Reserve Bank  
11 X, wants to pay \$1,000,000 to Bank B, which has an account in  
12 Federal Reserve Bank Y, Bank A can issue an instruction to  
13 Reserve Bank X requesting a debit of \$1,000,000 to Bank A's  
14 Reserve account and an equal credit to Bank B's Reserve account.  
15 Reserve Bank X will debit Bank A's account and will credit the  
16 account of Reserve Bank Y. Reserve Bank X will issue an  
17 instruction to Reserve Bank Y requesting a debit of \$1,000,000 to  
18 the account of Reserve Bank X and an equal credit to Bank B's  
19 account in Reserve Bank Y. Reserve Bank Y will make the  
20 requested debit and credit and will give Bank B an advice of  
21 credit. The definition of "bank" in Section 4A-105(a)(2)  
22 [section 4-1105(1)(b)] includes both Reserve Bank X and Reserve  
23 Bank Y. Bank A's instruction to Reserve Bank X to pay money to  
24 Bank B is a payment order under Section 4A-103(a)(1) [section  
25 4-1103(1)(a)]. Bank A is the sender and Reserve Bank X is the  
26 receiving bank. Bank B is the beneficiary of Bank A's order and  
27 of the funds transfer. Bank A is the originator of the funds  
28 transfer and is also the originator's bank. Section 4A-104(c)  
29 and (d) [section 4-1104(3) and(4)]. Reserve Bank X, an  
30 intermediary bank under Section 4A-104(b) [section 4-1104(2)],  
31 executes Bank A's order by sending a payment order to Reserve  
32 Bank Y instructing that bank to credit the Federal Reserve  
33 account of Bank B. Reserve Bank Y is the beneficiary's bank.

34 Suppose the transfer of funds from Bank A to Bank B is part  
35 of a larger transaction in which Originator, a customer of Bank  
36 A, wants to pay Beneficiary, a customer of Bank B. Originator  
37 issues a payment order to Bank A to pay \$1,000,000 to the account  
38 of Beneficiary in Bank B. Bank A may execute Originator's order  
39 by means of Fedwire which simultaneously transfers \$1,000,000  
40 from Bank A to Bank B and carries a message instructing Bank B to  
41 pay \$1,000,000 to the account of Y. The Fedwire transfer is  
42 carried out as described in the previous paragraph, except that  
43 the beneficiary of the funds transfer is Beneficiary rather than  
44 Bank B. Reserve Bank X and Reserve Bank Y are intermediary  
45 banks. When Reserve Bank Y advises Bank B of the credit to its  
46 Federal Reserve account it will also instruct Bank B to pay to  
47 the account of Beneficiary. The instruction is a payment order

2 to Bank B which is the beneficiary's bank. When Reserve Bank Y  
3 advises Bank B of the credit to its Federal Reserve account Bank  
4 B receives payment of the payment order issued to it by Reserve  
5 Bank Y. Section 4A-403(a)(1) [section 4-1403(1)(a)]. The  
6 payment order is automatically accepted by Bank B at the time it  
7 receives the payment order of Reserve Bank Y. Section  
8 4A-209(b)(2) [section 4-1209(2)(b)]. At the time of acceptance  
9 by Bank B payment by Originator to Beneficiary also occurs.  
10 Thus, in a Fedwire transfer, payment to the beneficiary's bank,  
11 acceptance by the beneficiary's bank and payment by the  
12 originator to the beneficiary all occur simultaneously by  
13 operation of law at the time the payment order to the  
14 beneficiary's bank is received.

15 If Originator orders payment to the account of Beneficiary  
16 in Bank C rather than Bank B, the analysis is somewhat modified.  
17 Bank A may not have any relationship with Bank C and may not be  
18 able to make payment directly to Bank C. In that case, Bank A  
19 could send a Fedwire instructing Bank B to instruct Bank C to pay  
20 Beneficiary. The analysis is the same as the previous case  
21 except that Bank B is an intermediary bank and Bank C is the  
22 beneficiary's bank.

23 2. A funds transfer can also be made through a Federal  
24 Reserve Bank in an automated clearing house transaction. In a  
25 typical case, Originator instructs Originator's Bank to pay to  
26 the account of Beneficiary in Beneficiary's Bank. Originator's  
27 instruction to pay a particular beneficiary is transmitted to  
28 Originator's Bank along with many other instructions for payment  
29 to other beneficiaries by many different beneficiary's banks.  
30 All of these instructions are contained in a magnetic tape or  
31 other electronic device. Transmission of instructions to the  
32 various beneficiary's banks requires that Originator's  
33 instructions be processed and repackaged with instructions of  
34 other originators so that all instructions to a particular  
35 beneficiary's bank are transmitted together to that bank. The  
36 repackaging is done in processing centers usually referred to as  
37 automated clearing houses. Automated clearinghouses are operated  
38 either by Federal Reserve Banks or by other associations of  
39 banks. If Originator's Bank chooses to execute Originator's  
40 instructions by transmitting them to a Federal Reserve Bank for  
41 processing by the Federal Reserve Bank, the transmission to the  
42 Federal Reserve Bank results in the issuance of payment orders by  
43 Originator's Bank to the Federal Reserve Bank, which is an  
44 intermediary bank. Processing by the Federal Reserve Bank will  
45 result in the issuance of payment orders by the Federal Reserve  
46 Bank to Beneficiary's Bank as well as payment orders to other  
47 beneficiary's banks making payments to carry out Originator's  
48 instructions.

2 3. Although the terms of Article 4A [Article 4-A] apply to  
3 funds transfers involving Federal Reserve Banks, federal  
4 preemption would make ineffective any Article 4A [Article 4-A]  
5 provision that conflicts with federal law. The payments  
6 activities of the Federal Reserve Banks are governed by  
7 regulations of the Federal Reserve Board and by operating  
8 circulars issued by the Reserve Banks themselves. In some  
9 instances, the operating circulars are issued pursuant to a  
10 Federal Reserve Board regulation. In other cases, the Reserve  
11 Bank issues the operating circular under its own authority under  
12 the Federal Reserve Act, subject to review by the Federal Reserve  
13 Board. Section 4A-107 [section 4-1107] states that Federal  
14 Reserve Board regulations and operating circulars of the Federal  
15 Reserve Banks supersede any inconsistent provision of Article 4A  
16 [Article 4-A] to the extent of the inconsistency. Federal  
17 Reserve Board regulations, being valid exercises of regulatory  
18 authority pursuant to a federal statute, take precedence over  
19 state law if there is an inconsistency. Childs v. Federal  
20 Reserve Bank of Dallas, 719 F.2d 812 (5th Cir.1983), reh. den.  
21 724 F.2d 127 (5th Cir. 1984). Section 4A-107 [section 4-1107]  
22 treats operating circulars as having the same effect whether  
23 issued under the Reserve Bank's own authority or under a Federal  
24 Reserve Board regulation.

25 §4-1108. Exclusion of consumer transactions governed by federal  
26 law

27 This Article does not apply to a funds transfer any part of  
28 which is governed by the Electronic Fund Transfer Act of 1978  
29 Title XX, Public Law 95-630, 92 Stat. 3728, 15 United States  
30 Code, Section 1693 et seq., as amended.

31 1991 Uniform Comment

32 The Electronic Fund Transfer Act of 1978 is a federal  
33 statute that covers a wide variety of electronic funds transfers  
34 involving consumers. The types of transfers covered by the  
35 federal statute are essentially different from the wholesale wire  
36 transfers that are the primary focus of Article 4A [Article  
37 4-A]. Section 4A-108 [section 4-1108] excludes a funds transfer  
38 from Article 4A [Article 4-A] if any part of the transfer is  
39 covered by the federal law. Existing procedures designed to  
40 comply with federal law will not be affected by Article 4A  
41 [Article 4-A]. The effect of Section 4A-108 [section 4-1108] is  
42 to make Article 4A [Article 4-A] and EFTA mutually exclusive.  
43 For example, if a funds transfer is to a consumer account in the  
44 beneficiary's bank and the funds transfer is made in part by use  
45 of Fedwire and in part by means of an automated clearing house,

2 EFTA applies to the ACH part of the transfer but not to the  
Fedwire part. Under Section 4A-108 [section 4-1108], Article 4A  
4 [Article 4-A] does not apply to any part of the transfer.  
However, in the absence of any law to govern the part of the  
6 funds transfer that is not subject to EFTA, a court might apply  
appropriate principles from Article 4A [Article 4-A] by analogy.

8 **PART 2**

10 **ISSUE AND ACCEPTANCE OF PAYMENT ORDER**

12 **§4-1201. Security procedure**

14 "Security procedure" means a procedure established by  
16 agreement of a customer and a receiving bank for the purpose of:

18 (1) Verifying that a payment order or communication  
amending or cancelling a payment order is that of the customer; or

20 (2) Detecting error in the transmission or the content of  
22 the payment order or communication.

24 A security procedure may require the use of algorithms or  
other codes, identifying words or numbers, encryption, callback  
procedures or similar security devices. Comparison of a  
signature on a payment order or communication with an authorized  
specimen signature of the customer is not by itself a security  
procedure.

30 **1991 Uniform Comment**

32 A large percentage of payment orders and communications  
34 amending or cancelling payment orders are transmitted  
electronically and it is standard practice to use security  
36 procedures that are designed to assure the authenticity of the  
message. Security procedures can also be used to detect error in  
38 the content of messages or to detect payment orders that are  
transmitted by mistake as in the case of multiple transmission of  
the same payment order. Security procedures might also apply to  
40 communications that are transmitted by telephone or in writing.  
Section 4A-201 [section 4-1201] defines these security  
42 procedures. The definition of security procedure limits the term  
to a procedure "established by agreement of a customer and a  
44 receiving bank." The term does not apply to procedure that the  
receiving bank may follow unilaterally in processing payment  
46 orders. The question of whether loss that may result from the  
transmission of a spurious or erroneous payment order will be  
48 borne by the receiving bank or the sender or purported sender is  
affected by whether a security procedure was or was not in effect

2 and whether there was or was not compliance with the procedure.  
Security procedures are referred to in Sections 4A-202 [section  
4-1202] and 4A-203 [section 4-1203], which deal with authorized  
4 and verified payment orders, and Section 4A-205 [section 4-1205],  
which deals with erroneous payment orders.

6 **§4-1202. Authorized and verified payment orders**

8 (1) A payment order received by the receiving bank is the  
10 authorized order of the person identified as sender if that  
person authorized the order or is otherwise bound by it under the  
12 law of agency.

14 (2) If a bank and its customer have agreed that the  
16 authenticity of payment orders issued to the bank in the name of  
the customer as sender will be verified pursuant to a security  
procedure, a payment order received by the receiving bank is  
18 effective as the order of the customer, whether or not  
authorized, if:

20 (a) The security procedure is a commercially reasonable  
22 method of providing security against unauthorized payment  
orders; and

24 (b) The bank proves that it accepted the payment order in  
26 good faith and in compliance with the security procedure and  
any written agreement or instruction of the customer  
restricting acceptance of payment orders issued in the name  
28 of the customer. The bank is not required to follow an  
instruction that violates a written agreement with the  
customer or notice of which is not received at a time and in  
30 a manner affording the bank a reasonable opportunity to act  
32 on it before the payment order is accepted.

34 (3) Commercial reasonableness of a security procedure is a  
36 question of law to be determined by considering the wishes of the  
customer expressed to the bank, the circumstances of the customer  
known to the bank, including the size, type and frequency of  
38 payment orders normally issued by the customer to the bank,  
alternative security procedures offered to the customer and  
security procedures in general use by customers and receiving  
40 banks similarly situated. A security procedure is deemed to be  
42 commercially reasonable if:

44 (a) The security procedure was chosen by the customer after  
46 the bank offered and the customer refused, a security  
procedure that was commercially reasonable for that  
48 customer; and

2 (b) The customer expressly agreed in writing to be bound by  
3 any payment order, whether or not authorized, issued in its  
4 name and accepted by the bank in compliance with the  
5 security procedure chosen by the customer.

6 (4) The term "sender" in this Article includes the customer  
7 in whose name a payment order is issued if the order is the  
8 authorized order of the customer under subsection (1), or it is  
9 effective as the order of the customer under subsection (2).

10 (5) This section applies to amendments and cancellations of  
11 payment orders to the same extent it applies to payment orders.

12 (6) Except as provided in this section and in section  
13 4-1203, subsection (1), paragraph (a), rights and obligations  
14 arising under this section or section 4-1203 may not be varied by  
15 agreement.

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1991 Uniform Comment

This section is discussed in the Comment following Section  
4A-203 [section 4-1203].

**§4-1203. Unenforceability of certain verified payment orders**

(1) If an accepted payment order is not under section  
4-1202, subsection (1) an authorized order of a customer  
identified as sender but is effective as an order of the customer  
pursuant to section 4-1202, subsection (2), the following rules  
apply.

(a) By express written agreement, the receiving bank may  
limit the extent to which it is entitled to enforce or  
retain payment of the payment order.

(b) The receiving bank is not entitled to enforce or retain  
payment of the payment order if the customer proves that the  
order was not caused, directly or indirectly, by a person:

(i) Entrusted at any time with duties to act for the  
customer with respect to payment orders or the security  
procedure or who obtained access to transmitting  
facilities of the customer; or

(ii) Who obtained from a source controlled by the  
customer and without authority of the receiving bank  
information facilitating breach of the security  
procedure, regardless of how the information was  
obtained or whether the customer was at fault.

Information includes any access device, computer  
software or the like.

(2) This section applies to amendments of payment orders to  
the same extent it applies to payment orders.

1991 Uniform Comment

1. Some person will always be identified as the sender of a payment order. Acceptance of the order by the receiving bank is based on a belief by the bank that the order was authorized by the person identified as the sender. If the receiving bank is the beneficiary's bank acceptance means that the receiving bank is obliged to pay the beneficiary. If the receiving bank is not the beneficiary's bank, acceptance means that the receiving bank has executed the sender's order and is obliged to pay the bank that accepted the order issued in execution of the sender's order. In either case the receiving bank may suffer a loss unless it is entitled to enforce payment of the payment order that it accepted. If the person identified as the sender of the order refuses to pay on the ground that the order was not authorized by that person, what are the rights of the receiving bank? In the absence of a statute or agreement that specifically addresses the issue, the question usually will be resolved by the law of agency. In some cases, the law of agency works well. For example, suppose the receiving bank executes a payment order given by means of a letter apparently written by a corporation that is a customer of the bank and apparently signed by an officer of the corporation. If the receiving bank acts solely on the basis of the letter, the corporation is not bound as the sender of the payment order unless the signature was that of the officer and the officer was authorized to act for the corporation in the issuance of payment orders, or some other agency doctrine such as apparent authority or estoppel causes the corporation to be bound. Estoppel can be illustrated by the following example. Suppose P is aware that A, who is unauthorized to act for P, has fraudulently misrepresented to T that A is authorized to act for P. T believes A and is about to rely on the misrepresentation. If P does not notify T of the true facts although P could easily do so, P may be estopped from denying A's lack of authority. A similar result could follow if the failure to notify T is the result of negligence rather than a deliberate decision. Restatement, Second, Agency §8B. Other equitable principles such as subrogation or restitution might also allow a receiving bank to recover with respect to an unauthorized payment order that it accepted. In Gatoll (U.S.A.), Inc. v. Forest Hill State Bank, 1 U.C.C. Rep. Serv.2d 171 (D. Md. 1986), a joint venturer not authorized to order payments from the account of the joint venture, ordered a funds transfer from the account. The transfer

2 paid a bona fide debt of the joint venture. Although the  
transfer was unauthorized the court refused to require recredit  
4 of the account because the joint venture suffered no loss. The  
result can be rationalized on the basis of subrogation of the  
6 receiving bank to the right of the beneficiary of the funds  
transfer to receive the payment from the joint venture.

8 But in most cases these legal principles give the receiving  
bank very little protection in the case of an authorized payment  
10 order. Cases like those just discussed are not typical of the  
way that most payment orders are transmitted and accepted, and  
12 such cases are likely to become even less common. Given the  
large amount of the typical payment order, a prudent receiving  
14 bank will be unwilling to accept a payment order unless it has  
assurance that the order is what it purports to be. This  
16 assurance is normally provided by security procedures described  
in Section 4A-201 [section 4-1201].

18 In a very large percentage of cases covered by Article 4A  
[Article 4-A], transmission of the payment order is made  
20 electronically. The receiving bank may be required to act on the  
basis of a message that appears on a computer screen. Common law  
22 concepts of authority of agent to bind principal are not  
helpful. There is no way of determining the identity or the  
24 authority of the person who caused the message to be sent. The  
receiving bank is not relying on the authority of any particular  
26 person to act for the purported sender. The case is not  
comparable to payment of a check by the drawee bank on the basis  
28 of a signature that is forged. Rather, the receiving bank relies  
on a security procedure pursuant to which the authenticity of the  
30 message can be "tested" by various devices which are designed to  
provide certainty that the message is that of the sender  
32 identified in the payment order. In the wire transfer business  
the concept of "authorized" is different from that found in  
34 agency law. In that business a payment order is treated as the  
order of the person in whose name it is issued if it is properly  
36 tested pursuant to a security procedure and the order passes the  
test.

40 Section 4A-202 [section 4-1202] reflects the reality of the  
wire transfer business. A person in whose name a payment order  
42 is issued is considered to be the sender of the order if the  
order is "authorized" as stated in subsection (a) [subsection  
44 (1)] or if the order is "verified" pursuant to a security  
procedure in compliance with subsection (b) [subsection (2)]. If  
46 subsection (b) [subsection (2)] does not apply, the question of  
whether the customer is responsible for the order is determined  
48 by the law of agency. The issue is one of actual or apparent  
authority of the person who caused the order to be issued in the

2 name of the customer. In some cases the law of agency might  
allow the customer to be bound by an unauthorized order if  
4 conduct of the customer can be used to find an estoppel against  
the customer to deny that the order was unauthorized. If the  
customer is bound by the order under any of these agency  
6 doctrines, subsection (a) [subsection (1)] treats the order as  
authorized and thus the customer is deemed to be the sender of  
8 the order. In most cases, however, subsection (b) [subsection  
(2)] will apply. In that event there is no need to make an  
10 agency law analysis to determine authority. Under Section 4A-202  
[section 4-1202], the issue of liability of the purported sender  
12 of the payment order will be determined by agency law only if the  
receiving bank did not comply with subsection (b) [subsection  
14 (2)].

16 2. The scope of Section 4A-202 [section 4-1202] can be  
illustrated by the following cases.

18 Case #1. A payment order purporting to be that of Customer  
is received by Receiving Bank but the order was fraudulently  
20 transmitted by a person who had no authority to act for  
Customer. Case #2. An authentic payment order was sent by  
22 Customer, but before the order was received by Receiving Bank the  
order was fraudulently altered by an unauthorized person to  
24 change the beneficiary. Case #3. An authentic payment order was  
received by Receiving Bank, but before the order was executed by  
26 Receiving Bank a person who had no authority to act for Customer  
fraudulently sent a communication purporting to amend the order  
28 by changing the beneficiary. In each case Receiving Bank acted  
on the fraudulent communication by accepting the payment order.  
30 These cases are all essentially similar and they are treated  
identically by Section 4A-202 [section 4-1202]. In each case  
32 Receiving Bank acted on a communication that it thought was  
authorized by Customer when in fact the communication was  
34 fraudulent. No distinction is made between Case # 1 in which  
Customer took no part at all in the transaction and Case # 2 and  
36 Case # 3 in which an authentic order was fraudulently altered or  
amended by an unauthorized person. If subsection (b) [subsection  
38 (2)] does not apply, each case is governed by subsection (a)  
[subsection (1)]. If there are no additional facts on which an  
42 estoppel might be found, Customer is not responsible in Case # 1  
for the fraudulently issued payment order, in Case #2 for the  
44 fraudulent alteration or in Case #3 for the fraudulent  
amendment. Thus, in each case Customer is not liable to pay the  
46 order and Receiving Bank takes the loss. The only remedy of  
Receiving Bank is to seek recovery from the person who received  
48 payment as beneficiary of the fraudulent order. If there was  
verification in compliance with subsection (b) [subsection (2)],

Customer will take the loss unless Section 4A-203 [section 4-1203] applies.

3. Subsection (b) of Section 4A-202 [section 4-1202(2)] is based on the assumption that losses due to fraudulent payment orders can best be avoided by the use of commercially reasonable security procedures, and that the use of such procedures should be encouraged. The subsection is designed to protect both the customer and the receiving bank. A receiving bank needs to be able to rely on objective criteria to determine whether it can safely act on a payment order. Employees of the bank can be trained to "test" a payment order according to the various steps specified in the security procedure. The bank is responsible for the acts of these employees. Subsection (b)(ii) [subsection (2)(b)] requires the bank to prove that it accepted the payment order in good faith and "in compliance with the security procedure." If the fraud was not detected because the bank's employee did not perform the acts required by the security procedure, the bank has not complied. Subsection (b)(ii) [subsection (2)(b)] also requires the bank to prove that it complied with any agreement or instruction that restricts acceptance of payment orders issued in the name of the customer. A customer may want to protect itself by imposing limitations on acceptance of payment orders by the bank. For example, the customer may prohibit the bank from accepting a payment order that is not payable from an authorized account, that exceeds the credit balance in specified accounts of the customer, or that exceeds some other amount. Another limitation may relate to the beneficiary. The customer may provide the bank with a list of authorized beneficiaries and prohibit acceptance of any payment order to a beneficiary not appearing on the list. Such limitations may be incorporated into the security procedure itself or they may be covered by a separate agreement or instruction. In either case, the bank must comply with the limitations if the conditions stated in subsection (b) [subsection (2)] are met. Normally limitations on acceptance would be incorporated into an agreement between the customer and the receiving bank, but in some cases the instruction might be unilaterally given by the customer. If standing instructions or an agreement state limitations on the ability of the receiving bank to act, provision must be made for later modification of the limitations. Normally this would be done by an agreement that specifies particular procedures to be followed. Thus, subsection (b) [subsection (2)] states that the receiving bank is not required to follow an instruction that violates a written agreement. The receiving bank is not bound by an instruction unless it has adequate notice of it. Subsections (25), (26) and (27) of Section 1-201 apply.

Subsection (b)(i) [subsection (2)(a)] assures that the interests of the customer will be protected by providing an incentive to a bank to make available to the customer a security procedure that is commercially reasonable. If a commercially reasonable security procedure is not made available to the customer, subsection (b) [subsection (2)] does not apply. The result is that subsection (a) [subsection (1)] applies and the bank acts at its peril in accepting a payment order that may be unauthorized. Prudent banking practice may require that security procedures be utilized in virtually all cases except for those in which personal contact between the customer and the bank eliminates the possibility of an unauthorized order. The burden of making available commercially reasonable security procedures is imposed on receiving banks because they generally determine what security procedures can be used and are in the best position to evaluate the efficacy of procedures offered to customers to combat fraud. The burden on the customer is to supervise its employees to assure compliance with the security procedure and to safeguard confidential security information and access to transmitting facilities so that the security procedure cannot be breached.

4. The principal issue that is likely to arise in litigation involving subsection (b) [subsection (2)] is whether the security procedure in effect when a fraudulent payment order was accepted was commercially reasonable. The concept of what is commercially reasonable in a given case is flexible. Verification entails labor and equipment costs that can vary greatly depending upon the degree of security that is sought. A customer that transmits very large numbers of payment orders in very large amounts may desire and may reasonably expect to be provided with state-of-the-art procedures that provide maximum security. But the expense involved may make use of a state-of-the-art procedure infeasible for a customer that normally transmits payment orders infrequently or in relatively low amounts. Another variable is the type of receiving bank. It is reasonable to require large money center banks to make available state-of-the-art security procedures. On the other hand, the same requirement may not be reasonable for a small country bank. A receiving bank might have several security procedures that are designed to meet the varying needs of different customers. The type of payment order is another variable. For example, in a wholesale wire transfer, each payment order is normally transmitted electronically and individually. A testing procedure will be individually applied to each payment order. In funds transfers to be made by means of an automated clearing house many payment orders are incorporated into an electronic device such as a magnetic tape that is physically delivered. Testing of the individual payment orders

2 is not feasible. Thus, a different kind of security procedure  
3 must be adopted to take into account the different mode of  
4 transmission.

6 The issue of whether a particular security procedure is  
7 commercially reasonable is a question of law. Whether the  
8 receiving bank complied with the procedure is a question of  
9 fact. It is appropriate to make the finding concerning  
10 commercial reasonability a matter of law because security  
11 procedures are likely to be standardized in the banking industry  
12 and a question of law standard leads to more predictability  
13 concerning the level of security that a bank must offer to its  
14 customers. The purpose of subsection (b) [subsection (2)] is to  
15 encourage banks to institute reasonable safeguards against fraud  
16 but not to make them insurers against fraud. A security  
17 procedure is not commercially unreasonable simply because another  
18 procedure might have been better or because the judge deciding  
19 the question would have opted for a more stringent procedure.  
20 The standard is not whether the security procedure is the best  
21 available. Rather it is whether the procedure is reasonable for  
22 the particular customer and the particular bank, which is a lower  
23 standard. On the other hand, a security procedure that fails to  
24 meet prevailing standards of good banking practice applicable to  
25 the particular bank should not be held to be commercially  
26 reasonable. Subsection (c) [subsection (3)] states factors to be  
27 considered by the judge in making the determination of commercial  
28 reasonableness. Sometimes an informed customer refuses a  
29 security procedure that is commercially reasonable and suitable  
30 for that customer and insists on using a higher-risk procedure  
31 because it is more convenient or cheaper. In that case, under  
32 the last sentence of subsection (c) [subsection (3)], the  
33 customer has voluntarily assumed the risk of failure of the  
34 procedure and cannot shift the loss to the bank. But this result  
35 follows only if the customer expressly agrees in writing to  
36 assume that risk. It is implicit in the last sentence of  
37 subsection (c) [subsection (3)] that a bank that accedes to the  
38 wishes of its customer in this regard is not acting in bad faith  
39 by so doing so long as the customer is made aware of the risk.  
40 In all cases, however, a receiving bank cannot get the benefit of  
41 subsection (b) [subsection (2)] unless it has made available to  
42 the customer a security procedure that is commercially reasonable  
43 and suitable for use by that customer. In most cases, the mutual  
44 interest of bank and customer to protect against fraud should  
45 lead to agreement to a security procedure which is commercially  
46 reasonable.

48 5. The effect of Section 4A-202(b) [section 4-1202(2)] is  
to place the risk of loss on the customer if an unauthorized  
payment order is accepted by the receiving bank after

2 verification by the bank in compliance with a commercially  
3 reasonable security procedure. An exception to this result is  
4 provided by Section 4A-203(a)(2) [section 4-1203(1)(b)]. The  
5 customer may avoid the loss resulting from such a payment order  
6 if the customer can prove that the fraud was not committed by a  
7 person described in that subsection. Breach of a commercially  
8 reasonable security procedure requires that the person committing  
9 the fraud have knowledge of how the procedure works and knowledge  
10 of codes, identifying devices, and the like. That person may  
11 also need access to transmitting facilities through an access  
12 device or other software in order to breach the security  
13 procedure. This confidential information must be obtained either  
14 from a source controlled by the customer or from a source  
15 controlled by the receiving bank. If the customer can prove that  
16 the person committing the fraud did not obtain the confidential  
17 information from an agent or former agent of the customer or from  
18 a source controlled by the customer, the loss is shifted to the  
19 bank. "Prove" is defined in Section 4A-105(a)(7) [section  
20 4-1105(1)(g)]. Because of bank regulation requirements, in this  
21 kind of case there will always be a criminal investigation as  
22 well as an internal investigation of the bank to determine the  
23 probable explanation for the breach of security. Because a funds  
24 transfer fraud usually will involve a very large amount of money,  
25 both the criminal investigation and the internal investigation  
26 are likely to be thorough. In some cases there may be an  
27 investigation by bank examiners as well. Frequently, these  
28 investigations will develop evidence of who is at fault and the  
29 cause of the loss. The customer will have access to evidence  
30 developed in these investigations and that evidence can be used  
31 by the customer in meeting its burden of proof.

32 6. The effect of Section 4A-202(b) [section 4-1202(2)] may  
33 also be changed by an agreement meeting the requirements of  
34 Section 4A-203(a)(1) [section 4-1203(1)(a)]. Some customers may  
35 be unwilling to take all or part of the risk of loss with respect  
36 to unauthorized payment orders even if all of the requirements of  
37 Section 4A-202(b) [section 4-1202(2)] are met. By virtue of  
38 Section 4A-203(a)(1) [section 4-1203(1)(a)], a receiving bank may  
39 assume all of the risk of loss with respect to unauthorized  
40 payment orders or the customer and bank may agree that losses  
41 from unauthorized payment orders are to be divided as provided in  
42 the agreement.

44 7. In a large majority of cases the sender of a payment  
45 order is a bank. In many cases in which there is a bank sender,  
46 both the sender and the receiving bank will be members of a funds  
47 transfer system over which the payment order is transmitted.  
48 Since Section 4A-202(f) [section 4-1202(6)] does not prohibit a  
funds transfer system rule from varying rights and obligations

under Section 4A-202 [section 4-1202], a rule of the funds transfer system can determine how loss due to an unauthorized payment order from a participating bank to another participating bank is to be allocated. A funds transfer system rule, however, cannot change the rights of a customer that is not a participating bank. §4A-501(b) [section 4-1501(2)]. Section 4A-202(f) [section 4-1202(6)] also prevents variation by agreement except to the extent stated.

**§4-1204. Refund of payment and duty of customer to report with respect to unauthorized payment order**

(1) If a receiving bank accepts a payment order issued in the name of its customer as sender that is not authorized and not effective as the order of the customer under section 4-1202 or not enforceable in whole or in part, against the customer under section 4-1203, the bank shall refund any payment of the payment order received from the customer to the extent the bank is not entitled to enforce payment and shall pay interest on the refundable amount calculated from the date the bank received payment to the date of the refund. The customer is not entitled to interest from the bank on the amount to be refunded if the customer fails to exercise ordinary care to determine that the order was not authorized by the customer and to notify the bank of the relevant facts within a reasonable time not exceeding 90 days after the date the customer received notification from the bank that the order was accepted or that the customer's account was debited with respect to the order. The bank is not entitled to any recovery from the customer on account of a failure by the customer to give notification as stated in this section.

(2) Reasonable time under subsection (1) may be fixed by agreement as stated in section 1-204, subsection (1), but the obligation of a receiving bank to refund payment as stated in subsection (1) may not otherwise be varied by agreement.

**1991 Uniform Comment**

1. With respect to unauthorized payment orders, in a very large percentage of cases a commercially reasonable security procedure will be in effect. Section 4A-204 [section 4-1204] applies only to cases in which (i) no commercially reasonable security procedure is in effect, (ii) the bank did not comply with a commercially reasonable security procedure that was in effect, (iii) the sender can prove, pursuant to Section 4A-203(a)(2) [section 4-1203(1)(b)], that the culprit did not obtain confidential security information controlled by the customer, or (iv) the bank, pursuant to Section 4A-203(a)(1) [section 4-1203(1)(a)] agreed to take all or part of the loss

resulting from an unauthorized payment order. In each of these cases the bank takes the risk of loss with respect to an unauthorized payment order because the bank is not entitled to payment from the customer with respect to the order. The bank normally debits the customer's account or otherwise receives payment from the customer shortly after acceptance of the payment order. Subsection (a) of Section 4A-204 [section 4-1204(1)] states that the bank must recredit the account or refund payment to the extent the bank is not entitled to enforce payment.

2. Section 4A-204 [section 4-1204] is designed to encourage a customer to promptly notify the receiving bank that it has accepted an unauthorized payment order. Since cases of unauthorized payment orders will almost always involve fraud, the bank's remedy is normally to recover from the beneficiary of the unauthorized order if the beneficiary was party to the fraud. This remedy may not be worth very much and it may not make any difference whether or not the bank promptly learns about the fraud. But in some cases prompt notification may make it easier for the bank to recover some part of its loss from the culprit. The customer will routinely be notified of the debit to its account with respect to an unauthorized order or will otherwise be notified of acceptance of the order. The customer has a duty to exercise ordinary care to determine that the order was unauthorized after it has received notification from the bank, and to advise the bank of the relevant facts within a reasonable time not exceeding 90 days after receipt of notification. Reasonable time is not defined and it may depend on the facts of the particular case. If a payment order for \$1,000,000 is wholly unauthorized, the customer should normally discover it in far less than 90 days. If a \$1,000,000 payment order was authorized but the name of the beneficiary was fraudulently changed, a much longer period may be necessary to discover the fraud. But in any event, if the customer delays more than 90 days the customer's duty has not been met. The only consequence of a failure of the customer to perform this duty is a loss of interest on the refund payable by the bank. A customer that acts promptly is entitled to interest from the time the customer's account was debited or the customer otherwise made payment. The rate of interest is stated in Section 4A-506 [section 4-1506]. If the customer fails to perform the duty, no interest is recoverable for any part of the period before the bank learns that it accepted an unauthorized order. But the bank is not entitled to any recovery from the customer based on negligence for failure to inform the bank. Loss of interest is in the nature of a penalty on the customer designed to provide an incentive for the customer to police its account. There is no intention to impose a duty on the customer that might result in shifting loss from the unauthorized order to the customer.



2 **§4-1205. Erroneous payment orders**

4 (1) If an accepted payment order was transmitted pursuant  
6 to a security procedure for the detection of error and the  
8 payment order erroneously instructed payment to a beneficiary not  
10 intended by the sender, erroneously instructed payment in an  
12 amount greater than the amount intended by the sender or was an  
14 erroneously transmitted duplicate of a payment order previously  
16 sent by the sender, the following rules apply.

18 (a) If the sender proves that the sender or a person acting  
20 on behalf of the sender pursuant to section 4-1206 complied  
22 with the security procedure and that the error would have  
24 been detected if the receiving bank had also complied, the  
26 sender is not obliged to pay the order to the extent stated  
28 in paragraphs (b) and (c).

30 (b) If the funds transfer is completed on the basis of a  
32 payment order that erroneously instructed payment to a  
34 beneficiary not intended by the sender or that was an  
36 erroneously transmitted duplicate of a payment order  
38 previously sent by the sender, the sender is not obliged to  
40 pay the order and the receiving bank is entitled to recover  
42 from the beneficiary any amount paid to the beneficiary to  
44 the extent allowed by the law governing mistake and  
46 restitution.

48 (c) If the funds transfer is completed on the basis of a  
payment order erroneously instructing payment in an amount  
greater than the amount intended by the sender, the sender  
is not obliged to pay the order to the extent the amount  
received by the beneficiary is greater than the amount  
intended by the sender. In that case, the receiving bank is  
entitled to recover from the beneficiary the excess amount  
received to the extent allowed by the law governing mistake  
and restitution.

(2) If the sender of an erroneous payment order described  
in subsection (1) is not obliged to pay all or part of the order,  
and the sender receives notification from the receiving bank that  
the order was accepted by the bank or that the sender's account  
was debited with respect to the order, the sender has a duty to  
exercise ordinary care, on the basis of information available to  
the sender, to discover the error with respect to the order and  
to advise the bank of the relevant facts within a reasonable  
time, not exceeding 90 days, after the bank's notification was  
received by the sender. If the bank proves that the sender  
failed to perform that duty, the sender is liable to the bank for

2 the loss the bank proves it incurred as a result of the failure,  
4 but the liability of the sender may not exceed the amount of the  
6 sender's order.

8 (3) This section applies to amendments to payment orders to  
10 the same extent it applies to payment orders.

12 **1991 Uniform Comment**

14 1. This section concerns error in the content or in the  
16 transmission of payment orders. It deals with three kinds of  
18 error. Case #1. The order identifies a beneficiary not intended  
20 by the sender. For example, Sender intends to wire funds to a  
22 beneficiary identified only by an account number. The wrong  
24 account number is stated in the order. Case #2. The error is in  
26 the amount of the order. For example, Sender intends to wire  
28 \$1,000 to Beneficiary. Through error, the payment order  
instructs payment of \$1,000,000. Case #3. A payment order is  
sent to the receiving bank and then, by mistake, the same payment  
order is sent to the receiving bank again. In Case #3, the  
receiving bank may have no way of knowing whether the second  
order is a duplicate of the first or is another order.  
Similarly, in Case #1 and Case #2, the receiving bank may have no  
way of knowing that the error exists. In each case, if this  
section does not apply and the funds transfer is completed,  
Sender is obliged to pay the order. Section 4A-402 [section  
4-1402]. Sender's remedy, based on payment by mistake, is to  
recover from the beneficiary that received payment.

Sometimes, however, transmission of payment orders of the  
sender to the receiving bank is made pursuant to a security  
procedure designed to detect one or more of the errors described  
above. Since "security procedure" is defined by Section 4A-201  
[section 4-1201] as "a procedure established by agreement of a  
customer and a receiving bank for the purpose of \* \* \* detecting  
error \* \* \*," Section 4A-205 [section 4-1205] does not apply if  
the receiving bank and the customer did not agree to the  
establishment of a procedure for detecting error. A security  
procedure may be designed to detect an account number that is not  
one to which Sender normally makes payment. In that case, the  
security procedure may require a special verification that  
payment to the stated account number was intended. In the case  
of dollar amounts, the security procedure may require different  
codes for different dollar amounts. If a \$1,000,000 payment  
order contains a code that is inappropriate for that amount, the  
error in amount should be detected. In the case of duplicate  
orders, the security procedure may require that each payment  
order be identified by a number or code that applies to no other  
order. If the number or code of each payment order received is

2 registered in a computer base, the receiving bank can quickly  
3 identify a duplicate order. The three cases covered by this  
4 section are essentially similar. In each, if the error is not  
5 detected, some beneficiary will receive funds that the  
6 beneficiary was not intended to receive. If this section  
7 applies, the risk of loss with respect to the error of the sender  
8 is shifted to the bank which has the burden of recovering the  
9 funds from the beneficiary. The risk of loss is shifted to the  
10 bank only if the sender proves that the error would have been  
11 detected if there had been compliance with the procedure and that  
12 the sender (or an agent under Section 4A-206 [section 4-1206])  
13 complied. In the case of a duplicate order or a wrong  
14 beneficiary, the sender doesn't have to pay the order. In the  
15 case of an overpayment, the sender does not have to pay the order  
16 to the extent of the overpayment. If subsection (a)(1)  
17 [subsection (1)(a)] applies, the position of the receiving bank is  
18 comparable to that of a receiving bank that erroneously executes  
19 a payment order as noted in Section 4A-303 [section 4-1303].  
20 However, failure of the sender to timely report the error is  
21 covered by Section 4A-205(b) [section 4-1205(2)] rather than by  
22 Section 4A-304 [section 4-1304] which applies only to erroneous  
23 execution under Section 4A-303 [section 4-1303]. A receiving  
24 bank to which the risk of loss is shifted by subsection (a)(1) or  
25 (2) [subsection (1)(a) or (b)] is entitled to recover the amount  
26 erroneously paid to the beneficiary to the extent allowed by the  
27 law of mistake and restitution. Rights of the receiving bank  
28 against the beneficiary are similar to those of a receiving bank  
29 that erroneously executes a payment order as stated in Section  
30 4A-303 [section 4-1303]. Those rights are discussed in Comment 2  
31 to Section 4A-303 [section 4-1303].

32 2. A security procedure established for the purpose of  
33 detecting error is not effective unless both sender and receiving  
34 bank comply with the procedure. Thus, the bank undertakes a duty  
35 of complying with the procedure for the benefit of the sender.  
36 This duty is recognized in subsection (a)(1) [subsection  
37 (1)(a)]. The loss with respect to the sender's error is shifted  
38 to the bank if the bank fails to comply with the procedure and  
39 the sender (or an agent under Section 4A-206 [section 4-1206])  
40 does comply. Although the customer may have been negligent in  
41 transmitting the erroneous payment order, the loss is put on the  
42 bank on a last-clear-chance theory. A similar analysis applies  
43 to subsection (b) [subsection (2)]. If the loss with respect to  
44 an error is shifted to the receiving bank and the sender is  
45 notified by the bank that the erroneous payment order was  
46 accepted, the sender has a duty to exercise ordinary care to  
47 discover the error and notify the bank of the relevant facts  
48 within a reasonable time not exceeding 90 days. If the bank can  
49 prove that the sender failed in this duty it is entitled to

2 compensation for the loss incurred as a result of the failure.  
3 Whether the bank is entitled to recover from the sender depends  
4 upon whether the failure to give timely notice would have made  
5 any difference. If the bank could not have recovered from the  
6 beneficiary that received payment under the erroneous payment  
7 order even if timely notice had been given, the sender's failure  
8 to notify did not cause any loss of the bank.

9 3. Section 4A-205 [section 4-1205] is subject to variation  
10 by agreement under Section 4A-501 [section 4-1501]. Thus, if a  
11 receiving bank and its customer have agreed to a security  
12 procedure for detection of error, the liability of the receiving  
13 bank for failing to detect an error of the customer as provided  
14 in Section 4A-205 [section 4-1205] may be varied as provided in  
15 an agreement of the bank and the customer.

16 §4-1206. Transmission of payment order through funds transfer or  
17 other communication system

18 (1) If a payment order addressed to a receiving bank is  
19 transmitted to a funds transfer system or other 3rd-party  
20 communication system for transmittal to the bank, the system is  
21 deemed to be an agent of the sender for the purpose of  
22 transmitting the payment order to the bank. If there is a  
23 discrepancy between the terms of the payment order transmitted to  
24 the system and the terms of the payment order transmitted by the  
25 system to the bank, the terms of the payment order of the sender  
26 are those transmitted by the system. This section does not apply  
27 to a funds transfer system of the Federal Reserve Banks.

28 (2) This section applies to cancellations and amendments of  
29 payment orders to the same extent it applies to payment orders.

30 1991 Uniform Comment

31 1. A payment order may be issued to a receiving bank  
32 directly by delivery of a writing or electronic device or by an  
33 oral or electronic communication. If an agent of the sender is  
34 employed to transmit orders on behalf of the sender, the sender  
35 is bound by the order transmitted by the agent on the basis of  
36 agency law. Section 4A-206 [section 4-1206] is an application of  
37 that principle to cases in which a funds transfer or  
38 communication system acts as an intermediary in transmitting the  
39 sender's order to the receiving bank. The intermediary is deemed  
40 to be an agent of the sender for the purpose of transmitting  
41 payment orders and related messages for the sender. Section  
42 4A-206 [section 4-1206] deals with error by the intermediary.

2. Transmission by an automated clearing house of an association of banks other than the Federal Reserve Banks is an example of a transaction covered by Section 4A-206 [section 4-1206]. Suppose Originator orders Originator's Bank to cause a large number of payments to be made to many accounts in banks in various parts of the country. These payment orders are electronically transmitted to Originator's Bank and stored in an electronic device that is held by Originator's Bank. Or, transmission of the various payment orders is made by delivery to Originator's Bank of an electronic device containing the instruction to the bank. In either case the terms of the various payment orders by Originator are determined by the information contained in the electronic device. In order to execute the various orders, the information in the electronic device must be processed. For example, if some of the orders are for payments to accounts in Bank X and some to accounts in Bank Y, Originator's Bank will execute these orders of Originator by issuing a series of payment orders to Bank X covering all payments to accounts in that bank, and by issuing a series of payment orders to Bank Y covering all payments to accounts in that bank. The orders to Bank X may be transmitted together by means of an electronic device, and those to Bank Y may be included in another electronic device. Typically, this processing is done by an automated clearing house acting for a group of banks including Originator's Bank. The automated clearing house is a funds transfer system. Section 4A-105(a)(5) [section 4-1105(1)(e)]. Originator's Bank delivers Originator's electronic device or transmits the information contained in the device to the funds transfer system for processing into payment orders of Originator's Bank to the appropriate beneficiary's banks. The processing may result in an erroneous payment order. Originator's Bank, by use of Originator's electronic device, may have given information to the funds transfer system instructing payment of \$100,000 to an account in Bank X, but because of human error or an equipment malfunction the processing may have converted that instruction into an instruction to Bank X to make a payment of \$1,000,000. Under Section 4A-206 [section 4-1206], Originator's Bank issued a payment order for \$1,000,000 to Bank X when the erroneous information was sent to Bank X. Originator's Bank is responsible for the error of the automated clearing house. The liability of the funds transfer system that made the error is not governed by Article 4A [Article 4-A]. It is left to the law of contract, a funds transfer system rule, or other applicable law.

In the hypothetical case just discussed, if the automated clearing house is operated by a Federal Reserve Bank, the analysis is different. Section 4A-206 [section 4-1206] does not apply. Originator's Bank will execute Originator's payment

orders by delivery or transmission of the electronic information to the Federal Reserve Bank for processing. The result is that Originator's Bank has issued payment orders to the Federal Reserve Bank which, in this case, is acting as an intermediary bank. When the Federal Reserve Bank has processed the information given to it by Originator's Bank it will issue payment orders to the various beneficiary's banks. If the processing results in an erroneous payment order, the Federal Reserve Bank has erroneously executed the payment order of Originator's Bank and the case is governed by Section 4A-303 [section 4-1303].

#### §4-1207. Misdescription of beneficiary

(1) Subject to subsection (2), if, in a payment order received by the beneficiary's bank, the name, bank account number or other identification of the beneficiary refers to a nonexistent or unidentifiable person or account, no person has rights as a beneficiary of the order and acceptance of the order can not occur.

(2) If a payment order received by the beneficiary's bank identifies the beneficiary both by name and by an identifying or bank account number and the name and number identify different persons, the following rules apply.

(a) Except as otherwise provided in subsection (3), if the beneficiary's bank does not know that the name and number refer to different persons, it may rely on the number as the proper identification of the beneficiary of the order. The beneficiary's bank need not determine whether the name and number refer to the same person.

(b) If the beneficiary's bank pays the person identified by name or knows that the name and number identify different persons, no person has rights as beneficiary except the person paid by the beneficiary's bank if that person was entitled to receive payment from the originator of the funds transfer. If no person has rights as beneficiary, acceptance of the order can not occur.

(3) If a payment order described in subsection (2) is accepted, the originator's payment order described the beneficiary inconsistently by name and number and the beneficiary's bank pays the person identified by number as permitted by subsection (2), paragraph (a), the following rules apply.

2 (a) If the originator is a bank, the originator is obliged  
3 to pay its order.

4 (b) If the originator is not a bank and proves that the  
5 person identified by number was not entitled to receive  
6 payment from the originator, the originator is not obliged  
7 to pay its order unless the originator's bank proves that  
8 the originator, before acceptance of the originator's order,  
9 had notice that payment of a payment order issued by the  
10 originator might be made by the beneficiary's bank on the  
11 basis of an identifying or bank account number even if it  
12 identifies a person different from the named beneficiary.  
13 Proof of notice may be made by any admissible evidence. The  
14 originator's bank satisfies the burden of proof if it proves  
15 that the originator, before the payment order was accepted,  
16 signed a writing stating the information to which the notice  
17 relates.

18 (4) In a case governed by subsection (2), paragraph (a), if  
19 the beneficiary's bank rightfully pays the person identified by  
20 number and that person was not entitled to receive payment from  
21 the originator, the amount paid may be recovered from that person  
22 to the extent allowed by the law governing mistake and  
23 restitution as follows.

24 (a) If the originator is obliged to pay its payment order  
25 as stated in subsection (3), the originator has the right to  
26 recover.

27 (b) If the originator is not a bank and is not obliged to  
28 pay its payment order, the originator's bank has the right  
29 to recover.

30 **1991 Uniform Comment**

31 1. Subsection (a) [subsection (1)] deals with the problem  
32 of payment orders issued to the beneficiary's bank for payment to  
33 nonexistent or unidentifiable persons or accounts. Since it is  
34 not possible in that case for the funds transfer to be completed,  
35 subsection (a) [subsection (1)] states that the order cannot be  
36 accepted. Under Section 4A-402(c) [section 4-1402(3)], a sender  
37 of a payment order is not obliged to pay its order unless the  
38 beneficiary's bank accepts a payment order instructing payment to  
39 the beneficiary of that sender's order. Thus, if the beneficiary  
40 of a funds transfer is nonexistent or unidentifiable, each sender  
41 in the funds transfer that has paid its payment order is entitled  
42 to get its money back.

2 2. Subsection (b) [subsection (2)], which takes precedence  
3 over subsection (a) [subsection (1)], deals with the problem of  
4 payment orders in which the description of the beneficiary does  
5 not allow identification of the beneficiary because the  
6 beneficiary is described by name and by an identifying number or  
7 an account number and the name and number refer to different  
8 persons. A very large percentage of payment orders issued to the  
9 beneficiary's bank by another bank are processed by automated  
10 means using machines capable of reading orders on standard  
11 formats that identify the beneficiary by an identifying number or  
12 the number of a bank account. The processing of the order by the  
13 beneficiary's bank and the crediting of the beneficiary's account  
14 are done by use of the identifying or bank account number without  
15 human reading of the payment order itself. The process is  
16 comparable to that used in automated payment of checks. The  
17 standard format, however, may also allow the inclusion of the  
18 name of the beneficiary and other information which can be useful  
19 to the beneficiary's bank and the beneficiary but which plays no  
20 part in the process of payment. If the beneficiary's bank has  
21 both the account number and name of the beneficiary supplied by  
22 the originator of the funds transfer, it is possible for the  
23 beneficiary's bank to determine whether the name and number refer  
24 to the same person, but if a duty to make that determination is  
25 imposed on the beneficiary's bank the benefits of automated  
26 payment are lost. Manual handling of payment orders is both  
27 expensive and subject to human error. If payment orders can be  
28 handled on an automated basis there are substantial economies of  
29 operation and the possibility of clerical error is reduced.  
30 Subsection (b) [subsection (2)] allows banks to utilize automated  
31 processing by allowing banks to act on the basis of the number  
32 without regard to the name if the bank does not know that the  
33 name and number refer to different persons. "Know" is defined in  
34 Section 1-201(25) to mean actual knowledge, and Section 1-201(27)  
35 states rules for determining when an organization has knowledge  
36 of information received by the organization. The time of payment  
37 is the pertinent time at which knowledge or lack of knowledge  
38 must be determined.

39 Although the clear trend is for beneficiary's banks to  
40 process payment orders by automated means, Section 4A-207  
41 [section 4-1207] is not limited to cases in which processing is  
42 done by automated means. A bank that processes by semi-automated  
43 means or even manually may rely on number as stated in Section  
44 4A-207 [section 4-1207].

45 In cases covered by subsection (b) [subsection (2)] the  
46 erroneous identification would in virtually all cases be the  
47 identifying or bank account number. In the typical case the  
48 error is made by the originator of the funds transfer. The

2 originator should know the name of the person who is to receive  
3 payment and can further identify that person by an address that  
4 would normally be known to the originator. It is not unlikely,  
5 however, that the originator may not be sure whether the  
6 identifying or account number refers to the person the originator  
7 intends to pay. Subsection (b)(1) [subsection (2)(a)] deals with  
8 the typical case in which the beneficiary's bank pays on the  
9 basis of the account number and is not aware at the time of  
10 payment that the named beneficiary is not the holder of the  
11 account which was paid. In some cases the false number will be  
12 the result of error by the originator. In other cases fraud is  
13 involved. For example, Doe is the holder of shares in Mutual  
14 Fund. Thief, impersonating Doe, requests redemption of the  
15 shares and directs Mutual Fund to wire the redemption proceeds to  
16 Doe's account #12345 in Beneficiary's Bank. Mutual Fund  
17 originates a funds transfer by issuing a payment order to  
18 Originator's Bank to make the payment to Doe's account #12345 in  
19 Beneficiary's Bank. Originator's Bank executes the order by  
20 issuing a conforming payment order to Beneficiary's Bank which  
21 makes payment to account #12345. That account is the account of  
22 Roe rather than Doe. Roe might be a person acting in concert  
23 with Thief or Roe might be an innocent third party. Assume that  
24 Roe is a gem merchant that agreed to sell gems to Thief who  
25 agreed to wire the purchase price to Roe's account in  
26 Beneficiary's Bank. Roe believed that the credit to Roe's  
27 account was a transfer of funds from Thief and released the gems  
28 to Thief in good faith in reliance on the payment. The case law  
29 is unclear on the responsibility of a beneficiary's bank in  
30 carrying out a payment order in which the identification of the  
31 beneficiary by name and number is conflicting. See Securities  
32 Fund Services, Inc. v. American National Bank, 542 F.Supp. 323  
33 (N.D. Ill. 1982) and Bradford Trust Co. v. Texas American Bank,  
34 790 F.2d 407 (5th Cir.1986). Section 4A-207 [section 4-1207]  
35 resolves the issue.

36 If Beneficiary's Bank did not know about the conflict  
37 between the name and number, subsection (b)(1) [subsection  
38 (2)(a)] applies. Beneficiary's Bank has no duty to determine  
39 whether there is a conflict and it may rely on the number as the  
40 proper identification of the beneficiary of the order. When it  
41 accepts the order, it is entitled to payment from Originator's  
42 Bank. Section 4A-402(b) [section 4-1402]. On the other hand, if  
43 Beneficiary's Bank knew about the conflict between the name and  
44 number and nevertheless paid Roe, subsection (b)(2) [subsection  
45 (2)(b)] applies. Under that provision, acceptance of the payment  
46 order of Originator's Bank did not occur because there is no  
47 beneficiary of that order. Since acceptance did not occur  
48 Originator's Bank is not obliged to pay Beneficiary's Bank.  
Section 4A-402(b) [section 4-1402(2)]. Similarly, Mutual Fund is

2 excused from its obligation to pay Originator's Bank. Section  
3 4A-402(c) [section 4-1402(3)]. Thus, Beneficiary's Bank takes  
4 the loss. Its only cause of action is against Thief. Roe is not  
5 obliged to return the payment to the beneficiary's bank because  
6 Roe received the payment in good faith and for value. Article 4A  
7 [Article 4-A] makes irrelevant the issue of whether Mutual Fund  
8 was or was not negligent in issuing its payment order.

9 3. Normally, subsection (b)(1) [subsection (2)(a)] will  
10 apply to the hypothetical case discussed in Comment 2.  
11 Beneficiary's Bank will pay on the basis of the number without  
12 knowledge of the conflict. In that case subsection (c)  
13 [subsection (3)] places the loss on either Mutual Fund or  
14 Originator's Bank. It is not unfair to assign the loss to Mutual  
15 Fund because it is the person who dealt with the imposter and it  
16 supplied the wrong account number. It could have avoided the  
17 loss if it had not used an account number that it was not sure  
18 was that of Doe. Mutual Fund, however, may not have been aware  
19 of the risk involved in giving both name and number. Subsection  
20 (c) [subsection (3)] is designed to protect the originator,  
21 Mutual Fund, in this case. Under that subsection, the originator  
22 is responsible for the inconsistent description of the  
23 beneficiary if it had notice that the order might be paid by the  
24 beneficiary's bank on the basis of the number. If the originator  
25 is a bank, the originator always has that responsibility. The  
26 rationale is that any bank should know how payment orders are  
27 processed and paid. If the originator is not a bank, the  
28 originator's bank must prove that its customer, the originator,  
29 had notice. Notice can be proved by any admissible evidence, but  
30 the bank can always prove notice by providing the customer with a  
31 written statement of the required information and obtaining the  
32 customer's signature to the statement. That statement will then  
33 apply to any payment order accepted by the bank thereafter. The  
34 information need not be supplied more than once.

35 In the hypothetical case if Originator's Bank made the  
36 disclosure stated in the last sentence of subsection (c)(2)  
37 [subsection (3)(b)], Mutual Fund must pay Originator's Bank.  
38 Under subsection (d)(1) [subsection (4)(a)], Mutual Fund has an  
39 action to recover from Roe if recovery from Roe is permitted by  
40 the law governing mistake and restitution. Under the assumed  
41 facts Roe should be entitled to keep the money as a person who  
42 took it in good faith and for value since it was taken as payment  
43 for the gems. In that case, Mutual Fund's only remedy is against  
44 Thief. If Roe was not acting in good faith, Roe has to return  
45 the money to Mutual Fund. If Originator's Bank does not prove  
46 that Mutual Fund had notice as stated in subsection (c)(2)  
47 [subsection (3)(b)], Mutual Fund is not required to pay  
48 Originator's Bank. Thus, the risk of loss falls on Originator's

Bank whose remedy is against Roe or Thief as stated above.  
Subsection (d)(2) [subsection (4)(b)].

**§4-1208. Misdescription of intermediary bank or beneficiary's bank**

(1) This subsection applies to a payment order identifying an intermediary bank or the beneficiary's bank only by an identifying number.

(a) The receiving bank may rely on the number as the proper identification of the intermediary or beneficiary's bank and need not determine whether the number identifies a bank.

(b) The sender is obliged to compensate the receiving bank for any loss and expenses incurred by the receiving bank as a result of its reliance on the number in executing or attempting to execute the order.

(2) This subsection applies to a payment order identifying an intermediary bank or the beneficiary's bank both by name and an identifying number if the name and number identify different persons.

(a) If the sender is a bank, the receiving bank may rely on the number as the proper identification of the intermediary or beneficiary's bank if the receiving bank, when it executes the sender's order, does not know that the name and number identify different persons. The receiving bank need not determine whether the name and number refer to the same person or whether the number refers to a bank. The sender is obliged to compensate the receiving bank for any loss and expenses incurred by the receiving bank as a result of its reliance on the number in executing or attempting to execute the order.

(b) If the sender is not a bank and the receiving bank proves that the sender, before the payment order was accepted, had notice that the receiving bank might rely on the number as the proper identification of the intermediary or beneficiary's bank even if it identifies a person different from the bank identified by name, the rights and obligations of the sender and the receiving bank are governed by paragraph (a), as though the sender were a bank. Proof of notice may be made by any admissible evidence. The receiving bank satisfies the burden of proof if it proves that the sender, before the payment order was accepted, signed a writing stating the information to which the notice relates.

(c) Regardless of whether the sender is a bank, the receiving bank may rely on the name as the proper identification of the intermediary or beneficiary's bank if the receiving bank, at the time it executes the sender's order, does not know that the name and number identify different persons. The receiving bank need not determine whether the name and number refer to the same person.

(d) If the receiving bank knows that the name and number identify different persons, reliance on either the name or the number in executing the sender's payment order is a breach of the obligation stated in section 4-1302, subsection (1), paragraph (a).

**1991 Uniform Comment**

1. This section addresses an issue similar to that addressed by Section 4A-207 [section 4-1207]. Because of automation in the processing of payment orders, a payment order may identify the beneficiary's bank or an intermediary bank by an identifying number. The bank identified by number might or might not also be identified by name. The following two cases illustrate Section 4A-208(a) and (b) [section 4-1208(1) and (2)]:

Case #1. Originator's payment order to Originator's Bank identifies the beneficiary's bank as Bank A and instructs payment to Account #12345 in that bank. Originator's Bank executes Originator's order by issuing a payment order to Intermediary Bank. In the payment order of Originator's Bank the beneficiary's bank is identified as Bank A but is also identified by number, #67890. The identifying number refers to Bank B rather than Bank A. If processing by Intermediary Bank of the payment order of Originator's Bank is done by automated means, Intermediary Bank, in executing the order, will rely on the identifying number and will issue a payment order to Bank B rather than Bank A. If there is an Account # 12345 in Bank B, the payment order of Intermediary Bank would normally be accepted and payment would be made to a person not intended by Originator. In this case, Section 4A-208(b)(1) [section 4-1208(2)(a)] puts the risk of loss on Originator's Bank. Intermediary Bank may rely on the number #67890 as the proper identification of the beneficiary's bank. Intermediary Bank has properly executed the payment order of Originator's Bank. By using the wrong number to describe the beneficiary's bank, Originator's Bank has improperly executed Originator's payment order because the payment order of Originator's Bank provides for payment to the wrong beneficiary, the holder of Account #12345 in Bank B rather than the holder of Account # 12345 in Bank A.

2 Section 4A-302(a)(2) [section 4-1302(1)(b)] and Section 4A-303(c)  
3 [section 4-1303(3)]. Originator's Bank is not entitled to  
4 payment from Originator but is required to pay Intermediary  
5 Bank. Section 4A-303(c) [section 4-1303(3)] and Section  
6 4A-402(c) [section 4-1402(3)]. Intermediary Bank is also  
7 entitled to compensation for any loss and expenses resulting from  
8 the error by Originator's Bank.

9 If there is no Account # 12345 in Bank B, the result is that  
10 there is no beneficiary of the payment order issued by  
11 Originator's Bank and the funds transfer will not be completed.  
12 Originator's Bank is not entitled to payment from Originator and  
13 Intermediary Bank is not entitled to payment from Originator's  
14 Bank. Section 4A-402(c) [section 4-1402(3)]. Since Originator's  
15 Bank improperly executed Originator's payment order it may be  
16 liable for damages under Section 4A-305 [section 4-1305]. As  
17 stated above, Intermediary Bank is entitled to compensation for  
18 loss and expenses resulting from the error by Originator's Bank.

19 Case #2. Suppose the same payment order by Originator to  
20 Originator's Bank as in Case # 1. In executing the payment order  
21 Originator's Bank issues a payment order to Intermediary Bank in  
22 which the beneficiary's bank is identified only by number,  
23 #67890. That number does not refer to Bank A. Rather, it  
24 identifies a person that is not a bank. If Processing by  
25 Intermediary Bank of the payment order of Originator's Bank is  
26 done by automated means, Intermediary Bank will rely on the  
27 number #67890 to identify the beneficiary's bank. Intermediary  
28 Bank has no duty to determine whether the number identifies a  
29 bank. The funds transfer cannot be completed in this case  
30 because no bank is identified as the beneficiary's bank.  
31 Subsection (a) [subsection (1)] puts the risk of loss on  
32 Originator's Bank. Originator's Bank is not entitled to payment  
33 from Originator. Section 4A-402(c) [section 4-1402(3)].  
34 Originator's Bank has improperly executed Originator's payment  
35 order and may be liable for damages under Section 4A-305 [section  
36 4-1305]. Originator's Bank is obliged to compensate Intermediary  
37 Bank for loss and expenses resulting from the error by  
38 Originator's Bank.

39 Subsection (a) [subsection (1)] also applies if #67890  
40 identifies a bank, but the bank is not Bank A. Intermediary Bank  
41 may rely on the number as the proper identification of the  
42 beneficiary's bank. If the bank to which Intermediary Bank sends  
43 its payment order accepts the order, Intermediary Bank is  
44 entitled to payment from Originator's Bank, but Originator's Bank  
45 is not entitled to payment from Originator. The analysis is  
46 similar to that in Case # 1.

2 2. Subsection (b)(2) [subsection (2)(b)] of Section 4A-208  
3 [section 4-1208] addresses cases in which an erroneous  
4 identification of a beneficiary's bank or intermediary bank by  
5 name and number is made in a payment order of a sender that is  
6 not a bank. Suppose Originator issues a payment order to  
7 Originator's Bank that instructs that bank to use an intermediary  
8 bank identified as Bank A and by an identifying number, #67890.  
9 The identifying number refers to Bank B. Originator intended to  
10 identify Bank A as intermediary bank. If Originator's Bank  
11 relied on the number and issued a payment order to Bank B the  
12 rights of Originator's Bank depend upon whether the proof of  
13 notice stated in subsection (b)(2) [subsection (2)(b)] is made by  
14 Originator's Bank. If proof is made, Originator's Bank's rights  
15 are governed by subsection (b)(1) [subsection (2)(a)] of Section  
16 4A-208 [section 4-1208]. Originator's Bank is not liable for  
17 breach of Section 4A-302(a)(1) [section 4-1302(1)(a)] and is  
18 entitled to compensation from Originator for any loss and  
19 expenses resulting from Originator's error. If notice is not  
20 proved, Originator's Bank may not rely on the number in executing  
21 Originator's payment order. Since Originator's Bank does not get  
22 the benefit of subsection (b)(1) [subsection (2)(a)] in that  
23 case, Originator's Bank improperly executed Originator's payment  
24 order and is in breach of the obligation stated in Section  
25 4A-302(a)(1) [section 4-1302(1)(a)]. If notice is not given,  
26 Originator's Bank can rely on the name if it is not aware of the  
27 conflict in name and number. Subsection (b)(3) [subsection  
28 (2)(c)].

29 3. Although the principal purpose of Section 4A-208  
30 [section 4-1208] is to accommodate automated processing of  
31 payment orders, Section 4A-208 [section 4-1208] applies  
32 regardless of whether processing is done by automation,  
33 semi-automated means or manually.

#### 34 §4-1209. Acceptance of payment order

35 (1) Subject to subsection (4), a receiving bank other than  
36 the beneficiary's bank accepts a payment order when it executes  
37 the order.

38 (2) Subject to subsections (3) and (4), a beneficiary's  
39 bank accepts a payment order at the earliest of the following  
40 times:

41 (a) When the bank pays the beneficiary as stated in section  
42 4-1405, subsection (1) or (2), or notifies the beneficiary  
43 of receipt of the order or that the account of the  
44 beneficiary has been credited with respect to the order  
45 unless the notice indicates that the bank is rejecting the  
46 order.

2 order or that funds with respect to the order may not be  
4 withdrawn or used until receipt of payment from the sender  
6 of the order.

8 (b) When the bank receives payment of the entire amount of  
10 the sender's order pursuant to section 4-1403, subsection  
12 (1), paragraph (a) or (b); or

14 (c) The opening of the next funds transfer business day of  
16 the bank following the payment date of the order if at that  
18 time, the amount of the sender's order is fully covered by a  
20 withdrawable credit balance in an authorized account of the  
22 sender or the bank has otherwise received full payment from  
24 the sender, unless the order was rejected before that time  
26 or is rejected within one hour after that time or one hour  
28 after the opening of the next business day of the sender  
30 following the payment date if that time is later. If notice  
32 of rejection is received by the sender after the payment  
34 date and the authorized account of the sender does not bear  
36 interest, the bank is obliged to pay interest to the sender  
38 on the amount of the order for the number of days elapsing  
40 after the payment date to the day the sender receives notice  
42 or learns that the order was not accepted, counting that day  
44 as an elapsed day. If the withdrawable credit balance  
46 during that period falls below the amount of the order, the  
48 amount of interest payable is reduced accordingly.

2 (3) Acceptance of a payment order can not occur before the  
4 order is received by the receiving bank. Acceptance does not  
6 occur under subsection (2), paragraph (b) or (c) if the  
8 beneficiary of the payment order does not have an account with  
10 the receiving bank, the account has been closed or the receiving  
12 bank is not permitted by law to receive credits for the  
14 beneficiary's account.

16 (4) A payment order issued to the originator's bank can not  
18 be accepted until the payment date if the bank is the  
20 beneficiary's bank or the execution date if the bank is not the  
22 beneficiary's bank. If the originator's bank executes the  
24 originator's payment order before the execution date or pays the  
26 beneficiary of the originator's payment order before the payment  
28 date and the payment order is subsequently canceled pursuant to  
30 section 4-1211, subsection (2), the bank may recover from the  
32 beneficiary any payment received to the extent allowed by the law  
34 governing mistake and restitution.

1991 Uniform Comment

2 1. This section treats the sender's payment order as a  
4 request by the sender to the receiving bank to execute or pay the  
6 order and that request can be accepted or rejected by the  
8 receiving bank. Section 4A-209 [section 4-1209] defines when  
10 acceptance occurs. Section 4A-210 [section 4-1210] covers  
12 rejection. Acceptance of the payment order imposes an obligation  
14 on the receiving bank to the sender if the receiving bank is not  
16 the beneficiary's bank, or to the beneficiary if the receiving  
18 bank is the beneficiary's bank. These obligations are stated in  
20 Section 4A-302 [section 4-1302] and Section 4A-404 [section  
22 4-1404].

24 2. Acceptance by a receiving bank other than the  
26 beneficiary's bank is defined in Section 4A-209(a) [section  
28 4-1209(1)]. That subsection states the only way that a bank  
30 other than the beneficiary's bank can accept a payment order. A  
32 payment order to a bank other than the beneficiary's bank is, in  
34 effect, a request that the receiving bank execute the sender's  
36 order by issuing a payment order to the beneficiary's bank or to  
38 an intermediary bank. Normally, acceptance occurs at the time of  
40 execution, but there is an exception stated in subsection (d)  
42 [subsection (4)] and discussed in Comment 9. Execution occurs  
44 when the receiving bank "issues a payment order intended to carry  
46 out" the sender's order. Section 4A-301(a) [section 4-1301(1)].  
48 In some cases the payment order issued by the receiving bank may  
not conform to the sender's order. For example, the receiving  
bank might make a mistake in the amount of its order, or the  
order might be issued to the wrong beneficiary's bank or for the  
benefit of the wrong beneficiary. In all of these cases there is  
acceptance of the sender's order by the bank when the receiving  
bank issues its order intended to carry out the sender's order,  
even though the bank's payment order does not in fact carry out  
the instruction of the sender. Improper execution of the  
sender's order may lead to liability to the sender for damages or  
it may mean that the sender is not obliged to pay its payment  
order. These matters are covered in Section 4A-303 [section  
4-1303], Section 4A-305 [section 4-1305], and Section 4A-402  
[section 4-1402].

3. A receiving bank has no duty to accept a payment order  
unless the bank makes an agreement, either before or after  
issuance of the payment order, to accept it, or acceptance is  
required by a funds transfer system rule. If the bank makes such  
an agreement it incurs a contractual obligation based on the  
agreement and may be held liable for breach of contract if a  
failure to execute violates the agreement. In many cases a bank  
will enter into an agreement with its customer to govern the  
rights and obligations of the parties with respect to payment  
orders issued to the bank by the customer or, in cases in which



2 the sender is also a bank, there may be a funds transfer system  
3 rule that governs the obligations of a receiving bank with  
4 respect to payment orders transmitted over the system. Such  
5 agreements or rules can specify the circumstances under which a  
6 receiving bank is obliged to execute a payment order and can  
7 define the extent of liability of the receiving bank for breach  
8 of the agreement or rule. Section 4A-305(d) [section 4-1305(4)]  
9 states the liability for breach of an agreement to execute a  
10 payment order.

11 4. In the case of a payment order issued to the  
12 beneficiary's bank, acceptance is defined in Section 4A-209(b)  
13 [section 4-1209(2)]. The function of a beneficiary's bank that  
14 receives a payment order is different from that of a receiving  
15 bank that receives a payment order for execution. In the typical  
16 case, the beneficiary's bank simply receives payment from the  
17 sender of the order, credits the account of the beneficiary and  
18 notifies the beneficiary of the credit. Acceptance by the  
19 beneficiary's bank does not create any obligation to the sender.  
20 Acceptance by the beneficiary's bank means that the bank is  
21 liable to the beneficiary for the amount of the order. Section  
22 4A-404(a) [section 4-1404(1)]. There are three ways in which the  
23 beneficiary's bank can accept a payment order which are described  
24 in the following comments.

25 5. Under Section 4A-209(b)(1) [section 4-1209(2)(a)], the  
26 beneficiary's bank can accept a payment order by paying the  
27 beneficiary. In the normal case of crediting an account of the  
28 beneficiary, payment occurs when the beneficiary is given notice  
29 of the right to withdraw the credit, the credit is applied to a  
30 debt of the beneficiary, or "funds with respect to the order" are  
31 otherwise made available to the beneficiary. Section 4A-405(a)  
32 [section 4-1405(1)]. The quoted phrase covers cases in which  
33 funds are made available to the beneficiary as a result of  
34 receipt of a payment order for the benefit of the beneficiary but  
35 the release of funds is not expressed as payment of the order.  
36 For example, the beneficiary's bank might express a release of  
37 funds equal to the amount of the order as a "loan" that will be  
38 automatically repaid when the beneficiary's bank receives payment  
39 by the sender of the order. If the release of funds is  
40 designated as a loan pursuant to a routine practice of the bank,  
41 the release is conditional payment of the order rather than a  
42 loan, particularly if normal incidents of a loan such as the  
43 signing of a loan agreement or note and the payment of interest  
44 are not present. Such a release of funds is payment to the  
45 beneficiary under Section 4A-405(a) [section 4-1405(1)]. Under  
46 Section 4A-405(c) [section 4-1405(3)] the bank cannot recover the  
47 money from the beneficiary if the bank does not receive payment  
48 from the sender of the payment order that it accepted.

2 Exceptions to this rule are stated in §4A-405(d) and (e) [section  
3 4-1405(4) and (5)]. The beneficiary's bank may also accept by  
4 notifying the beneficiary that the order has been received.  
5 "Notifies" is defined in Section 1-201(26). In some cases a  
6 beneficiary's bank will receive a payment order during the day  
7 but settlement of the sender's obligation to pay the order will  
8 not occur until the end of the day. If the beneficiary's bank  
9 wants to defer incurring liability to the beneficiary until the  
10 beneficiary's bank receives payment, it can do so. The  
11 beneficiary's bank incurs no liability to the beneficiary with  
12 respect to a payment order that it receives until it accepts the  
13 order. If the bank does not accept pursuant to subsection (b)(2)  
14 [subsection (2)(b)], acceptance does not occur until the end of  
15 the day when the beneficiary's bank receives settlement. If the  
16 sender settles, the payment order will be accepted under  
17 subsection (b)(2) [subsection (2)(b)] and the funds will be  
18 released to the beneficiary the next morning. If the sender  
19 doesn't settle, no acceptance occurs. In either case the  
20 beneficiary's bank suffers no loss.

21 6. In most cases the beneficiary's bank will receive a  
22 payment order from another bank. If the sender is a bank and the  
23 beneficiary's bank receives payment from the sender by formal  
24 settlement through the Federal Reserve System or a funds transfer  
25 system (Section 4A-403(a)(1) [section 4-1403(1)(a)]) or, less  
26 commonly, through credit to an account of the beneficiary's bank  
27 with the sender or another bank (Section 4A-403(a)(2) [section  
28 4-1403(1)(b)]), acceptance by the beneficiary's bank occurs at  
29 the time payment is made. Section 4A-209(b)(2) [section  
30 4-1209(2)(b)]. A minor exception to this rule is stated in  
31 Section 4A-209(c) [section 4-1209(3)]. Section 4A-209(b)(2)  
32 [section 4-1209(2)(b)] results in automatic acceptance of payment  
33 orders issued to a beneficiary's bank by means of Fedwire because  
34 the Federal Reserve account of the beneficiary's bank is credited  
35 and final payment is made to that bank when the payment order is  
36 received.

37 Subsection (b)(2) [subsection (2)(b)] would also apply to  
38 cases in which the beneficiary's bank mistakenly pays a person  
39 who is not the beneficiary of the payment order issued to the  
40 beneficiary's bank. For example, suppose the payment order  
41 provides for immediate payment to Account #12345. The  
42 beneficiary's bank erroneously credits Account # 12346 and  
43 notifies the holder of that account of the credit. No acceptance  
44 occurs in this case under subsection (b)(1) [subsection (2)(a)]  
45 because the beneficiary of the order has not been paid or  
46 notified. The holder of Account #12345 is the beneficiary of the  
47 order issued to the beneficiary's bank. But acceptance will  
48 normally occur if the beneficiary's bank takes no other action,

2 because the bank will normally receive settlement with respect to  
the payment order. At that time the bank has accepted because  
4 the sender paid its payment order. The bank is liable to pay the  
holder of Account #12345. The bank has paid the holder of  
6 Account # 12346 by mistake, and has a right to recover the  
payment if the credit is withdrawn, to the extent provided in the  
law governing mistake and restitution.

8  
10 7. Subsection (b)(3) [subsection (2)(c)] covers cases of  
inaction by the beneficiary's bank. It applies whether or not  
the sender is a bank and covers a case in which the sender and  
12 the beneficiary both have accounts with the receiving bank and  
payment will be made by debiting the account of the sender and  
14 crediting the account of the beneficiary. Subsection (b)(3)  
[subsection (2)(c)] is similar to subsection (b)(2) [subsection  
16 (2)(b)] in that it bases acceptance by the beneficiary's bank on  
payment by the sender. Payment by the sender is effected by a  
18 debit to the sender's account if the account balance is  
sufficient to cover the amount of the order. On the payment date  
20 (Section 4A-401 [section 4-1401]) of the order the beneficiary's  
bank will normally credit the beneficiary's account and notify  
22 the beneficiary of receipt of the order if it is satisfied that  
the sender's account balance covers the order or is willing to  
24 give credit to the sender. In some cases, however, the bank may  
not be willing to give credit to the sender and it may not be  
26 possible for the bank to determine until the end of the day on  
the payment date whether there are sufficient good funds in the  
28 sender's account. There may be various transactions during the  
day involving funds going into and out of the account. Some of  
30 these transactions may occur late in the day or after the close  
of the banking day. To accommodate this situation, subsection  
32 (b)(3) [subsection (2)(c)] provides that the status of the  
account is determined at the opening of the next funds transfer  
34 business day of the beneficiary's bank after the payment date of  
the order. If the sender's account balance is sufficient to  
36 cover the order, the beneficiary's bank has a source of payment  
and the result in almost all cases is that the bank accepts the  
38 order at that time if it did not previously accept under  
subsection (b)(1) [subsection (2)(a)]. In rare cases, a bank may  
40 want to avoid acceptance under subsection (b)(3) [subsection  
(2)(c)] by rejecting the order as discussed in Comment 8.

42  
44 8. Section 4A-209 [section 4-1209] is based on a general  
principle that a receiving bank is not obliged to accept a  
46 payment order unless it has agreed or is bound by a funds  
transfer system rule to do so. Thus, provision is made to allow  
48 the receiving bank to prevent acceptance of the order. This  
principle is consistently followed if the receiving bank is not  
the beneficiary's bank. If the receiving bank is not the

2 beneficiary's bank, acceptance is in the control of the receiving  
bank because it occurs only if the order is executed. But in the  
4 case of the beneficiary's bank acceptance can occur by passive  
receipt of payment under subsection (b)(2) or (3) [subsection  
6 (2)(b) or (c)]. In the case of a payment made by Fedwire  
acceptance cannot be prevented. In other cases the beneficiary's  
8 bank can prevent acceptance by giving notice of rejection to the  
sender before payment occurs under Section 4A-403(a)(1) or (2)  
10 [section 4-1403(1)(a) or (b)]. A minor exception to the ability  
of the beneficiary's bank to reject is stated in Section  
12 4A-502(c)(3) [section 4-1502(3)(c)].

14 Under subsection (b)(3) [subsection (2)(c)] acceptance  
occurs at the opening of the next funds transfer business day of  
16 the beneficiary's bank following the payment date unless the bank  
rejected the order before that time or it rejects within one hour  
18 after that time. In some cases the sender and the beneficiary's  
bank may not be in the same time zone or the beginning of the  
20 business day of the sender and the funds transfer business day of  
the beneficiary's bank may not coincide. For example, the sender  
22 may be located in California and the beneficiary's bank in New  
York. Since in most cases notice of rejection would be  
24 communicated electronically or by telephone, it might not be  
feasible for the bank to give notice before one hour after the  
26 opening of the funds transfer business day in New York because at  
that hour, the sender's business day may not have started in  
28 California. For that reason, there are alternative deadlines  
stated in subsection (b)(3) [subsection (2)(c)]. In the case  
30 stated, the bank acts in time if it gives notice within one hour  
after the opening of the business day of the sender. But if the  
32 notice of rejection is received by the sender after the payment  
date, the bank is obliged to pay interest to the sender if the  
34 sender's account does not bear interest. In that case the bank  
had the use of funds of the sender that the sender could  
36 reasonably assume would be used to pay the beneficiary. The rate  
of interest is stated in Section 4A-506 [section 4-1506]. If the  
38 sender receives notice on the day after the payment date the  
sender is entitled to one day's interest. If receipt of notice  
40 is delayed for more than one day, the sender is entitled to  
interest for each additional day of delay.

42  
44 9. Subsection (d) [subsection (4)] applies only to a  
payment order by the originator of a funds transfer to the  
46 originator's bank and it refers to the following situation. On  
April 1, Originator instructs Bank A to make a payment on April  
15 to the account of Beneficiary in Bank B. By mistake, on April  
48 1, Bank A executes Originator's payment order by issuing a  
payment order to Bank B instructing immediate payment to  
Beneficiary. Bank B credited Beneficiary's account and

2 immediately released the funds to Beneficiary. Under subsection  
(d) [subsection (4)] no acceptance by Bank A occurred on April 1  
when Originator's payment order was executed because acceptance  
cannot occur before the execution date which in this case would  
be April 15 or shortly before that date. Section 4A-301(b)  
[section 4-1301(2)]. Under Section 4A-402(c) [section  
4-1402(3)], Originator is not obliged to pay Bank A until the  
order is accepted and that can't occur until the execution date.  
But Bank A is required to pay Bank B when Bank B accepted Bank  
A's order on April 1. Unless Originator and Beneficiary are the  
same person, in almost all cases Originator is paying a debt owed  
to Beneficiary and early payment does not injure Originator  
because Originator does not have to pay Bank A until the  
execution date. Section 4A-402(c) [section 4-1402(3)]. Bank A  
takes the interest loss. But suppose that on April 3, Originator  
concludes that no debt was owed to Beneficiary or that the debt  
was less than the amount of the payment order. Under Section  
4A-211(b) [section 4-1211(2)] Originator can cancel its payment  
order if Bank A has not accepted. If early execution of  
Originator's payment order is acceptance, Originator can suffer a  
loss because cancellation after acceptance is not possible  
without the consent of Bank A and Bank B. Section 4A-211(c)  
[section 4-1211(3)]. If Originator has to pay Bank A, Originator  
would be required to seek recovery of the money from  
Beneficiary. Subsection (d) [subsection (4)] prevents this  
result and puts the risk of loss on Bank A by providing that the  
early execution does not result in acceptance until the execution  
date. Since on April 3 Originator's order was not yet accepted,  
Originator can cancel it under Section 4A-211(b) [section  
4-1211(2)]. The result is that Bank A is not entitled to payment  
from Originator but is obliged to pay Bank B. Bank A has paid  
Beneficiary by mistake. If Originator's payment order is  
cancelled, Bank A becomes the originator of an erroneous funds  
transfer to Beneficiary. Bank A has the burden of recovering  
payment from Beneficiary on the basis of a payment by mistake.  
If Beneficiary received the money in good faith in payment of a  
debt owed to Beneficiary by Originator, the law of mistake and  
restitution may allow Beneficiary to keep all or part of the  
money received. If Originator owed money to Beneficiary, Bank A  
has paid Originator's debt and, under the law of restitution,  
which applies pursuant to Section 1-103, Bank A is subrogated to  
Beneficiary's rights against Originator on the debt.

44 If Bank A is the Beneficiary's bank and Bank A credited  
Beneficiary's account and released the funds to Beneficiary on  
April 1, the analysis is similar. If Originator's order is  
cancelled, Bank A has paid Beneficiary by mistake. The right of  
Bank A to recover the payment from Beneficiary is similar to Bank  
A's rights in the preceding paragraph.

## 2 §4-1210. Rejection of payment order

4 (1) A payment order is rejected by the receiving bank by a  
6 notice of rejection transmitted to the sender orally,  
8 electronically or in writing. A notice of rejection need not use  
10 any particular words and is sufficient if it indicates that the  
12 receiving bank is rejecting the order or will not execute or pay  
14 the order. Rejection is effective when the notice is given if  
16 transmission is by a means that is reasonable in the  
18 circumstances. If notice of rejection is given by a means that  
20 is not reasonable, rejection is effective when the notice is  
22 received. If an agreement of the sender and receiving bank  
24 establishes the means to be used to reject a payment order, any  
26 means complying with the agreement is reasonable and any means  
28 not complying is not reasonable unless no significant delay in  
30 receipt of the notice resulted from the use of the noncomplying  
32 means.

20 (2) This subsection applies if a receiving bank other than  
22 the beneficiary's bank fails to execute a payment order despite  
24 the existence on the execution date of a withdrawable credit  
26 balance in an authorized account of the sender sufficient to  
28 cover the order. If the sender does not receive notice of  
30 rejection of the order on the execution date and the authorized  
32 account of the sender does not bear interest, the bank is obliged  
34 to pay interest to the sender on the amount of the order for the  
36 number of days elapsing after the execution date to the earlier  
38 of the day the order is canceled pursuant to section 4-1211,  
40 subsection (4) or the day the sender receives notice or learns  
42 that the order was not executed, counting the final day of the  
44 period as an elapsed day. If the withdrawable credit balance  
46 during that period falls below the amount of the order, the  
48 amount of interest is reduced accordingly.

36 (3) If a receiving bank suspends payments, all unaccepted  
38 payment orders issued to it are deemed rejected at the time the  
40 bank suspends payments.

40 (4) Acceptance of a payment order precludes a later  
42 rejection of the order. Rejection of a payment order precludes a  
44 later acceptance of the order.

### 44 1991 Uniform Comment

46 1. With respect to payment orders issued to a receiving  
48 bank other than the beneficiary's bank, notice of rejection is  
not necessary to prevent acceptance of the order. Acceptance can  
occur only if the receiving bank executes the order. Section

2 4A-209(a) [section 4-1209(1)]. But notice of rejection will  
3 routinely be given by such a bank in cases in which the bank  
4 cannot or is not willing to execute the order for some reason.  
5 There are many reasons why a bank doesn't execute an order. The  
6 payment order may not clearly instruct the receiving bank because  
7 of some ambiguity in the order or an internal inconsistency. In  
8 some cases, the receiving bank may not be able to carry out the  
9 instruction because of equipment failure, credit limitations on  
10 the receiving bank, or some other factor which makes proper  
11 execution of the order infeasible. In those cases notice of  
12 rejection is a means of informing the sender of the facts so that  
13 a corrected payment order can be transmitted or the sender can  
14 seek alternate means of completing the funds transfer. The other  
15 major reason for not executing an order is that the sender's  
16 account is insufficient to cover the order and the receiving bank  
17 is not willing to give credit to the sender. If the sender's  
18 account is sufficient to cover the order and the receiving bank  
19 chooses not to execute the order, notice of rejection is  
20 necessary to prevent liability to pay interest to the sender if  
21 the case falls within Section 4A-210(b) [section 4-1210(2)] which  
22 is discussed in Comment 3.

23 2. A payment order to the beneficiary's bank can be  
24 accepted by inaction of the bank. Section 4A-209(b)(2) and (3)  
25 [section 4-1209(2)(b) and (c)]. To prevent acceptance under  
26 those provisions it is necessary for the receiving bank to send  
27 notice of rejection before acceptance occurs. Subsection (a) of  
28 Section 4A-210 [section 4-1210(1)] states the rule that rejection  
29 is accomplished by giving notice of rejection. This incorporates  
30 the definitions in Section 1-201(26). Rejection is effective  
31 when notice is given if it is given by a means that is reasonable  
32 in the circumstances. Otherwise, it is effective when the notice  
33 is received. The question of when rejection is effective is  
34 important only in the relatively few cases under subsection  
35 (b)(2) and (3) [subsection (2)(b) and (c)] in which a notice of  
36 rejection is necessary to prevent acceptance. The question of  
37 whether a particular means is reasonable depends on the facts in  
38 a particular case. In a very large percentage of cases the  
39 sender and the receiving bank will be in direct electronic  
40 contact with each other and in those cases a notice of rejection  
41 can be transmitted instantaneously. Since time is of the essence  
42 in a large proportion of funds transfers, some quick means of  
43 transmission would usually be required, but this is not always  
44 the case. The parties may specify by agreement the means by  
45 which communication between the parties is to be made.

46 3. Subsection (b) [subsection (2)] deals with cases in  
47 which a sender does not learn until after the execution date that  
48 the sender's order has not been executed. It applies only to

2 cases in which the receiving bank was assured of payment because  
3 the sender's account was sufficient to cover the order.  
4 Normally, the receiving bank will accept the sender's order if it  
5 is assured of payment, but there may be some cases in which the  
6 bank chooses to reject. Unless the receiving bank had obligated  
7 itself by agreement to accept, the failure to accept is not  
8 wrongful. There is no duty of the receiving bank to accept the  
9 payment order unless it is obliged to accept by express  
10 agreement. Section 4A-212 [section 4-1212]. But even if the  
11 bank has not acted wrongfully, the receiving bank had the use of  
12 the sender's money that the sender could reasonably assume was to  
13 be the source of payment of the funds transfer. Until the sender  
14 learns that the order was not accepted the sender is denied the  
15 use of that money. Subsection (b) [subsection (2)] obliges the  
16 receiving bank to pay interest to the sender as restitution  
17 unless the sender receives notice of rejection on the execution  
18 date. The time of receipt of notice is determined pursuant to  
19 §1-201(27). The rate of interest is stated in Section 4A-506  
20 [section 4-1506]. If the sender receives notice on the day after  
21 the execution date, the sender is entitled to one day's  
22 interest. If receipt of notice is delayed for more than one day,  
23 the sender is entitled to interest for each additional day of  
24 delay.

25 4. Subsection (d) [subsection (4)] treats acceptance and  
26 rejection as mutually exclusive. If a payment order has been  
27 accepted, rejection of that order becomes impossible. If a  
28 payment order has been rejected it cannot be accepted later by  
29 the receiving bank. Once notice of rejection has been given, the  
30 sender may have acted on the notice by making the payment through  
31 other channels. If the receiving bank wants to act on a payment  
32 order that it has rejected it has to obtain the consent of the  
33 sender. In that case the consent of the sender would amount to  
34 the giving of a second payment order that substitutes for the  
35 rejected first order. If the receiving bank suspends payments  
36 (Section 4-104(1)(k)), subsection (c) [subsection (3)] provides  
37 that unaccepted payment orders are deemed rejected at the time  
38 suspension of payments occurs. This prevents acceptance by  
39 passage of time under Section 4A-209(b)(3) [section 4-1209(2)(c)].

#### 40 §4-1211. Cancellation and amendment of payment order

41 (1) A communication of the sender of a payment order  
42 cancelling or amending the order may be transmitted to the  
43 receiving bank orally, electronically or in writing. If a  
44 security procedure is in effect between the sender and the  
45 receiving bank, the communication is not effective to cancel or  
46 amend the order unless the communication is verified pursuant to  
47

2 the security procedure or the bank agrees to the cancellation or  
3 amendment.

4 (2) Subject to subsection (1), a communication by the  
5 sender cancelling or amending a payment order is effective to  
6 cancel or amend the order if notice of the communication is  
7 received at a time and in a manner affording the receiving bank a  
8 reasonable opportunity to act on the communication before the  
9 bank accepts the payment order.

10 (3) After a payment order has been accepted, cancellation  
11 or amendment of the order is not effective unless the receiving  
12 bank agrees or a funds transfer system rule allows cancellation  
13 or amendment without agreement of the bank.

14 (a) With respect to a payment order accepted by a receiving  
15 bank other than the beneficiary's bank, cancellation or  
16 amendment is not effective unless a conforming cancellation  
17 or amendment of the payment order issued by the receiving  
18 bank is also made.

19 (b) With respect to a payment order accepted by the  
20 beneficiary's bank, cancellation or amendment is not  
21 effective unless the order was issued in execution of an  
22 unauthorized payment order or because of a mistake by a  
23 sender in the funds transfer that resulted in the issuance  
24 of a payment order:

25 (i) That is a duplicate of a payment order previously  
26 issued by the sender;

27 (ii) That orders payment to a beneficiary not entitled  
28 to receive payment from the originator; or

29 (iii) That orders payment in an amount greater than  
30 the amount the beneficiary was entitled to receive from  
31 the originator.

32 If the payment order is canceled or amended, the  
33 beneficiary's bank is entitled to recover from the  
34 beneficiary any amount paid to the beneficiary to the extent  
35 allowed by the law governing mistake and restitution.

36 (4) An unaccepted payment order is canceled by operation of  
37 law at the close of the 5th funds transfer business day of the  
38 receiving bank after the execution date or payment date of the  
39 order.

2 (5) A canceled payment order can not be accepted. If an  
3 accepted payment order is canceled, the acceptance is nullified  
4 and a person does not have any right or obligation based on the  
5 acceptance. Amendment of a payment order is deemed to be  
6 cancellation of the original order at the time of amendment and  
7 issue of a new payment order in the amended form at the same time.

8 (6) Unless otherwise provided in an agreement of the  
9 parties or in a funds transfer system rule, if the receiving bank  
10 after accepting a payment order agrees to cancellation or  
11 amendment of the order by the sender or is bound by a funds  
12 transfer system rule allowing cancellation or amendment without  
13 the bank's agreement, the sender whether or not cancellation or  
14 amendment is effective is liable to the bank for any loss and  
15 expenses including reasonable attorney's fees incurred by the  
16 bank as a result of the cancellation or amendment or attempted  
17 cancellation or amendment.

18 (7) A payment order is not revoked by the death or legal  
19 incapacity of the sender unless the receiving bank knows of the  
20 death or of an adjudication of incapacity by a court of competent  
21 jurisdiction and has reasonable opportunity to act before  
22 acceptance of the order.

23 (8) A funds transfer system rule is not effective to the  
24 extent it conflicts with subsection (3), paragraph (b).

25 1991 Uniform Comment

26 1. This section deals with cancellation and amendment of  
27 payment orders. It states the conditions under which  
28 cancellation or amendment is both effective and rightful. There  
29 is no concept of wrongful cancellation or amendment of a payment  
30 order. If the conditions stated in this section are not met the  
31 attempted cancellation or amendment is not effective. If the  
32 stated conditions are met the cancellation or amendment is  
33 effective and rightful. The sender of a payment order may want  
34 to withdraw or change the order because the sender has had a  
35 change of mind about the transaction or because the payment order  
36 was erroneously issued or for any other reason. One common  
37 situation is that of multiple transmission of the same order.  
38 The sender that mistakenly transmits the same order twice wants  
39 to correct the mistake by cancelling the duplicate order. Or, a  
40 sender may have intended to order a payment of \$1,000,000 but  
41 mistakenly issued an order to pay \$10,000,000. In this case the  
42 sender might try to correct the mistake by cancelling the order  
43 and issuing another order in the proper amount. Or, the mistake  
44 could be corrected by amending the order to change it to the  
45 proper amount. Whether the error is corrected by amendment or  
46 the proper amount.

2 cancellation and reissue the net result is the same. This result  
3 is stated in the last sentence of subsection (a) [subsection (5)].

4 2. Subsection (a) [subsection (1)] allows a cancellation or  
5 amendment of a payment order to be communicated to the receiving  
6 bank "orally, electronically, or in writing." The quoted phrase  
7 is consistent with the language of Section 4A-103(a) [section  
8 4-1103(1)] applicable to payment orders. Cancellations and  
9 amendments are normally subject to verification pursuant to  
10 security procedures to the same extent as payment orders.  
11 Subsection (a) [subsection (1)] recognizes this fact by providing  
12 that in cases in which there is a security procedure in effect  
13 between the sender and the receiving bank the bank is not bound  
14 by a communication cancelling or amending an order unless  
15 verification has been made. This is necessary to protect the  
16 bank because under subsection (b) [subsection (2)] a cancellation  
17 or amendment can be effective by unilateral action of the  
18 sender. Without verification the bank cannot be sure whether the  
19 communication was or was not effective to cancel or amend a  
20 previously verified payment order.

21 3. If the receiving bank has not yet accepted the order,  
22 there is no reason why the sender should not be able to cancel or  
23 amend the order unilaterally so long as the requirements of  
24 subsections (a) and (b) [subsections (1) and (2)] are met. If  
25 the receiving bank has accepted the order, it is possible to  
26 cancel or amend but only if the requirements of subsection (c)  
27 [subsection (3)] are met.

28  
29 First consider the case of a receiving bank other than the  
30 beneficiary's bank. If the bank has not yet accepted the order,  
31 the sender can unilaterally cancel or amend. The communication  
32 amending or cancelling the payment order must be received in time  
33 to allow the bank to act on it before the bank issues its payment  
34 order in execution of the sender's order. The time that the  
35 sender's communication is received is governed by Section 4A-106  
36 [section 4-1106]. If a payment order does not specify a delayed  
37 payment date or execution date, the order will normally be  
38 executed shortly after receipt. Thus, as a practical matter, the  
39 sender will have very little time in which to instruct  
40 cancellation or amendment before acceptance. In addition, a  
41 receiving bank will normally have cut-off times for receipt of  
42 such communications, and the receiving bank is not obliged to act  
43 on communications received after the cut-off hour. Cancellation  
44 by the sender after execution of the order by the receiving bank  
45 requires the agreement of the bank unless a funds transfer rule  
46 otherwise provides. Subsection (c) [subsection (3)]. Although  
47 execution of the sender's order by the receiving bank does not  
48 itself impose liability on the receiving bank (under Section

4A-402 [section 4-1402] no liability is incurred by the receiving  
2 bank to pay its order until it is accepted, it would commonly be  
3 the case that acceptance follows shortly after issuance. Thus,  
4 as a practical matter, a receiving bank that has executed a  
5 payment order will incur a liability to the next bank in the  
6 chain before it would be able to act on the cancellation request  
7 of its customer. It is unreasonable to impose on the receiving  
8 bank a risk of loss with respect to a cancellation request  
9 without the consent of the receiving bank.

10  
11 The statute does not state how or when the agreement of the  
12 receiving bank must be obtained for cancellation after  
13 execution. The receiving bank's consent could be obtained at the  
14 time cancellation occurs or it could be based on a preexisting  
15 agreement. Or, a funds transfer system rule could provide that  
16 cancellation can be made unilaterally by the sender. By virtue  
17 of that rule any receiving bank covered by the rule is bound.  
18 Section 4A-501 [section 4-1501]. If the receiving bank has  
19 already executed the sender's order, the bank would not consent  
20 to cancellation unless the bank to which the receiving bank has  
21 issued its payment order consents to cancellation of that order.  
22 It makes no sense to allow cancellation of a payment order unless  
23 all subsequent payment orders in the funds transfer that were  
24 issued because of the cancelled payment order are also  
25 cancelled. Under subsection (c)(1) [subsection (3)(a)], if a  
26 receiving bank consents to cancellation of the payment order  
27 after it has executed, the cancellation is not effective unless  
28 the receiving bank also cancels the payment order issued by the  
29 bank.

30  
31 4. With respect to a payment order issued to the  
32 beneficiary's bank, acceptance is particularly important because  
33 it creates liability to pay the beneficiary, it defines when the  
34 originator pays its obligation to the beneficiary, and it defines  
35 when any obligation for which the payment is made is discharged.  
36 Since acceptance affects the rights of the originator and the  
37 beneficiary it is not appropriate to allow the beneficiary's bank  
38 to agree to cancellation or amendment except in unusual cases.  
39 Except as provided in subsection (c)(2) [subsection (3)(b)],  
40 cancellation or amendment after acceptance by the beneficiary's  
41 bank is not possible unless all parties affected by the order  
42 agree. Under subsection (c)(2) [subsection (3)(b)], cancellation  
43 or amendment is possible only in the four cases stated. The  
44 following examples illustrate subsection (c)(2) [subsection  
45 (3)(b)]:

46  
47 Case #1. Originator's Bank executed a payment order issued  
48 in the name of its customer as sender. The order was not  
authorized by the customer and was fraudulently issued.

Beneficiary's Bank accepted the payment order issued by Originator's Bank. Under subsection (c)(2) [subsection (3)(b)] Originator's Bank can cancel the order if Beneficiary's Bank consents. It doesn't make any difference whether the payment order that Originator's Bank accepted was or was not enforceable against the customer under Section 4A-202(b) [section 4-1202(2)]. Verification under that provision is important in determining whether Originator's Bank or the customer has the risk of loss, but it has no relevance under Section 4A-211(c)(2) [section 4-1211(3)(b)]. Whether or not verified, the payment order was not authorized by the customer. Cancellation of the payment order to Beneficiary's Bank causes the acceptance of Beneficiary's Bank to be nullified. Subsection (e) [subsection (5)]. Beneficiary's Bank is entitled to recover payment from the beneficiary to the extent allowed by the law of mistake and restitution. In this kind of case the beneficiary is usually a party to the fraud who has no right to receive or retain payment of the order.

Case #2. Originator owed Beneficiary \$1,000,000 and ordered Bank A to pay that amount to the account of Beneficiary in Bank B. Bank A issued a complying order to Bank B, but by mistake issued a duplicate order as well. Bank B accepted both orders. Under subsection (c)(2)(i) [subsection (3)(b)(i)] cancellation of the duplicate order could be made by Bank A with the consent of Bank B. Beneficiary has no right to receive or retain payment of the duplicate payment order if only \$1,000,000 was owed by Originator to Beneficiary. If Originator owed \$2,000,000 to Beneficiary, the law of restitution might allow Beneficiary to retain the \$1,000,000 paid by Bank B on the duplicate order. In that case Bank B is entitled to reimbursement from Bank A under subsection (f) [subsection (6)].

Case #3. Originator owed \$1,000,000 to X. Intending to pay X, Originator ordered Bank A to pay \$1,000,000 to Y's account in Bank B. Bank A issued a complying payment order to Bank B which Bank B accepted by releasing the \$1,000,000 to Y. Under subsection (c)(2)(ii) [subsection (3)(b)(ii)] Bank A can cancel its payment order to Bank B with the consent of Bank B if Y was not entitled to receive payment from Originator. Originator can also cancel its order to Bank A with Bank A's consent. Subsection (c)(1) [subsection (3)(a)]. Bank B may recover the \$1,000,000 from Y unless the law of mistake and restitution allows Y to retain some or all of the amount paid. If no debt was owed to Y, Bank B should have a right of recovery.

Case #4. Originator owed Beneficiary \$10,000. By mistake Originator ordered Bank A to pay \$1,000,000 to the account of Beneficiary in Bank B. Bank A issued a complying order to Bank B

which accepted by notifying Beneficiary of its right to withdraw \$1,000,000. Cancellation is permitted in this case under subsection (c)(2)(iii) [subsection (3)(b)(iii)]. If Bank B paid Beneficiary it is entitled to recover the payment except to the extent the law of mistake and restitution allows Beneficiary to retain payment. In this case Beneficiary might be entitled to retain \$10,000, the amount of the debt owed to Beneficiary. If Beneficiary may retain \$10,000, Bank B would be entitled to \$10,000 from Bank A pursuant to subsection (f) [subsection (6)]. In this case Originator also cancelled its order. Thus Bank A would be entitled to \$10,000 from Originator pursuant to subsection (f) [subsection (6)].

5. Unless constrained by a funds transfer system rule, a receiving bank may agree to cancellation or amendment of the payment order under subsection (c) [subsection (3)] but is not required to do so regardless of the circumstances. If the receiving bank has incurred liability as a result of its acceptance of the sender's order, there are substantial risks in agreeing to cancellation or amendment. This is particularly true for a beneficiary's bank. Cancellation or amendment after acceptance by the beneficiary's bank can be made only in the four cases stated and the beneficiary's bank may not have any way of knowing whether the requirements of subsection (c) [subsection (3)] have been met or whether it will be able to recover payment from the beneficiary that received payment. Even with indemnity the beneficiary's bank may be reluctant to alienate its customer, the beneficiary, by denying the customer the funds. Subsection (c) [subsection (3)] leaves the decision to the beneficiary's bank unless the consent of the beneficiary's bank is not required under a funds transfer system rule or other interbank agreement. If a receiving bank agrees to cancellation or amendment under subsection (c)(1) or (2) [subsection (3)(a) or (b)], it is automatically entitled to indemnification from the sender under subsection (f) [subsection (6)]. The indemnification provision recognizes that a sender has no right to cancel a payment order after it is accepted by the receiving bank. If the receiving bank agrees to cancellation, it is doing so as an accommodation to the sender and it should not incur a risk of loss in doing so.

6. Acceptance by the receiving bank of a payment order issued by the sender is comparable to acceptance of an offer under the law of contracts. Under that law the death or legal incapacity of an offeror terminates the offer even though the offeree has no notice of the death or incapacity. Restatement Second, Contracts §48. Comment a. to that section states that the "rule seems to be a relic of the obsolete view that a contract requires a 'meeting of minds,' and it is out of harmony with the modern doctrine that a manifestation of assent is

effective without regard to actual mental assent." Subsection (g) [subsection (7)], which reverses the Restatement rule in the case of a payment order, is similar to Section 4-405(1) which applies to checks. Subsection (g) [subsection (7)] does not address the effect of the bankruptcy of the sender of a payment order before the order is accepted, but the principle of subsection (g) [subsection (7)] has been recognized in Bank of Marin v. England, 385 U.S. 99 (1966). Although Bankruptcy Code Section 542(c) may not have been drafted with wire transfers in mind, its language can be read to allow the receiving bank to charge the sender's account for the amount of the payment order if the receiving bank executed it in ignorance of the bankruptcy.

7. Subsection (d) [subsection (4)] deals with stale payment orders. Payment orders normally are executed on the execution date or the day after. An order issued to the beneficiary's bank is normally accepted on the payment date or the day after. If a payment order is not accepted on its execution or payment date or shortly thereafter, it is probable that there was some problem with the terms of the order or the sender did not have sufficient funds or credit to cover the amount of the order. Delayed acceptance of such an order is normally not contemplated, but the order may not have been cancelled by the sender. Subsection (d) [subsection (4)] provides for cancellation by operation of law to prevent an unexpected delayed acceptance.

8. A funds transfer system rule can govern rights and obligations between banks that are parties to payment orders transmitted over the system even if the rule conflicts with Article 4A [Article 4-A]. In some cases, however, a rule governing a transaction between two banks can affect a third party in an unacceptable way. Subsection (h) [subsection (8)] deals with such a case. A funds transfer system rule cannot allow cancellation of a payment order accepted by the beneficiary's bank if the rule conflicts with subsection (c)(2) [subsection (3)(b)]. Because rights of the beneficiary and the originator are directly affected by acceptance, subsection (c)(2) [subsection (3)(b)] severely limits cancellation. These limitations cannot be altered by funds transfer system rule.

**§4-1212. Liability and duty of receiving bank regarding unaccepted payment order**

If a receiving bank fails to accept a payment order that it is obliged by express agreement to accept, the bank is liable for breach of the agreement to the extent provided in the agreement or in this Article but does not otherwise have any duty to accept a payment order or before acceptance to take any action or refrain from taking action with respect to the order except as

provided in this Article or by express agreement. Liability based on acceptance arises only when acceptance occurs as stated in section 4-1209 and liability is limited to that provided in this Article. A receiving bank is not the agent of the sender or beneficiary of the payment order it accepts or of any other party to the funds transfer and the bank owes no duty to any party to the funds transfer except as provided in this Article or by express agreement.

**1991 Uniform Comment**

With limited exceptions stated in this Article, the duties and obligations of receiving banks that carry out a funds transfer arise only as a result of acceptance of payment orders or of agreements made by receiving banks. Exceptions are stated in Section 4A-209(b)(3) [section 4-1209(2)(c)] and Section 4A-210(b) [section 4-1210(2)]. A receiving bank is not like a collecting bank under Article 4. No receiving bank, whether it be an originator's bank, an intermediary bank or a beneficiary's bank, is an agent for any other party in the funds transfer.

**PART 3**

**EXECUTION OF SENDER'S PAYMENT ORDER BY RECEIVING BANK**

**§4-1301. Execution and execution date**

(1) A payment order is "executed" by the receiving bank when it issues a payment order intended to carry out the payment order received by the bank. A payment order received by the beneficiary's bank can be accepted but can not be executed.

(2) "Execution date" of a payment order means the day on which the receiving bank may properly issue a payment order in execution of the sender's order. The execution date may be determined by instruction of the sender but can not be earlier than the day the order is received and, unless otherwise determined, is the day the order is received. If the sender's instruction states a payment date, the execution date is the payment date or an earlier date on which execution is reasonably necessary to allow payment to the beneficiary on the payment date.

**1991 Uniform Comment**

1. The terms "executed," "execution" and "execution date" are used only with respect to a payment order to a receiving bank other than the beneficiary's bank. The beneficiary's bank can accept the payment order that it receives, but it does not



2 execute the order. Execution refers to the act of the receiving  
3 bank in issuing a payment order "intended to carry out" the  
4 payment order that the bank received. A receiving bank has  
5 executed an order even if the order issued by the bank does not  
6 carry out the order received by the bank. For example, the bank  
7 may have erroneously issued an order to the wrong beneficiary, or  
8 in the wrong amount or to the wrong beneficiary's bank. In each  
9 of these cases execution has occurred but the execution is  
10 erroneous. Erroneous execution is covered in Section 4A-303  
11 [section 4-1303].

12 2. "Execution date" refers to the time a payment order  
13 should be executed rather than the day it is actually executed.  
14 Normally the sender will not specify an execution date, but most  
15 payment orders are meant to be executed immediately. Thus, the  
16 execution date is normally the day the order is received by the  
17 receiving bank. It is common for the sender to specify a  
18 "payment date" which is defined in Section 4A-401 [section  
19 4-1401] as "the day on which the amount of the order is payable  
20 to the beneficiary by the beneficiary's bank." Except for  
21 automated clearing house transfers, if a funds transfer is  
22 entirely within the United States and the payment is to be  
23 carried out electronically, the execution date is the payment  
24 date unless the order is received after the payment date. If the  
25 payment is to be carried out through an automated clearing house,  
26 execution may occur before the payment date. In an ACH transfer  
27 the beneficiary is usually paid one or two days after issue of  
28 the originator's payment order. The execution date is determined  
29 by the stated payment date and is a day before the payment date  
30 on which execution is reasonably necessary to allow payment on  
31 the payment date. A funds transfer system rule could also  
32 determine the execution date of orders received by the receiving  
33 bank if both the sender and the receiving bank are participants  
34 in the funds transfer system. The execution date can be  
35 determined by the payment order itself or by separate  
36 instructions of the sender or an agreement of the sender and the  
37 receiving bank. The second sentence of subsection (b)  
38 [subsection (2)] must be read in the light of Section 4A-106  
39 [section 4-1106] which states that if a payment order is received  
40 after the cut-off time of the receiving bank it may be treated by  
41 the bank as received at the opening of the next funds transfer  
42 business day.

44 3. Execution on the execution date is timely, but the order  
45 can be executed before or after the execution date. Section  
46 4A-209(d) [section 4-1209(4)] and Section 4A-402(c) [section  
47 4-1402(3)] state the consequences of early execution and Section  
48 4A-305(a) [section 4-1305(1)] states the consequences of late  
49 execution.

2 §4-1302. Obligations of receiving bank in execution of  
3 payment order

4 (1) Except as provided in subsections (2) to (4), if the  
5 receiving bank accepts a payment order pursuant to section  
6 4-1209, subsection (1), the bank has the following obligations in  
7 executing the order.

8 (a) The receiving bank is obliged to issue, on the  
9 execution date, a payment order complying with the sender's  
10 order and to follow the sender's instructions concerning:

11 (i) Any intermediary bank or funds-transfer system to  
12 be used in carrying out the funds transfer; or

13 (ii) The means by which payment orders are to be  
14 transmitted in the funds transfer. If the originator's  
15 bank issues a payment order to an intermediary bank,  
16 the originator's bank is obliged to instruct the  
17 intermediary bank according to the instruction of the  
18 originator. An intermediary bank in the funds transfer  
19 is similarly bound by an instruction given to it by the  
20 sender of the payment order it accepts.

21 (b) If the sender's instruction states that the funds  
22 transfer is to be carried out telephonically or by wire  
23 transfer or otherwise indicates that the funds transfer is  
24 to be carried out by the most expeditious means, the  
25 receiving bank is obliged to transmit its payment order by  
26 the most expeditious available means and to instruct any  
27 intermediary bank accordingly. If a sender's instruction  
28 states a payment date, the receiving bank is obliged to  
29 transmit its payment order at a time and by means reasonably  
30 necessary to allow payment to the beneficiary on the payment  
31 date or as soon thereafter as is feasible.

32 (2) Unless otherwise instructed, a receiving bank executing  
33 a payment order may:

34 (a) Use any funds transfer system if use of that system is  
35 reasonable in the circumstances; and

36 (b) Issue a payment order to the beneficiary's bank or to  
37 an intermediary bank through which a payment order  
38 conforming to the sender's order can expeditiously be issued  
39 to the beneficiary's bank if the receiving bank exercises  
40 ordinary care in the selection of the intermediary bank. A  
41 receiving bank is not required to follow an instruction of

2 the sender designating a funds transfer system used in  
3 carrying out the funds transfer if the receiving bank, in  
4 good faith, determines that it is not feasible to follow the  
5 instruction or that following the instruction unduly delays  
6 completion of the funds transfer.

7 (3) Unless subsection (1), paragraph (b) applies or the  
8 receiving bank is otherwise instructed, the bank may execute a  
9 payment order by transmitting its payment order by first class  
10 mail or by any reasonable means. If the receiving bank is  
11 instructed to execute the sender's order by transmitting its  
12 payment order by a particular means, the receiving bank may issue  
13 its payment order by the means stated or by any equivalent means.

14 (4) Unless instructed by the sender:

15 (a) The receiving bank may not obtain payment of its  
16 charges for services and expenses in connection with the  
17 execution of the sender's order by issuing a payment order  
18 in an amount equal to the amount of the sender's order less  
19 the amount of the charges; and

20 (b) May not instruct a subsequent receiving bank to obtain  
21 payment of its charges in the same manner.

22 **1991 Uniform Comment**

23 1. In the absence of agreement, the receiving bank is not  
24 obliged to execute an order of the sender. Section 4A-212  
25 [section 4-1212]. Section 4A-302 [section 4-1302] states the  
26 manner in which the receiving bank may execute the sender's order  
27 if execution occurs. Subsection (a)(1) [subsection (1)(a)]  
28 states the residual rule. The payment order issued by the  
29 receiving bank must comply with the sender's order and, unless  
30 some other rule is stated in the section, the receiving bank is  
31 obliged to follow any instruction of the sender concerning which  
32 funds transfer system is to be used, which intermediary banks are  
33 to be used, and what means of transmission is to be used. The  
34 instruction of the sender may be incorporated in the payment  
35 order itself or may be given separately. For example, there may  
36 be a master agreement between the sender and receiving bank  
37 containing instructions governing payment orders to be issued  
38 from time to time by the sender to the receiving bank. In most  
39 funds transfers, speed is a paramount consideration. A sender  
40 that wants assurance that the funds transfer will be  
41 expeditiously completed can specify the means to be used. The  
42 receiving bank can follow the instructions literally or it can  
43 use an equivalent means. For example, if the sender instructs  
44 the receiving bank to transmit by telex, the receiving bank could

2 use telephone instead. Subsection (c) [subsection (3)]. In most  
3 cases the sender will not specify a particular means but will use  
4 a general term such as "by wire" or "wire transfer" or "as soon  
5 as possible." These words signify that the sender wants a  
6 same-day transfer. In these cases the receiving bank is required  
7 to use a telephonic or electronic communication to transmit its  
8 order and is also required to instruct any intermediary bank to  
9 which it issues its order to transmit by similar means.  
10 Subsection (a)(2) [subsection (1)(b)]. In other cases, such as  
11 an automated clearing house transfer, a same-day transfer is not  
12 contemplated. Normally the sender's instruction or the context  
13 in which the payment order is received makes clear the type of  
14 funds transfer that is appropriate. If the sender states a  
15 payment date with respect to the payment order, the receiving  
16 bank is obliged to execute the order at a time and in a manner to  
17 meet the payment date if that is feasible. Subsection (a)(2)  
18 [subsection (1)(b)]. This provision would apply to many ACH  
19 transfers made to pay recurring debts of the sender. In other  
20 cases, involving relatively small amounts, time may not be an  
21 important factor and cost may be a more important element. Fast  
22 means, such as telephone or electronic transmission, are more  
23 expensive than slow means such as mailing. Subsection (c)  
24 [subsection (3)] states that in the absence of instructions the  
25 receiving bank is given discretion to decide. It may issue its  
26 payment order by first class mail or by any means reasonable in  
27 the circumstances. Section 4A-305 [section 4-1305] states the  
28 liability of a receiving bank for breach of the obligations  
29 stated in Section 4A-302 [section 4-1302].

30 2. Subsection (b) [subsection (2)] concerns the choice of  
31 intermediary banks to be used in completing the funds transfer,  
32 and the funds transfer system to be used. If the receiving bank  
33 is not instructed about the matter, it can issue an order  
34 directly to the beneficiary's bank or can issue an order to an  
35 intermediary bank. The receiving bank also has discretion  
36 concerning use of a funds transfer system. In some cases it may  
37 be reasonable to use either an automated clearing house system or  
38 a wire transfer system such as Fedwire or CHIPS. Normally, the  
39 receiving bank will follow the instruction of the sender in these  
40 matters, but in some cases it may be prudent for the bank not to  
41 follow instructions. The sender may have designated a funds  
42 transfer system to be used in carrying out the funds transfer,  
43 but it may not be feasible to use the designated system because  
44 of some impediment such as a computer breakdown which prevents  
45 prompt execution of the order. The receiving bank is permitted  
46 to use an alternate means of transmittal in a good faith effort  
47 to execute the order expeditiously. The same leeway is not given  
48 to the receiving bank if the sender designates an intermediary  
bank through which the funds transfer is to be routed. The

2 sender's designation of that intermediary bank may mean that the  
3 beneficiary's bank is expecting to obtain a credit from that  
4 intermediary bank and may have relied on that anticipated  
5 credit. If the receiving bank uses another intermediary bank the  
6 expectations of the beneficiary's bank may not be realized. The  
7 receiving bank could choose to route the transfer to another  
8 intermediary bank and then to the designated intermediary bank if  
9 there were some reason such as a lack of a correspondent-bank  
10 relationship or a bilateral credit limitation, but the designated  
11 intermediary bank cannot be circumvented. To do so violates the  
12 sender's instructions.

13 3. The normal rule, under subsection (a)(1) [subsection  
14 (1)(a)], is that the receiving bank, in executing a payment  
15 order, is required to issue a payment order that complies as to  
16 amount with that of the sender's order. In most cases the  
17 receiving bank issues an order equal to the amount of the  
18 sender's order and makes a separate charge for services and  
19 expenses in executing the sender's order. In some cases,  
20 particularly if it is an intermediary bank that is executing an  
21 order, charges are collected by deducting them from the amount of  
22 the payment order issued by the executing bank. If that is done,  
23 the amount of the payment order accepted by the beneficiary's  
24 bank will be slightly less than the amount of the originator's  
25 payment order. For example, Originator, in order to pay an  
26 obligation of \$1,000,000 owed to Beneficiary, issues a payment  
27 order to Originator's Bank to pay \$1,000,000 to the account of  
28 Beneficiary in Beneficiary's Bank. Originator's Bank issues a  
29 payment order to Intermediary Bank for \$1,000,000 and debits  
30 Originator's account for \$1,000,010. The extra \$10 is the fee of  
31 Originator's Bank. Intermediary Bank executes the payment order  
32 of Originator's Bank by issuing a payment order to Beneficiary's  
33 Bank for \$999,990, but under §4A-402(c) [section 4-1402(3)] is  
34 entitled to receive \$1,000,000 from Originator's Bank. The \$10  
35 difference is the fee of Intermediary Bank. Beneficiary's Bank  
36 credits Beneficiary's account for \$999,990. When Beneficiary's  
37 Bank accepts the payment order of Intermediary Bank the result is  
38 a payment of \$999,990 from Originator to Beneficiary. Section  
39 4A-406(a) [subsection 4-1406(1)]. If that payment discharges the  
40 \$1,000,000 debt, the effect is that Beneficiary has paid the  
41 charges of Intermediary Bank and Originator has paid the charges  
42 of Originator's Bank. Subsection (d) of Section 4A-302 [section  
43 4-1302(4)] allows Intermediary Bank to collect its charges by  
44 deducting them from the amount of the payment order, but only if  
45 instructed to do so by Originator's Bank. Originator's Bank is  
46 not authorized to give that instruction to Intermediary Bank  
47 unless Originator authorized the instruction. Thus, Originator  
48 can control how the charges of Originator's Bank and Intermediary

2 Bank are to be paid. Subsection (d) [subsection (4)] does not  
3 apply to charges of Beneficiary's Bank to Beneficiary.

4 In the case discussed in the preceding paragraph the \$10  
5 charge is trivial in relation to the amount of the payment and it  
6 may not be important to Beneficiary how the charge is paid. But  
7 it may be very important if the \$1,000,000 obligation represented  
8 the price of exercising a right such as an option favorable to  
9 Originator and unfavorable to Beneficiary. Beneficiary might  
10 well argue that it was entitled to receive \$1,000,000. If the  
11 option was exercised shortly before its expiration date, the  
12 result could be loss of the option benefit because the required  
13 payment of \$1,000,000 was not made before the option expired.  
14 Section 4A-406(c) [section 4-1406(3)] allows Originator to  
15 preserve the option benefit. The amount received by Beneficiary  
16 is deemed to be \$1,000,000 unless Beneficiary demands the \$10 and  
17 Originator does not pay it.

#### 18 §4-1303. Erroneous execution of payment order

19  
20 (1) A receiving bank that executes the payment order of the  
21 sender by issuing a payment order in an amount greater than the  
22 amount of the sender's order or issues a payment order in  
23 execution of the sender's order and then issues a duplicate order  
24 is entitled to payment of the amount of the sender's order under  
25 section 4-1402, subsection (3) if that subsection is otherwise  
26 satisfied. The bank is entitled to recover from the beneficiary  
27 of the erroneous order the excess payment received to the extent  
28 allowed by the law governing mistake and restitution.

29  
30 (2) A receiving bank that executes the payment order of the  
31 sender by issuing a payment order in an amount less than the  
32 amount of the sender's order is entitled to payment of the amount  
33 of the sender's order under section 4-1402, subsection (3) if  
34 that subsection is otherwise satisfied and the bank corrects its  
35 mistake by issuing an additional payment order for the benefit of  
36 the beneficiary of the sender's order. If the error is not  
37 corrected, the issuer of the erroneous order is entitled to  
38 receive or retain payment from the sender of the order to  
39 accepted only to the extent of the amount of the erroneous  
40 order. This subsection does not apply if the receiving bank  
41 executes the sender's payment order by issuing a payment order in  
42 an amount less than the amount of the sender's order for the  
43 purpose of obtaining payment of its charges for services and  
44 expenses pursuant to an instruction of the sender.

45  
46 (3) If a receiving bank executes the payment order of the  
47 sender by issuing a payment order to a beneficiary different from  
48 the beneficiary of the sender's order and the funds transfer is

completed on the basis of that error, the sender of the payment order that was erroneously executed and all previous senders in the funds transfer are not obliged to pay the payment orders they issued. The issuer of the erroneous order is entitled to recover from the beneficiary of the order the payment received to the extent allowed by the law governing mistake and restitution.

1991 Uniform Comment

1. Section 4A-303 [section 4-1303] states the effect of erroneous execution of a payment order by the receiving bank. Under Section 4A-402(c) [section 4-1402(3)] the sender of a payment order is obliged to pay the amount of the order to the receiving bank if the bank executes the order, but the obligation to pay is excused if the beneficiary's bank does not accept a payment order instructing payment to the beneficiary of the sender's order. If erroneous execution of the sender's order causes the wrong beneficiary to be paid, the sender is not required to pay. If erroneous execution causes the wrong amount to be paid the sender is not obliged to pay the receiving bank an amount in excess of the amount of the sender's order. Section 4A-303 [section 4-1303] takes precedence over Section 4A-402(c) [section 4-1402(3)] and states the liability of the sender and the rights of the receiving bank in various cases of erroneous execution.

2. Subsections (a) and (b) [subsections (1) and (2)] deal with cases in which the receiving bank executes by issuing a payment order in the wrong amount. If Originator ordered Originator's Bank to pay \$1,000,000 to the account of Beneficiary in Beneficiary's Bank, but Originator's Bank erroneously instructed Beneficiary's Bank to pay \$2,000,000 to Beneficiary's account, subsection (a) [subsection (1)] applies. If Beneficiary's Bank accepts the order of Originator's Bank, Beneficiary's Bank is entitled to receive \$2,000,000 from Originator's Bank, but Originator's Bank is entitled to receive only \$1,000,000 from Originator. Originator's Bank is entitled to recover the overpayment from Beneficiary to the extent allowed by the law governing mistake and restitution. Originator's Bank would normally have a right to recover the overpayment from Beneficiary, but in unusual cases the law of restitution might allow Beneficiary to keep all or part of the overpayment. For example, if Originator owed \$2,000,000 to Beneficiary and Beneficiary received the extra \$1,000,000 in good faith in discharge of the debt, Beneficiary may be allowed to keep it. In this case Originator's Bank has paid an obligation of Originator and under the law of restitution, which applies through Section 1-103, Originator's Bank would be subrogated to Beneficiary's

rights against Originator on the obligation paid by Originator's Bank.

If Originator's Bank erroneously executed Originator's order by instructing Beneficiary's Bank to pay less than \$1,000,000, subsection (b) [subsection (2)] applies. If Originator's Bank corrects its error by issuing another payment order to Beneficiary's Bank that results in payment of \$1,000,000 to Beneficiary, Originator's Bank is entitled to payment of \$1,000,000 from Originator. If the mistake is not corrected, Originator's Bank is entitled to payment from Originator only in the amount of the order issued by Originator's Bank.

3. Subsection (a) [subsection (1)] also applies to duplicate payment orders. Assume Originator's Bank properly executes Originator's \$1,000,000 payment order and then by mistake issues a second \$1,000,000 payment order in execution of Originator's order. If Beneficiary's Bank accepts both orders issued by Originator's Bank, Beneficiary's Bank is entitled to receive \$2,000,000 from Originator's Bank but Originator's Bank is entitled to receive only \$1,000,000 from Originator. The remedy of Originator's Bank is the same as that of a receiving bank that executes by issuing an order in an amount greater than the sender's order. It may recover the overpayment from Beneficiary to the extent allowed by the law governing mistake and restitution and in a proper case as stated in Comment 2 may have subrogation rights if it is not entitled to recover from Beneficiary.

4. Suppose Originator instructs Originator's Bank to pay \$1,000,000 to Account # 12345 in Beneficiary's Bank. Originator's Bank erroneously instructs Beneficiary's Bank to pay \$1,000,000 to Account # 12346 and Beneficiary's Bank accepted. Subsection (c) [subsection (3)] covers this case. Originator is not obliged to pay its payment order, but Originator's Bank is required to pay \$1,000,000 to Beneficiary's Bank. The remedy of Originator's Bank is to recover \$1,000,000 from the holder of Account # 12346 that received payment by mistake. Recovery based on the law of mistake and restitution is described in Comment 2.

§4-1304. Duty of sender to report erroneously executed payment order

If the sender of a payment order that is erroneously executed as stated in section 4-1303 receives notification from the receiving bank that the order was executed or that the sender's account was debited with respect to the order, the sender has a duty to exercise ordinary care to determine, on the basis of information available to the sender, that the order was

erroneously executed and to notify the bank of the relevant facts within a reasonable time not exceeding 90 days after the notification from the bank was received by the sender. If the sender fails to perform that duty, the bank is not obliged to pay interest on any amount refundable to the sender under section 4-1402, subsection (4) for the period before the bank learns of the execution error. The bank is not entitled to any recovery from the sender because the sender failed to perform the duty stated in this section.

1991 Uniform Comment

This section is identical in effect to Section 4A-204 [section 4-1204] which applies to unauthorized orders issued in the name of a customer of the receiving bank. The rationale is stated in Comment 2 to Section 4A-204 [section 4-1204].

§4-1305. Liability for late or improper execution or failure to execute payment order

(1) If a funds transfer is completed but execution of a payment order by the receiving bank in breach of section 4-1302 results in delay in payment to the beneficiary, the bank is obliged to pay interest to either the originator or the beneficiary of the funds transfer for the period of delay caused by the improper execution. Except as provided in subsection (3), additional damages are not recoverable.

(2) If execution of a payment order by a receiving bank in breach of section 4-1302 results in noncompletion of the funds transfer, failure to use an intermediary bank designated by the originator or issuance of a payment order that does not comply with the terms of the payment order of the originator, the bank is liable to the originator for its expenses in the funds transfer and for incidental expenses and interest losses, to the extent not covered by subsection (1), resulting from the improper execution. Except as provided in subsection (3), additional damages are not recoverable.

(3) In addition to the amounts payable under subsections (1) and (2), damages, including consequential damages, are recoverable to the extent provided in an express written agreement of the receiving bank.

(4) If a receiving bank fails to execute a payment order it was obliged by express agreement to execute, the receiving bank is liable to the sender for its expenses in the transaction and for incidental expenses and interest losses resulting from the failure to execute. Additional damages, including consequential

damages, are recoverable to the extent provided in an express written agreement of the receiving bank but are not otherwise recoverable.

(5) Reasonable attorney's fees are recoverable if demand for compensation under subsection (1) or (2) is made and refused before an action is brought on the claim. If a claim is made for breach of an agreement under subsection (4) and the agreement does not provide for damages, reasonable attorney's fees are recoverable if demand for compensation under subsection (4) is made and refused before an action is brought on the claim.

(6) Except as stated in this section, the liability of a receiving bank under subsections (1) and (2) may not be varied by agreement.

1991 Uniform Comment

1. Subsection (a) [subsection (1)] covers cases of delay in completion of a funds transfer resulting from an execution by a receiving bank in breach of Section 4A-302(a) [section 4-1302(1)]. The receiving bank is obliged to pay interest on the amount of the order for the period of the delay. The rate of interest is stated in Section 4A-506 [section 4-1506]. With respect to wire transfers (other than ACH transactions) within the United States, the expectation is that the funds transfer will be completed the same day. In those cases, the originator can reasonably expect that the originator's account will be debited on the same day as the beneficiary's account is credited. If the funds transfer is delayed, compensation can be paid either to the originator or to the beneficiary. The normal practice is to compensate the beneficiary's bank to allow that bank to compensate the beneficiary by back-valuing the payment by the number of days of delay. Thus, the beneficiary is in the same position that it would have been in if the funds transfer had been completed on the same day. Assume on Day 1, Originator's Bank issues its payment order to Intermediary Bank which is received on that day. Intermediary Bank does not execute that order until Day 2 when it issues an order to Beneficiary's Bank which is accepted on that day. Intermediary Bank complies with subsection (a) [subsection (1)] by paying one day's interest to Beneficiary's Bank for the account of Beneficiary.

2. Subsection (b) [subsection (2)] applies to cases of breach of Section 4A-302 [section 4-1302] involving more than mere delay. In those cases the bank is liable for damages for improper execution but they are limited to compensation for interest losses and incidental expenses of the sender resulting

2 from the breach, the expenses of the sender in the funds transfer  
and attorney's fees. This subsection reflects the judgment that  
4 imposition of consequential damages on a bank for commission of  
an error is not justified.

6 The leading common law case on the subject of consequential  
damages is Evra Corp. v. Swiss Bank Corp., 673 F.2d 951 (7th Cir.  
8 1982), in which Swiss Bank, an intermediary bank, failed to  
execute a payment order. Because the beneficiary did not receive  
10 timely payment the originator lost a valuable ship charter. The  
lower court awarded the originator \$2.1 million for lost profits  
12 even though the amount of the payment order was only \$27,000.  
The Seventh Circuit reversed, in part on the basis of the common  
14 law rule of Hadley v. Baxendale that consequential damages may  
not be awarded unless the defendant is put on notice of the  
16 special circumstances giving rise to them. Swiss Bank may have  
known that the originator was paying the shipowner for the hire  
18 of a vessel but did not know that a favorable charter would be  
lost if the payment was delayed. "Electronic payments are not so  
20 unusual as to automatically place a bank on notice of  
extraordinary consequences if such a transfer goes awry. Swiss  
22 Bank did not have enough information to infer that if it lost a  
\$27,000 payment order it would face liability in excess of  
24 \$2 million." 673 F.2d at 956.

26 If Evra means that consequential damages can be imposed if  
the culpable bank has notice of particular circumstances giving  
28 rise to the damages, it does not provide an acceptable solution  
to the problem of bank liability for consequential damages. In  
30 the typical case transmission of the payment order is made  
electronically. Personnel of the receiving bank that process  
32 payment orders are not the appropriate people to evaluate the  
risk of liability for consequential damages in relation to the  
34 price charged for the wire transfer service. Even if notice is  
received by higher level management personnel who could make an  
36 appropriate decision whether the risk is justified by the price,  
liability based on notice would require evaluation of payment  
38 orders on an individual basis. This kind of evaluation is  
inconsistent with the high-speed, low price, mechanical nature of  
40 the processing system that characterizes wire transfers.  
Moreover, in Evra the culpable bank was an intermediary bank with  
42 which the originator did not deal. Notice to the originator's  
bank would not bind the intermediary bank, and it seems  
44 impractical for the originator's bank to convey notice of this  
kind to intermediary banks in the funds transfer. The success of  
46 the wholesale wire transfer industry has largely been based on  
its ability to effect payment at low cost and great speed. Both  
48 of these essential aspects of the modern wire transfer system  
would be adversely affected by a rule that imposed on banks

2 liability for consequential damages. A banking industry amicus  
brief in Evra stated: "Whether banks can continue to make EFT  
4 services available on a widespread basis, by charging reasonable  
rates, depends on whether they can do so without incurring  
unlimited consequential risks. Certainly, no bank would handle  
6 for \$3.25 a transaction entailing potential liability in the  
millions of dollars.

8 As the court in Evra also noted, the originator of the funds  
transfer is in the best position to evaluate the risk that a  
10 funds transfer will not be made on time and to manage that risk  
by issuing a payment order in time to allow monitoring of the  
12 transaction. The originator, by asking the beneficiary, can  
quickly determine if the funds transfer has been completed. If  
14 the originator has sent the payment order at a time that allows a  
reasonable margin for correcting error, no loss is likely to  
16 result if the transaction is monitored. The other published  
cases on this issue reach the Evra result. Central Coordinates,  
18 Inc. v. Morgan Guaranty Trust Co., 40 U.C.C. Rep. Serv. 1340  
(N.Y. Sup. Ct. 1985), and Gatcoil (U.S.A.), Inc. v. Forest Hill  
20 State Bank, 1 U.C.C. Rep. Serv. 2d 171 (D. Md. 1986).

22 Subsection (c) [subsection (3)] allows the measure of  
24 damages in subsection (b) [subsection (2)] to be increased by an  
express written agreement of the receiving bank. An originator's  
26 bank might be willing to assume additional responsibilities and  
incur additional liability in exchange for a higher fee.

28 3. Subsection (d) [subsection (4)] governs cases in which a  
receiving bank has obligated itself by express agreement to  
30 accept payment orders of a sender. In the absence of such an  
agreement there is no obligation by a receiving bank to accept a  
32 payment order. Section 4A-212 [section 4-1212]. The measure of  
damages for breach of an agreement to accept a payment order is  
34 the same as that stated in subsection (b) [subsection (2)]. As  
in the case of subsection (b) [subsection (2)], additional  
36 damages, including consequential damages, may be recovered to the  
extent stated in an express written agreement of the receiving  
38 bank.

40 4. Reasonable attorney's fees are recoverable only in cases  
in which damages are limited to statutory damages stated in  
42 subsections (a), (b) and (d) [subsections (1), (2) and (4)]. If  
additional damages are recoverable because provided for by an  
44 express written agreement, attorney's fees are not recoverable.  
The rationale is that there is no need for statutory attorney's  
46 fees in the latter case, because the parties have agreed to a  
measure of damages which may or may not provide for attorney's  
48 fees.

2 5. The effect of subsection (f) [subsection (6)] is to  
4 prevent reduction of a receiving bank's liability under Section  
4A-305 [section 4-1305].

6 **PART 4**

8 **PAYMENT**

10 **§4-1401. Payment date**

12 "Payment date" of a payment order means the day on which the  
14 amount of the order is payable to the beneficiary by the  
16 beneficiary's bank. The payment date may be determined by  
18 instruction of the sender but can not be earlier than the day the  
20 order is received by the beneficiary's bank and, unless otherwise  
22 determined, is the day the order is received by the beneficiary's  
24 bank.

20 **1991 Uniform Comment**

22 "Payment date" refers to the day the beneficiary's bank is  
24 to pay the beneficiary. The payment date may be expressed in  
26 various ways so long as it indicates the day the beneficiary is  
28 to receive payment. For example, in ACH transfers the payment  
30 date is the equivalent of "settlement date" or "effective date."  
32 Payment date applies to the payment order issued to the  
34 beneficiary's bank, but a payment order issued to a receiving  
36 bank other than the beneficiary's bank may also state a date for  
38 payment to the beneficiary. In the latter case, the statement of  
40 a payment date is to instruct the receiving bank concerning time  
42 of execution of the sender's order. Section 4A-301(b) [section  
44 4-1301(2)].

34 **§4-1402. Obligation of sender to pay receiving bank**

36 (1) This section is subject to sections 4-1205 and 4-1207.

38 (2) With respect to a payment order issued to the  
40 beneficiary's bank, acceptance of the order by the bank obliges  
42 the sender to pay the bank the amount of the order but payment is  
44 not due until the payment date of the order.

44 (3) This subsection is subject to subsection (5) and to  
46 section 4-1303. With respect to a payment order issued to a  
48 receiving bank other than the beneficiary's bank, acceptance of  
the order by the receiving bank obliges the sender to pay the  
bank the amount of the sender's order. Payment by the sender is  
not due until the execution date of the sender's order. The

2 obligation of that sender to pay its payment order is excused if  
4 the funds transfer is not completed by acceptance by the  
6 beneficiary's bank of a payment order instructing payment to the  
8 beneficiary of that sender's payment order.

6 (4) If the sender of a payment order pays the order and was  
8 not obliged to pay all or part of the amount paid, the bank  
10 receiving payment is obliged to refund payment to the extent the  
12 sender was not obliged to pay. Except as provided in sections  
14 4-1204 and 4-1304, interest is payable on the refundable amount  
16 from the date of payment.

14 (5) If a funds transfer is not completed as stated in  
16 subsection (3) and an intermediary bank is obliged to refund  
18 payment as stated in subsection (4) but is unable to do so  
20 because not permitted by applicable law or because the bank  
22 suspends payments, a sender in the funds transfer that executed a  
24 payment order in compliance with an instruction, as stated in  
26 section 4-1302, subsection (1), paragraph (a), to route the funds  
28 transfer through that intermediary bank is entitled to receive or  
30 retain payment from the sender of the payment order that it  
32 accepted. The first sender in the funds transfer that issued an  
34 instruction requiring routing through that intermediary bank is  
36 subrogated to the right of the bank that paid the intermediary  
38 bank to refund as stated in subsection (4).

26 (6) The right of the sender of a payment order to be  
28 excused from the obligation to pay the order as stated in  
30 subsection (3) or to receive refund under subsection (4) may not  
32 be varied by agreement.

32 **1991 Uniform Comment**

34 1. Subsection (b) [subsection (2)] states that the sender  
36 of a payment order to the beneficiary's bank must pay the order  
38 when the beneficiary's bank accepts the order. At that point the  
40 beneficiary's bank is obliged to pay the beneficiary. Section  
42 4A-404(a) [section 4-1404(1)]. The last clause of subsection (b)  
44 [subsection (2)] covers a case of premature acceptance by the  
46 beneficiary's bank. In some funds transfers, notably automated  
48 clearing house transfers, a beneficiary's bank may receive a  
payment order with a payment date after the day the order is  
received. The beneficiary's bank might accept the order before  
the payment date by notifying the beneficiary of receipt of the  
order. Although the acceptance obliges the beneficiary's bank to  
pay the beneficiary, payment is not due until the payment date.  
The last clause of subsection (b) [subsection (2)] is consistent  
with that result. The beneficiary's bank is also not entitled to  
payment from the sender until the payment date.

2. Assume that Originator instructs Bank A to order immediate payment to the account of Beneficiary in Bank B. Execution of Originator's payment ordered by Bank A is acceptance under Section 4A-209(a) [section 4-1209(1)]. Under the second sentence of Section 4A-402(c) [section 4-1402(3)] the acceptance creates an obligation of Originator to pay Bank A the amount of the order. The last clause of that sentence deals with attempted funds transfers that are not completed. In that event the obligation of the sender to pay its payment order is excused. Originator makes payment to Beneficiary when Bank B, the beneficiary's bank, accepts a payment order for the benefit of Beneficiary. Section 4A-406(a) [section 4-1406(1)]. If that acceptance by Bank B does not occur, the funds transfer has miscarried because Originator has not paid Beneficiary. Originator doesn't have to pay its payment order, and if it has already paid it is entitled to refund of the payment with interest. The rate of interest is stated in Section 4A-506 [section 4-1506]. This "money-back guarantee" is an important protection of Originator. Originator is assured that it would not lose its money if something goes wrong in the transfer. For example, risk of loss resulting from payment to the wrong beneficiary is borne by some bank, not by Originator. The most likely reason for noncompletion is a failure to execute or an erroneous execution of a payment order by Bank A or an intermediary bank. Bank A may have issued its payment order to the wrong bank or it may have identified the wrong beneficiary in its order. The money-back guarantee is particularly important to Originator if noncompletion of the funds transfer is due to the fault of an intermediary bank rather than Bank A. In that case Bank A must refund payment to Originator, and Bank A has the burden of obtaining refund from the intermediary bank that it paid.

Subsection (c) [subsection (3)] can result in loss if an intermediary bank suspends payments. Suppose Originator instructs Bank A to pay to Beneficiary's account in Bank B and to use Bank C as an intermediary bank. Bank A executes Originator's order by issuing a payment order to Bank C. Bank A pays Bank C. Bank C fails to execute the order of Bank A and suspends payments. Under subsections (c) and (d) [subsections (3) and (4)], Originator is not obliged to pay Bank A and is entitled to refund from Bank A of any payment that it may have made. Bank A is entitled to a refund from Bank C, but Bank C is insolvent. Subsection (e) [subsection (5)] deals with this case. Bank A was required to issue its payment order to Bank C because Bank C was designated as an intermediary bank by Originator. Section 4A-302(a)(1) [section 4-1302(1)(a)]. In this case Originator takes the risk of insolvency of Bank C. Under subsection (e)

[subsection (5)], Bank A is entitled to payment from Originator and Originator is subrogated to the right of Bank A under subsection (d) [subsection (4)] to refund of payment from Bank C.

3. A payment order is not like a negotiable instrument on which the drawer or maker has liability. Acceptance of the order by the receiving bank creates an obligation of the sender to pay the receiving bank the amount of the order. That is the extent of the sender's liability to the receiving bank and no other person has any rights against the sender with respect to the sender's order.

#### §4-1403. Payment by sender to receiving bank

(1) Payment of the sender's obligation under section 4-1402 to pay the receiving bank occurs as follows.

(a) If the sender is a bank, payment occurs when the receiving bank receives final settlement of the obligation through a Federal Reserve Bank or through a funds transfer system.

(b) If the sender is a bank and the sender credited an account of the receiving bank with the sender or caused an account of the receiving bank in another bank to be credited, payment occurs when the credit is withdrawn or, if not withdrawn, at midnight of the day on which the credit is withdrawable and the receiving bank learns of that fact.

(c) If the receiving bank debits an account of the sender with the receiving bank, payment occurs when the debit is made to the extent the debit is covered by a withdrawable credit balance in the account.

(2) If the sender and receiving bank are members of a funds transfer system that nets obligations multilaterally among participants, the receiving bank receives final settlement when settlement is complete in accordance with the rules of the system. The obligation of the sender to pay the amount of a payment order transmitted through the funds transfer system may be satisfied, to the extent permitted by the rules of the system, by setting off and applying against the sender's obligation the right of the sender to receive payment from the receiving bank of the amount of any other payment order transmitted to the sender by the receiving bank through the funds transfer system. The aggregate balance of obligations owed by each sender to each receiving bank in the funds transfer system may be satisfied, to the extent permitted by the rules of the system, by setting off and applying against that balance the aggregate balance of



obligations owed to the sender by other members of the system. The aggregate balance is determined after the right of setoff stated in this subsection has been exercised.

(3) If 2 banks transmit payment orders to each other under an agreement that settlement of the obligations of each bank to the other under section 4-1402 will be made at the end of the day or other period, the total amount owed with respect to all orders transmitted by one bank is set off against the total amount owed with respect to all orders transmitted by the other bank. To the extent of the setoff, each bank has made payment to the other.

(4) In a case not covered by subsection (1), the time when payment of the sender's obligation under section 4-1402, subsection (2) or subsection (3) occurs is governed by applicable principles of law that determine when an obligation is satisfied.

1991 Uniform Comment

1. This section defines when a sender pays the obligation stated in Section 4A-402 [section 4-1402]. If a group of two or more banks engage in funds transfers with each other, the participating banks will sometimes be senders and sometimes receiving banks. With respect to payment orders other than Fedwires, the amounts of the various payment orders may be credited and debited to accounts of one bank with another or to a clearing house account of each bank and amounts owed and amounts due are netted. Settlement is made through a Federal Reserve Bank by charges to the Federal Reserve accounts of the net debtor banks and credits to the Federal Reserve accounts of the net creditor banks. In the case of Fedwires the sender's obligation is settled by a debit to the Federal Reserve account of the sender and a credit to the Federal Reserve account of the receiving bank at the time the receiving bank receives the payment order. Both of these cases are covered by subsection (a)(1) [subsection (1)(a)]. When the Federal Reserve settlement becomes final the obligation of the sender under Section 4A-402 [section 4-1402] is paid.

2. In some cases a bank does not settle an obligation owed to another bank through a Federal Reserve Bank. This is the case if one of the banks is a foreign bank without access to the Federal Reserve payment system. In this kind of case, payment is usually made by credits or debits to accounts of the two banks with each other or to accounts of the two banks in a third bank. Suppose Bank B has an account in Bank A. Bank A advises Bank B that its account in Bank A has been credited \$1,000,000 and that the credit is immediately withdrawable. Bank A also instructs Bank B to pay \$1,000,000 to the account of Beneficiary in Bank

B. This case is covered by subsection (a)(2) [subsection (1)(h)]. Bank B may want to immediately withdraw this credit. For example, it might do so by instructing Bank A to debit the account and pay some third party. Payment by Bank A to Bank B of Bank A's payment order occurs when the withdrawal is made. Suppose Bank B does not withdraw the credit. Since Bank B is the beneficiary's bank, one of the effects of receipt of payment by Bank B is that acceptance of Bank A's payment order automatically occurs at the time of payment. Section 4A-209(b)(2) [section 4-1209(2)(b)]. Acceptance means that Bank B is obliged to pay \$1,000,000 to Beneficiary. Section 4A-404(a) [section 4-1404(1)]. Subsection (a)(2) of Section 4A-403 [section 4-1403(1)(b)] states that payment does not occur until midnight if the credit is not withdrawn. This allows Bank B an opportunity to reject the order if it does not have time to withdraw the credit to its account and it is not willing to incur the liability to Beneficiary before it has use of the funds represented by the credit.

3. Subsection (a)(3) [subsection (1)(c)] applies to a case in which the sender (bank or nonbank) has a funded account in the receiving bank. If Sender has an account in Bank and issues a payment order to Bank, Bank can obtain payment from Sender by debiting the account of Sender, which pays its Section 4A-402 [section 4-1402] obligation to Bank when the debit is made.

4. Subsection (b) [subsection (2)] deals with multilateral settlements made through a funds transfer system and is based on the CHIPS settlement system. In a funds transfer system such as CHIPS, which allows the various banks that transmit payment orders over the system to settle obligations at the end of each day, settlement is not based on individual payment orders. Each bank using the system engages in funds transfers with many other banks using the system. Settlement for any participant is based on the net credit or debit position of that participant with all other banks using the system. Subsection (b) [subsection (2)] is designed to make clear that the obligations of any sender are paid when the net position of that sender is settled in accordance with the rules of the funds transfer system. This provision is intended to invalidate any argument, based on common-law principles, that multilateral netting is not valid because mutuality of obligation is not present. Subsection (b) [subsection (2)] dispenses with any mutuality of obligation requirements. Subsection (c) [subsection (3)] applies to cases in which two banks send payment orders to each other during the day and settle with each other at the end of the day or at the end of some other period. It is similar to subsection (b) [subsection (2)] in that it recognizes that a sender's obligation to pay a payment order is satisfied by a setoff. The obligations

of each bank as sender to the other as receiving bank are obligations of the bank itself and not as representative of customers. These two sections are important in the case of insolvency of a bank. They make clear that liability under Section 4A-402 [section 4-1402] is based on the net position of the insolvent bank after setoff.

5. Subsection (d) [subsection (4)] relates to the uncommon case in which the sender doesn't have an account relationship with the receiving bank and doesn't settle through a Federal Reserve Bank. An example would be a customer that pays over the counter for a payment order that the customer issues to the receiving bank. Payment would normally be by cash, check or bank obligation. When payment occurs is determined by law outside Article 4A [Article 4-A].

§4-1404. Obligation of beneficiary's bank to pay and give notice to beneficiary

(1) Subject to section 4-1211, subsection (5), and section 4-1405, subsections (4) and (5), if a beneficiary's bank accepts a payment order, the bank is obliged to pay the amount of the order to the beneficiary of the order. Payment is due on the payment date of the order, but if acceptance occurs on the payment date after the close of the funds transfer business day of the bank, payment is due on the next funds transfer business day. If the bank refuses to pay after demand by the beneficiary and receipt of notice of particular circumstances that will give rise to consequential damages as a result of nonpayment, the beneficiary may recover damages resulting from the refusal to pay to the extent the bank had notice of the damages, unless the bank proves that it did not pay because of a reasonable doubt concerning the right of the beneficiary to payment.

(2) If a payment order accepted by the beneficiary's bank instructs payment to an account of the beneficiary, the bank is obliged to notify the beneficiary of receipt of the order before midnight of the next funds transfer business day following the payment date. If the payment order does not instruct payment to an account of the beneficiary, the bank is required to notify the beneficiary only if notice is required by the order. Notice may be given by first class mail or any other means reasonable in the circumstances. If the bank fails to give the required notice, the bank is obliged to pay interest to the beneficiary on the amount of the payment order from the day notice should have been given until the day the beneficiary learned of receipt of the payment order by the bank. Other damages are not recoverable. Reasonable attorney's fees are also recoverable if demand for

interest is made and refused before an action is brought on the claim.

(3) The right of a beneficiary to receive payment and damages as stated in subsection (1) may not be varied by agreement or a funds transfer system rule. The right of a beneficiary to be notified as stated in subsection (2) may be varied by agreement of the beneficiary or by a funds transfer system rule if the beneficiary is notified of the rule before initiation of the funds transfer.

1991 Uniform Comment .

1. The first sentence of subsection (a) [subsection (1)] states the time when the obligation of the beneficiary's bank arises. The second and third sentences state when the beneficiary's bank must make funds available to the beneficiary. They also state the measure of damages for failure, after demand, to comply. Since the Expedited Funds Availability Act, 12 U.S.C. 4001 et seq., also governs funds availability in a funds transfer, the second and third sentences of subsection (a) [subsection (1)] may be subject to preemption by that Act.

2. Subsection (a) [subsection (1)] provides that the beneficiary of an accepted payment order may recover consequential damages if the beneficiary's bank refuses to pay the order after demand by the beneficiary if the bank at that time had notice of the particular circumstances giving rise to the damages. Such damages are recoverable only to the extent the bank had "notice of the damages." The quoted phrase requires that the bank have notice of the general type or nature of the damages that will be suffered as a result of the refusal to pay and their general magnitude. There is no requirement that the bank have notice of the exact or even the approximate amount of the damages, but if the amount of damages is extraordinary the bank is entitled to notice of that fact. For example, in *Evra Corp. v. Swiss Bank Corp.*, 673 F.2d 951 (7th Cir. 1982), failure to complete a funds transfer of only \$27,000 required to retain rights to a very favorable ship charter resulted in a claim for more than \$2,000,000 of consequential damages. Since it is not reasonably foreseeable that a failure to make a relatively small payment will result in damages of this magnitude, notice is not sufficient if the beneficiary's bank has notice only that the \$27,000 is necessary to retain rights on a ship charter. The bank is entitled to notice that an exceptional amount of damages will result as well. For example, there would be adequate notice if the bank had been made aware that damages of \$1,000,000 or more might result.

3. Under the last clause of subsection (a) [subsection (1)] the beneficiary's bank is not liable for damages if its refusal to pay was "because of a reasonable doubt concerning the right of the beneficiary to payment." Normally there will not be any question about the right of the beneficiary to receive payment. Normally, the bank should be able to determine whether it has accepted the payment order and, if it has been accepted, the first sentence of subsection (a) [subsection (1)] states that the bank is obliged to pay. There may be uncommon cases, however, in which there is doubt whether acceptance occurred. For example, if acceptance is based on receipt of payment by the beneficiary's bank under Section 4A-403(a)(1) or (2) [section 4-1403(1)(a) or (b)], there may be cases in which the bank is not certain that payment has been received. There may also be cases in which there is doubt about whether the person demanding payment is the person identified in the payment order as beneficiary of the order.

The last clause of subsection (a) [subsection (1)] does not apply to cases in which a funds transfer is being used to pay an obligation and a dispute arises between the originator and the beneficiary concerning whether the obligation is in fact owed. For example, the originator may try to prevent payment to the beneficiary by the beneficiary's bank by alleging that the beneficiary is not entitled to payment because of fraud against the originator or a breach of contract relating to the obligation. The fraud or breach of contract claim of the originator may be grounds for recovery by the originator from the beneficiary after the beneficiary is paid, but it does not affect the obligation of the beneficiary's bank to pay the beneficiary. Unless the payment order has been cancelled pursuant to Section 4A-211(c) [section 4-1211(3)], there is no excuse for refusing to pay the beneficiary and, in a proper case, the refusal may result in consequential damages. Except in the case of a book transfer, in which the beneficiary's bank is also the originator's bank, the originator of a funds transfer cannot cancel a payment order to the beneficiary's bank, with or without the consent of that bank, because the originator is not the sender of that order. Thus, the beneficiary's bank may safely ignore any instruction by the originator to withhold payment to the beneficiary.

4. Subsection (b) [subsection (2)] states the duty of the beneficiary's bank to notify the beneficiary of receipt of the order. If acceptance occurs under Section 4A-209(b)(1) [section 4-1209(2)(a)] the beneficiary is normally notified. Thus, subsection (b) [subsection (2)] applies primarily to cases in which acceptance occurs under Section 4A-209(b)(2) or (3) [section 4-1209(2)(b) or (c)]. Notice under subsection (b) [subsection (2)] is not required if the person entitled to the

notice agrees or a funds transfer system rule provides that notice is not required and the beneficiary is given notice of the rule. In ACH transactions the normal practice is not to give notice to the beneficiary unless notice is requested by the beneficiary. This practice can be continued by adoption of a funds transfer system rule. Subsection (a) [subsection (1)] is not subject to variation by agreement or by a funds transfer system rule.

#### §4-1405. Payment by beneficiary's bank to beneficiary

(1) If the beneficiary's bank credits an account of the beneficiary of a payment order, payment of the bank's obligation under section 4-1404, subsection (1) occurs when and to the extent:

(a) The beneficiary is notified of the right to withdraw the credit;

(b) The bank lawfully applies the credit to a debt of the beneficiary; or

(c) Funds with respect to the order are otherwise made available to the beneficiary by the bank.

(2) If the beneficiary's bank does not credit an account of the beneficiary of a payment order, the time when payment of the bank's obligation under section 4-1404, subsection (1) occurs is governed by principles of law that determine when an obligation is satisfied.

(3) Except as stated in subsections (4) and (5), if the beneficiary's bank pays the beneficiary of a payment order under a condition to payment or agreement of the beneficiary giving the bank the right to recover payment from the beneficiary if the bank does not receive payment of the order, the condition to payment or agreement is not enforceable.

(4) A funds transfer system rule may provide that payments made to a beneficiary of funds transfers made through the system are provisional until receipt of payment by the beneficiary's bank of the payment order it accepted. A beneficiary's bank that makes a payment that is provisional under the rule is entitled to a refund from the beneficiary if:

(a) The rule requires that both the beneficiary and the originator be given notice of the provisional nature of the payment before the funds transfer is initiated;

2 (b) The beneficiary, the beneficiary's bank and the  
3 originator's bank agreed to be bound by the rule; and

4 (c) The beneficiary's bank did not receive payment of the  
5 payment order that it accepted.

6 If the beneficiary is obliged to refund payment to the  
7 beneficiary's bank, acceptance of the payment order by the  
8 beneficiary's bank is nullified and no payment by the originator  
9 of the funds transfer to the beneficiary occurs under section  
10 4-1406.

11 (5) This subsection applies to a funds transfer that  
12 includes a payment order transmitted over a funds transfer system  
13 that nets obligations multilaterally among participants and has  
14 in effect a loss-sharing agreement among participants for the  
15 purpose of providing funds necessary to complete settlement of  
16 the obligations of one or more participants that do not meet  
17 their settlement obligations. If the beneficiary's bank in the  
18 funds transfer accepts a payment order and the system fails to  
19 complete settlement pursuant to its rules with respect to any  
20 payment order in the funds transfer:

21 (a) The acceptance by the beneficiary's bank is nullified  
22 and no person has any right or obligation based on the  
23 acceptance.

24 (b) The beneficiary's bank is entitled to recover payment  
25 from the beneficiary.

26 (c) No payment by the originator to the beneficiary occurs  
27 under section 4-1406; and

28 (d) Subject to section 4-1402, subsection (5), each sender  
29 in the funds transfer is excused from its obligation to pay  
30 its payment order under section 4-1402, subsection (3)  
31 because the funds transfer has not been completed.

32 **1991 Uniform Comment**

33 1. This section defines when the beneficiary's bank pays  
34 the beneficiary and when the obligation of the beneficiary's bank  
35 under Section 4A-404 [section 4-1404] to pay the beneficiary is  
36 satisfied. In almost all cases the bank will credit an account  
37 of the beneficiary when it receives a payment order. In the  
38 typical case the beneficiary is paid when the beneficiary is  
39 given notice of the right to withdraw the credit. Subsection  
40 (a)(i) [subsection (1)(a)]. In some cases payment might be made  
41 to the beneficiary not by releasing funds to the beneficiary, but

2 by applying the credit to a debt of the beneficiary. Subsection  
3 (a)(ii) [subsection (1)(b)]. In this case the beneficiary gets  
4 the benefit of the payment order because a debt of the  
5 beneficiary has been satisfied. The two principal cases in which  
6 payment will occur in this manner are setoff by the beneficiary's  
7 bank and payment of the proceeds of the payment order to a  
8 garnishing creditor of the beneficiary. These cases are  
9 discussed in Comment 2 to Section 4A-502 [section 4-1502].

10 2. If a beneficiary's bank releases funds to the  
11 beneficiary before it receives payment from the sender of the  
12 payment order, it assumes the risk that the sender may not pay  
13 the sender's order because of suspension of payments or other  
14 reason. Subsection (c) [subsection (3)]. As stated in Comment 5  
15 to Section 4A-209 [section 4-1209], the beneficiary's bank can  
16 protect itself against this risk by delaying acceptance. But if  
17 the bank accepts the order it is obliged to pay the beneficiary.  
18 If the beneficiary's bank has given the beneficiary notice of the  
19 right to withdraw a credit made to the beneficiary's account, the  
20 beneficiary has received payment from the bank. Once payment has  
21 been made to the beneficiary with respect to an obligation  
22 incurred by the bank under Section 4A-404(a) [section 4-1404(1)],  
23 the payment cannot be recovered by the beneficiary's bank unless  
24 subsection (d) or (e) [subsection (4) or (5)] applies. Thus, a  
25 right to withdraw a credit cannot be revoked if the right to  
26 withdraw constituted payment of the bank's obligation. This  
27 principle applies even if funds were released as a "loan" (see  
28 Comment 5 to Section 4A-209 [section 4-1209]), or were released  
29 subject to a condition that they would be repaid in the event the  
30 bank does not receive payment from the sender of the payment  
31 order, or the beneficiary agreed to return the payment if the  
32 bank did not receive payment from the sender.

33 3. Subsection (c) [subsection (3)] is subject to an  
34 exception stated in subsection (d) [subsection (4)] which is  
35 intended to apply to automated clearing house transfers. ACH  
36 transfers are made in batches. A beneficiary's bank will  
37 normally accept, at the same time and as part of a single batch,  
38 payment orders with respect to many different originator's  
39 banks. Comment 2 to Section 4A-206 [section 4-1206]. The custom  
40 in ACH transactions is to release funds to the beneficiary early  
41 on the payment date even though settlement to the beneficiary's  
42 bank does not occur until later in the day. The understanding is  
43 that payments to beneficiaries are provisional until the  
44 beneficiary's bank receives settlement. This practice is similar  
45 to what happens when a depository bank releases funds with  
46 respect to a check forwarded for collection. If the check is  
47 dishonored the bank is entitled to recover the funds from the  
48 customer. ACH transfers are widely perceived as check

2 substitutes. Section 4A-405(d) [section 4-1405(4)] allows the  
3 funds transfer system to adopt a rule making payments to  
4 beneficiaries provisional. If such a rule is adopted, a  
5 beneficiary's bank that releases funds to the beneficiary will be  
6 able to recover the payment if it doesn't receive payment of the  
7 payment order that it accepted. There are two requirements with  
8 respect to the funds transfer system rule. The beneficiary, the  
9 beneficiary's bank and the originator's bank must all agree to be  
10 bound by the rule and the rule must require that both the  
11 beneficiary and the originator be given notice of the provisional  
12 nature of the payment before the funds transfer is initiated.  
13 There is no requirement that the notice be given with respect to  
14 a particular funds transfer. Once notice of the provisional  
15 nature of the payment has been given, the notice is effective for  
16 all subsequent payments to or from the person to whom the notice  
17 was given. Subsection (d) [subsection (4)] provides only that  
18 the funds transfer system rule must require notice to the  
19 beneficiary and the originator. The beneficiary's bank will know  
20 what the rule requires, but it has no way of knowing whether the  
21 originator's bank complied with the rule. Subsection (d)  
22 [subsection (4)] does not require proof that the originator  
23 received notice. If the originator's bank failed to give the  
24 required notice and the originator suffered as a result, the  
25 appropriate remedy is an action by the originator against the  
26 originator's bank based on that failure. But the beneficiary's  
27 bank will not be able to get the benefit of subsection (d)  
28 [subsection (4)] unless the beneficiary had notice of the  
29 provisional nature of the payment because subsection (d)  
30 [subsection (4)] requires an agreement by the beneficiary to be  
31 bound by the rule. Implicit in an agreement to be bound by a  
32 rule that makes a payment provisional is a requirement that  
33 notice be given of what the rule provides. The notice can be  
34 part of the agreement or separately given. For example, notice  
35 can be given by providing a copy of the system's operating rules.

36 With respect to ACH transfers made through a Federal Reserve  
37 Bank acting as an intermediary bank, the Federal Reserve Bank is  
38 obliged under Section 4A-402(b) [section 4-1402(2)] to pay a  
39 beneficiary's bank that accepts the payment order. Unlike  
40 Fedwire transfers, under current ACH practice a Federal Reserve  
41 Bank that processes a payment order does not obligate itself to  
42 pay if the originator's bank fails to pay the Federal Reserve  
43 Bank. It is assumed that the Federal Reserve will use its right  
44 of preemption which is recognized in Section 4A-107 [section  
45 4-1107] to disclaim the Section 4A-402(b) [section 4-1402(2)]  
46 obligation in ACH transactions if it decides to retain the  
47 provisional payment rule.

2 4. Subsection (e) [subsection (5)] is another exception to  
3 subsection (c) [subsection (3)]. It refers to funds transfer  
4 systems having loss-sharing rules described in the subsection.  
5 CHIPS has proposed a rule that fits the description. Under the  
6 CHIPS loss-sharing rule the banks will have agreed to contribute  
7 funds to allow the system to settle for payment orders sent over  
8 the system during the day in the event that one or more banks are  
9 unable to meet their settlement obligations. Subsection (e)  
10 [subsection (5)] applies only if CHIPS fails to settle despite  
11 the loss-sharing rule. Since funds under the loss-sharing rule  
12 will be instantly available to CHIPS and will be in an amount  
13 sufficient to cover any failure that can be reasonably  
14 anticipated, it is extremely unlikely that CHIPS would ever fail  
15 to settle. Thus, subsection (e) [subsection (5)] addresses an  
16 event that should never occur. If that event were to occur, all  
17 payment orders made over the system would be cancelled under the  
18 CHIPS rule. Thus, no bank would receive settlement, whether or  
19 not a failed bank was involved in a particular funds transfer.  
20 Subsection (e) [subsection (5)] provides that each funds transfer  
21 in which there is a payment order with respect to which there is  
22 a settlement failure is unwound. Acceptance by the beneficiary's  
23 bank in each funds transfer is nullified. The consequences of  
24 nullification are that the beneficiary has no right to receive or  
25 retain payment by the beneficiary's bank, no payment is made by  
26 the originator to the beneficiary and each sender in the funds  
27 transfer is, subject to Section 4A-402(e) [section 4-1402(5)],  
28 not obliged to pay its payment order and is entitled to refund  
29 under Section 4A-402(d) [section 4-1402(4)] if it has already  
30 paid.

31 §4-1406. Payment by originator to beneficiary; discharge of  
32 underlying obligation

33 (1) Subject to section 4-1211, subsection (5) and section  
34 4-1405, subsections (4) and (5), the originator of a funds  
35 transfer pays the beneficiary of the originator's payment order  
36 at the time a payment order for the benefit of the beneficiary is  
37 accepted by the beneficiary's bank in the funds transfer and in  
38 an amount equal to the amount of the order accepted by the  
39 beneficiary's bank, but not more than the amount of the  
40 originator's order.

41 (2) If payment under subsection (1) is made to satisfy an  
42 obligation, the obligation is discharged to the same extent  
43 discharge would result from payment to the beneficiary of the  
44 same amount in money, unless:  
45  
46

2 (a) The payment under subsection (1) was made by a means  
3 prohibited by the contract of the beneficiary with respect  
4 to the obligation;

5 (b) The beneficiary, within a reasonable time after  
6 receiving notice of receipt of the order by the  
7 beneficiary's bank, notified the originator of the  
8 beneficiary's refusal of the payment;

9 (c) Funds with respect to the order were not withdrawn by  
10 the beneficiary or applied to a debt of the beneficiary; and

11 (d) The beneficiary would suffer a loss that could  
12 reasonably have been avoided if payment had been made by a  
13 means complying with the contract.

14 If payment by the originator does not result in discharge under  
15 this section, the originator is subrogated to the rights of the  
16 beneficiary to receive payment from the beneficiary's bank under  
17 section 4-1404, subsection (1).

18 (3) For the purpose of determining whether discharge of an  
19 obligation occurs under subsection (2), if the beneficiary's bank  
20 accepts a payment order in an amount equal to the amount of the  
21 originator's payment order less charges of one or more receiving  
22 banks in the funds transfer, payment to the beneficiary is deemed  
23 to be in the amount of the originator's order unless, upon demand  
24 by the beneficiary, the originator does not pay the beneficiary  
25 the amount of the deducted charges.

26 (4) Rights of the originator or of the beneficiary of a  
27 funds transfer under this section may be varied only by agreement  
28 of the originator and the beneficiary.

29 **1991 Uniform Comment**

30 1. Subsection (a) [subsection (1)] states the fundamental  
31 rule of Article 4A [Article 4-A] that payment by the originator  
32 to the beneficiary is accomplished by providing to the  
33 beneficiary the obligation of the beneficiary's bank to pay.  
34 Since this obligation arises when the beneficiary's bank accepts  
35 a payment order, the originator pays the beneficiary at the time  
36 of acceptance and in the amount of the payment order accepted.

37 2. In a large percentage of funds transfers, the transfer  
38 is made to pay an obligation of the originator. Subsection (a)  
39 [subsection (1)] states that the beneficiary is paid by the  
40 originator when the beneficiary's bank accepts a payment order  
41 for the benefit of the beneficiary. When that happens the effect

2 under subsection (b) [subsection (2)] is to substitute the  
3 obligation of the beneficiary's bank for the obligation of the  
4 originator. The effect is similar to that under Article 3 if a  
5 cashier's check payable to the beneficiary had been taken by the  
6 beneficiary. Normally, payment by funds transfer is sought by  
7 the beneficiary because it puts money into the hands of the  
8 beneficiary more quickly. As a practical matter the beneficiary  
9 and the originator will nearly always agree to the funds transfer  
10 in advance. Under subsection (b) [subsection (2)] acceptance by  
11 the beneficiary's bank will result in discharge of the obligation  
12 for which payment was made unless the beneficiary had made a  
13 contract with respect to the obligation which did not permit  
14 payment by the means used. Thus, if there is no contract of the  
15 beneficiary with respect to the means of payment of the  
16 obligation, acceptance by the beneficiary's bank of a payment  
17 order to the account of the beneficiary can result in discharge.

18 3. Suppose Beneficiary's contract stated that payment of an  
19 obligation owed by Originator was to be made by a cashier's check  
20 of Bank A. Instead, Originator paid by a funds transfer to  
21 Beneficiary's account in Bank B. Bank B accepted a payment order  
22 for the benefit of Beneficiary by immediately notifying  
23 Beneficiary that the funds were available for withdrawal. Before  
24 Beneficiary had a reasonable opportunity to withdraw the funds  
25 Bank B suspended payments. Under the "unless" clause of  
26 subsection (b) [subsection (2)] Beneficiary is not required to  
27 accept the payment as discharging the obligation owed by  
28 Originator to Beneficiary if Beneficiary's contract means that  
29 Beneficiary was not required to accept payment by wire transfer.  
30 Beneficiary could refuse the funds transfer as payment of the  
31 obligation and could resort to rights under the underlying  
32 contract to enforce the obligation. The rationale is that  
33 Originator cannot impose the risk of Bank B's insolvency on  
34 Beneficiary if Beneficiary had specified another means of payment  
35 that did not entail that risk. If Beneficiary is required to  
36 accept Originator's payment, Beneficiary would suffer a loss that  
37 would not have occurred if payment had been made by a cashier's  
38 check on Bank A, and Bank A has not suspended payments. In this  
39 case Originator will have to pay twice. It is obliged to pay the  
40 amount of its payment order to the bank that accepted it and has  
41 to pay the obligation it owes to Beneficiary which has not been  
42 discharged. Under the last sentence of subsection (b)  
43 [subsection (2)] Originator is subrogated to Beneficiary's right  
44 to receive payment from Bank B under Section 4A-404(a) [section  
45 4-1404(1)].

46 4. Suppose Beneficiary's contract called for payment by a  
47 Fedwire transfer to Bank B, but the payment order accepted by  
48 Bank B was not a Fedwire transfer. Before the funds were  
49 withdrawn by Beneficiary, Bank B suspended payments. The sender  
50

of the payment order to Bank B paid the amount of the order to Bank B. In this case the payment by Originator did not comply with Beneficiary's contract, but the noncompliance did not result in a loss to Beneficiary as required by subsection (b)(iv) [subsection (2)(d)]. A Fedwire transfer avoids the risk of insolvency of the sender of the payment order to Bank B, but it does not affect the risk that Bank B will suspend payments before withdrawal of the funds by Beneficiary. Thus, the "unless" clause of subsection (b) [subsection (2)] is not applicable and the obligation owed to Beneficiary is discharged.

5. Charges of receiving banks in a funds transfer normally are nominal in relationship to the amount being paid by the originator to the beneficiary. Wire transfers are normally agreed to in advance and the parties may agree concerning how these charges are to be divided between the parties. Subsection (c) [subsection (3)] states a rule that applies in the absence of agreement. In some funds transfers charges of banks that execute payment orders are collected by deducting the charges from the amount of the payment order issued by the bank, i.e. the bank issues a payment order that is slightly less than the amount of the payment order that is being executed. The process is described in Comment 3 to Section 4A-302 [section 4-1302]. The result in such a case is that the payment order accepted by the beneficiary's bank will be slightly less than the amount of the originator's order. Subsection (c) [subsection (3)] recognizes the principle that a beneficiary is entitled to full payment of a debt paid by wire transfer as a condition to discharge. On the other hand, subsection (c) [subsection (3)] prevents a beneficiary from denying the originator the benefit of the payment by asserting that discharge did not occur because deduction of bank charges resulted in less than full payment. The typical case is one in which the payment is made to exercise a valuable right such as an option which is unfavorable to the beneficiary. Subsection (c) [subsection (3)] allows discharge notwithstanding the deduction unless the originator fails to reimburse the beneficiary for the deducted charges after demand by the beneficiary.

#### PART 5

#### MISCELLANEOUS PROVISIONS

##### §A-1501. Variation by agreement and effect of funds transfer system rule

(1) Except as otherwise provided in this Article, the rights and obligations of a party to a funds transfer may be varied by agreement of the affected party.

(2) "Funds transfer system rule" means a rule of an association of banks:

(a) Governing transmission of payment orders by means of a funds transfer system of the association or rights and obligations with respect to those orders; or

(b) To the extent the rule governs rights and obligations between banks that are parties to a funds transfer in which a Federal Reserve Bank, acting as an intermediary bank, sends a payment order to the beneficiary's bank.

Except as otherwise provided in this Article, a funds transfer system rule governing rights and obligations between participating banks using the system may be effective even if the rule conflicts with this Article and indirectly affects another party to the funds transfer who does not consent to the rule. A funds transfer system rule may also govern rights and obligations of parties other than participating banks using the system to the extent stated in sections 4-1404, subsection (3), section 4-1405, subsection (4) and section 4-1507, subsection (3).

#### 1991 Uniform Comment

1. This section is designed to give some flexibility to Article 4A [Article 4-A]. Funds transfer system rules govern rights and obligations between banks that use the system. They may cover a wide variety of matters such as form and content of payment orders, security procedures, cancellation rights and procedures, indemnity rights, compensation rules for delays in completion of a funds transfer, time and method of settlement, credit restrictions with respect to senders of payment orders and risk allocation with respect to suspension of payments by a participating bank. Funds transfer system rules can be very effective in supplementing the provisions of Article 4A [Article 4-A] and in filling gaps that may be present in Article 4A [Article 4-A]. To the extent they do not conflict with Article 4A [Article 4-A] there is no problem with respect to their effectiveness. In that case they merely supplement Article 4A [Article 4-A]. Section 4A-501 [section 4-1501] goes further. It states that unless the contrary is stated, funds transfer system rules can override provisions of Article 4A [Article 4-A]. Thus, rights and obligations of a sender bank and a receiving bank with respect to each other can be different from that stated in Article 4A [Article 4-A] to the extent a funds transfer system rule applies. Since funds transfer system rules are defined as those governing the relationship between participating banks, a rule can have a direct effect only on participating banks. But a

rule that affects the conduct of a participating bank may indirectly affect the rights of nonparticipants such as the originator or beneficiary of a funds transfer, and such a rule can be effective even though it may affect nonparticipants without their consent. For example, a rule might prevent execution of a payment order or might allow cancellation of a payment order with the result that a funds transfer is not completed or is delayed. But a rule purporting to define rights and obligations of nonparticipants in the system would not be effective to alter Article 4A [Article 4-A] rights because the rule is not within the definition of funds transfer system rule. Rights and obligations arising under Article 4A [Article 4-A] may also be varied by agreement of the affected parties, except to the extent Article 4A [Article 4-A] otherwise provides. Rights and obligations arising under Article 4A [Article 4-A] can also be changed by Federal Reserve regulations and operating circulars of Federal Reserve Banks. Section 4A-107 [section 4-1107].

2. Subsection (b)(ii) [subsection (2)(b)] refers to ACH transfers. Whether an ACH transfer is made through an automated clearing house of a Federal Reserve Bank or through an automated clearing house of another association of banks, the rights and obligations of the originator's bank and the beneficiary's bank are governed by uniform rules adopted by various associations of banks in various parts of the nation. With respect to transfers in which a Federal Reserve Bank acts as intermediary bank these rules may be incorporated, in whole or in part, in operating circulars of the Federal Reserve Bank. Even if not so incorporated these rules can still be binding on the association banks. If a transfer is made through a Federal Reserve Bank, the rules are effective under subsection (b)(ii) [subsection (2)(b)]. If the transfer is not made through a Federal Reserve Bank, the association rules are effective under subsection (b)(i) [subsection (2)(a)].

**§4-1502. Creditor process served on receiving bank; setoff by beneficiary's bank**

(1) As used in this section, "creditor process" means levy, attachment, garnishment, notice of lien, sequestration or a similar process issued by or on behalf of a creditor or other claimant with respect to an account.

(2) This subsection applies to the creditor process with respect to an authorized account of the sender of a payment order if the creditor process is served on the receiving bank. For the purpose of determining rights with respect to the creditor process, if the receiving bank accepts the payment order, the balance in the authorized account is deemed to be reduced by the

amount of the payment order to the extent the bank did not otherwise receive payment of the order, unless the creditor process is served at a time and in a manner affording the bank a reasonable opportunity to act on it before the bank accepts the payment order.

(3) If a beneficiary's bank has received a payment order for payment to the beneficiary's account in the bank, the following rules apply.

(a) The bank may credit the beneficiary's account. The amount credited may be set off against an obligation owed by the beneficiary to the bank or applied to satisfy creditor process served on the bank with respect to the account.

(b) The bank may credit the beneficiary's account and allow withdrawal of the amount credited unless creditor process with respect to the account is served at a time and in a manner affording the bank a reasonable opportunity to act to prevent withdrawal.

(c) If creditor process with respect to the beneficiary's account has been served and the bank has had a reasonable opportunity to act on it, the bank may not reject the payment order except for a reason unrelated to the service of process.

(4) Creditor process with respect to a payment by the originator to the beneficiary pursuant to a funds transfer may be served only on the beneficiary's bank with respect to the debt owed by that bank to the beneficiary. Any other bank served with the creditor process is not obliged to act with respect to the process.

**1991 Uniform Comment**

1. When a receiving bank accepts a payment order, the bank normally receives payment from the sender by debiting an authorized account of the sender. In accepting the sender's order the bank may be relying on a credit balance in the account. If creditor process is served on the bank with respect to the account before the bank accepts the order but the bank employee responsible for the acceptance was not aware of the creditor process at the time the acceptance occurred, it is unjust to the bank to allow the creditor process to take the credit balance on which the bank may have relied. Subsection (b) [subsection (2)] allows the bank to obtain payment from the sender's account in this case. Under that provision, the balance in the sender's account to which the creditor process applies is



2 deemed to be reduced by the amount of the payment order unless  
3 there was sufficient time for notice of the service of creditor  
4 process to be received by personnel of the bank responsible for  
the acceptance.

6 2. Subsection (c) [subsection (3)] deals with payment  
7 orders issued to the beneficiary's bank. The bank may credit the  
8 beneficiary's account when the order is received, but under  
9 Section 4A-404(a) [section 4-1404(1)] the bank incurs no  
10 obligation to pay the beneficiary until the order is accepted  
11 pursuant to Section 4A-209(b) [section 4-1209(2)]. Thus, before  
12 acceptance, the credit to the beneficiary's account is  
13 provisional. But under Section 4A-209(b) [section 4-1209(2)]  
14 acceptance occurs if the beneficiary's bank pays the beneficiary  
15 pursuant to Section 4A-405(a) [section 4-1405(1)]. Under that  
16 provision, payment occurs if the credit to the beneficiary's  
17 account is applied to a debt of the beneficiary. Subsection  
18 (c)(1) [subsection (3)(a)] allows the bank to credit the  
19 beneficiary's account with respect to a payment order and to  
20 accept the order by setting off the credit against an obligation  
21 owed to the bank or applying the credit to creditor process with  
22 respect to the account.

24 Suppose a beneficiary's bank receives a payment order for  
25 the benefit of a customer. Before the bank accepts the order,  
26 the bank learns that creditor process has been served on the bank  
27 with respect to the customer's account. Normally there is no  
28 reason for a beneficiary's bank to reject a payment order, but if  
29 the beneficiary's account is garnished, the bank may be faced  
30 with a difficult choice. If it rejects the order, the garnishing  
31 creditor's potential recovery of funds of the beneficiary is  
32 frustrated. It may be faced with a claim by the creditor that  
33 the rejection was a wrong to the creditor. If the bank accepts  
34 the order, the effect is to allow the creditor to seize funds of  
35 its customer, the beneficiary. Subsection (c)(3) [subsection  
36 (3)(c)] gives the bank no choice in this case. It provides that  
37 it may not favor its customer over the creditor by rejecting the  
38 order. The beneficiary's bank may rightfully reject only if  
39 there is an independent basis for rejection.

40 3. Subsection (c)(2) [subsection (3)(b)] is similar to  
41 subsection (b) [subsection (2)]. Normally the beneficiary's bank  
42 will release funds to the beneficiary shortly after acceptance or  
43 it will accept by releasing funds. Since the bank is bound by a  
44 garnishment order served before funds are released to the  
45 beneficiary, the bank might suffer a loss if funds were released  
46 without knowledge that a garnishment order had been served.  
47 Subsection (c)(2) [subsection (3)(b)] protects the bank if it did  
48

2 not have adequate notice of the garnishment when the funds were  
3 released.

4 4. A creditor may want to reach funds involved in a funds  
5 transfer. The creditor may try to do so by serving process on  
6 the originator's bank, an intermediary bank or the beneficiary's  
7 bank. The purpose of subsection (d) [subsection (4)] is to guide  
8 the creditor and the court as to the proper method of reaching  
9 the funds involved in a funds transfer. A creditor of the  
10 originator can levy on the account of the originator in the  
11 originator's bank before the funds transfer is initiated, but  
12 that levy is subject to the limitations stated in subsection (b)  
13 [subsection (2)]. The creditor of the originator cannot reach  
14 any other funds because no property of the originator is being  
15 transferred. A creditor of the beneficiary cannot levy on  
16 property of the originator and until the funds transfer is  
17 completed by acceptance by the beneficiary's bank of a payment  
18 order for the benefit of the beneficiary, the beneficiary has no  
19 property interest in the funds transfer which the beneficiary's  
20 creditor can reach. A creditor of the beneficiary that wants to  
21 reach the funds to be received by the beneficiary must serve  
22 creditor process on the beneficiary's bank to reach the  
23 obligation of the beneficiary's bank to pay the beneficiary which  
24 arises upon acceptance by the beneficiary's bank under Section  
25 4A-404(a) [section 4-1404(1)].

26 5. "Creditor process" is defined in subsection (a)  
27 [subsection (1)] to cover a variety of devices by which a  
28 creditor of the holder of a bank account or a claimant to a bank  
29 account can seize the account. Procedure and nomenclature varies  
30 widely from state to state. The term used in Section 4A-502  
31 [section 4-1502] is a generic term.

32 §4-1503. Injunction or restraining order with respect to  
33 funds transfer

34 For proper cause and in compliance with applicable law, a  
35 court may restrain:

36 (1) A person from issuing a payment order to initiate a  
37 funds transfer;

38 (2) An originator's bank from executing the payment order  
39 of the originator; or

40 (3) The beneficiary's bank from releasing funds to the  
41 beneficiary or the beneficiary from withdrawing those funds.  
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A court may not otherwise restrain a person from issuing a payment order, paying or receiving payment of a payment order or otherwise acting with respect to a funds transfer.

1991 Uniform Comment

This section is related to Section 4A-502(d) [section 4-1502(4)] and to Comment 4 to Section 4A-502 [section 4-1502]. It is designed to prevent interruption of a funds transfer after it has been set in motion. The initiation of a funds transfer can be prevented by enjoining the originator or the originator's bank from issuing a payment order. After the funds transfer is completed by acceptance of a payment order by the beneficiary's bank, that bank can be enjoined from releasing funds to the beneficiary or the beneficiary can be enjoined from withdrawing the funds. No other injunction is permitted. In particular, intermediary banks are protected, and injunctions against the originator and the originator's bank are limited to issuance of a payment order. Except for the beneficiary's bank, nobody can be enjoined from paying a payment order, and no receiving bank can be enjoined from receiving payment from the sender of the order that it accepted.

§4-1504. Order in which items and payment orders may be charged to account; order of withdrawals from account

(1) If a receiving bank has received more than one payment order of the sender or one or more payment orders and other items that are payable from the sender's account, the bank may charge the sender's account with respect to the various orders and items in any sequence.

(2) In determining whether a credit to an account has been withdrawn by the holder of the account or applied to a debt of the holder of the account, credits first made to the account are first withdrawn or applied.

1991 Uniform Comment

Subsection (a) [subsection (1)] concerns priority among various obligations that are to be paid from the same account. A customer may have written checks on its account with the receiving bank and may have issued one or more payment orders payable from the same account. If the account balance is not sufficient to cover all of the checks and payment orders, some checks may be dishonored and some payment orders may not be accepted. Although there is no concept of wrongful dishonor of a payment order in Article 4A [Article 4-A] in the absence of an agreement to honor by the receiving bank, some rights and

obligations may depend on the amount in the customer's account. Section 4A-209(b)(3) [section 4-1209(2)(c)] and Section 4A-210(b) [section 4-1210(2)]. Whether dishonor of a check is wrongful also may depend upon the balance in the customer's account. Under subsection (a) [subsection (1)], the bank is not required to consider the competing items and payment orders in any particular order. Rather it may charge the customer's account for the various items and orders in any order. Suppose there is \$12,000 in the customer's account. If a check for \$5,000 is presented for payment and the bank receives a \$10,000 payment order from the customer, the bank could dishonor the check and accept the payment order. Dishonor of the check is not wrongful because the account balance was less than the amount of the check after the bank charged the account \$10,000 on account of the payment order. Or, the bank could pay the check and not execute the payment order because the amount of the order is not covered by the balance in the account.

§4-1505. Preclusion of objection to debit of customer's account

If a receiving bank has received payment from its customer with respect to a payment order issued in the name of the customer as sender and accepted by the bank and the customer received notification reasonably identifying the order, the customer is precluded from asserting that the bank is not entitled to retain the payment unless the customer notifies the bank of the customer's objection to the payment within one year after the notification was received by the customer.

1991 Uniform Comment

This section is in the nature of a statute of repose for objecting to debits made to the customer's account. A receiving bank that executes payment orders of a customer may have received payment from the customer by debiting the customer's account with respect to a payment order that the customer was not required to pay. For example, the payment order may not have been authorized or verified pursuant to Section 4A-202 [section 4-1202] or the funds transfer may not have been completed. In either case the receiving bank is obliged to refund the payment to the customer and this obligation to refund payment cannot be varied by agreement. Section 4A-204 [section 4-1204] and Section 4A-402 [section 4-1402]. Refund may also be required if the receiving bank is not entitled to payment from the customer because the bank erroneously executed a payment order. Section 4A-303 [section 4-1303]. A similar analysis applies to that case. Section 4A-402(d) and (f) [section 4-1402(4) and (6)] require refund and the obligation to refund may not be varied by

agreement. Under 4A-505 [section 4-1505], however, the obligation to refund may not be asserted by the customer if the customer has not objected to the debiting of the account within one year after the customer received notification of the debit.

#### §4-1506. Rate of interest

(1) If, under this Article, a receiving bank is obliged to pay interest with respect to a payment order issued to the bank, the amount payable may be determined:

(a) By agreement of the sender and receiving bank; or

(b) By a funds transfer system rule if the payment order is transmitted through a funds transfer system.

(2) If the amount of interest is not determined by an agreement or rule as stated in subsection (1), the amount is calculated by multiplying the applicable federal funds rate by the amount on which interest is payable and then multiplying the product by the number of days for which interest is payable. The applicable federal funds rate is the average of the federal funds rates published by the Federal Reserve Bank of New York for each of the days for which interest is payable, divided by 360. The federal funds rate for any day on which a published rate is not available is the same as the published rate for the next preceding day for which there is a published rate. If a receiving bank that accepted a payment order is required to refund payment to the sender of the order because the funds transfer was not completed, but the failure to complete was not due to any fault by the bank, the interest payable is reduced by a percentage equal to the reserve requirement on deposits of the receiving bank.

#### 1991 Uniform Comment

1. A receiving bank is required to pay interest on the amount of a payment order received by the bank in a number of situations. Sometimes the interest is payable to the sender and in other cases it is payable to either the originator or the beneficiary of the funds transfer. The relevant provisions are Section 4A-204(a) [section 4-1204(1)]; Section 4A-209(b)(3) [section 4-1209(2)(c)]; Section 4A-210(b) [section 4-1210(2)]; Section 4A-305(a) [section 4-1305(1)]; Section 4A-402(d) [section 4-1402(4)] and Section 4A-404(b) [section 4-1404(2)]. The rate of interest may be governed by a funds transfer system rule or by agreement as stated in subsection (a) [subsection (1)]. If subsection (a) [subsection (1)] doesn't apply, the rate is determined under subsection (b) [subsection (2)]. Subsection (b)

[subsection (2)] is frustrated by the following example. A bank is obliged to pay interest on \$1,000,000 for three days, July 3, July 4, and July 5. The published Fed Funds rate is .082 for July 3 and .081 for July 5. There is no published rate for July 4 because that day is not a banking day. The rate for July 3 applies to July 4. The applicable Fed Funds rate is .08167 (the average of .082, .082, and .081) divided by 360 which equals .0002268. The amount of interest payable is \$1,000,000 x .0002268 x 3 = \$680.40.

2. In some cases, interest is payable in spite of the fact that there is no fault by the receiving bank. The last sentence of subsection (b) [subsection (2)] applies to those cases. For example, a funds transfer might not be completed because the beneficiary's bank rejected the payment order issued to it by the originator's bank or an intermediary bank. Section 4A-402(c) [section 4-1402(3)] provides that the originator is not obliged to pay its payment order and Section 4A-402(d) [section 4-1402(4)] provides that the originator's bank must refund any payment received plus interest. The requirement to pay interest in this case is not based on fault by the originator's bank. Rather, it is based on restitution. Since the originator's bank had the use of the originator's money, it is required to pay the originator for the value of that use. The value of that use is not determined by multiplying the interest rate by the refundable amount because the originator's bank is required to deposit with the Federal Reserve a percentage of the bank's deposits as a reserve requirement. Since that deposit does not bear interest, the bank had use of the refundable amount reduced by a percentage equal to the reserve requirement. If the reserve requirement is 12%, the amount of interest payable by the bank under the formula stated in subsection (b) [subsection (2)] is reduced by 12%.

#### §4-1507. Choice of law

(1) The following rules apply unless the affected parties otherwise agree or subsection (3) applies.

(a) The rights and obligations between the sender of a payment order and the receiving bank are governed by the law of the jurisdiction in which the receiving bank is located.

(b) The rights and obligations between the beneficiary's bank and the beneficiary are governed by the law of the jurisdiction in which the beneficiary's bank is located.

(c) The issue of when payment is made pursuant to a funds transfer by the originator to the beneficiary is governed by

the law of the jurisdiction in which the beneficiary's bank is located.

(2) If the parties described in subsection (1), paragraphs (a), (b) and (c) have made an agreement and selected the law of a particular jurisdiction to govern rights and obligations between them, the law of that jurisdiction governs those rights and obligations whether or not the payment order or the funds transfer bears a reasonable relation to that jurisdiction.

(3) A funds transfer system rule may select the law of a particular jurisdiction to govern the rights and obligations:

(a) Between participating banks with respect to payment orders transmitted or processed through the system; or

(b) Of some or all parties to a funds transfer, any part of which is carried out by means of the system.

A choice of law made pursuant to paragraph (a) is binding on participating banks. A choice of law made pursuant to paragraph (b) is binding on the originator, other sender or a receiving bank having notice that the funds transfer system may be used in the funds transfer and notice of the choice of law by the system, when the originator, other sender or receiving bank issued or accepted a payment order. The beneficiary of a funds transfer is bound by the choice of law if, when the funds transfer is initiated, the beneficiary has notice that the funds transfer system may be used in the funds transfer and notice of the choice of law by the system. The law of a jurisdiction selected pursuant to this subsection may govern, whether or not that law bears a reasonable relation to the matter in issue.

(4) In the event of inconsistency between an agreement under subsection (2) and a choice-of-law rule under subsection (3), the agreement under subsection (2) prevails.

(5) If a funds transfer is made by use of more than one funds transfer system and there is inconsistency between the choice-of-law rules of the systems, the matter in issue is governed by the law of the selected jurisdiction that has the most significant relationship to the matter in issue.

#### 1991 Uniform Comment

1. Funds transfers are typically interstate or international in character. If part of a funds transfer is governed by Article 4A [Article 4-A] and another part is governed by other law, the rights and obligations of parties to the funds

transfer may be unclear because there is no clear consensus in various jurisdictions concerning the juridical nature of the transaction. Unless all of a funds transfer is governed by a single law it may be very difficult to predict the result if something goes wrong in the transfer. Section 4A-507 [section 4-1507] deals with this problem. Subsection (b) [subsection (2)] allows parties to a funds transfer to make a choice-of-law agreement. Subsection (c) [subsection (3)] allows a funds transfer system to select the law of a particular jurisdiction to govern funds transfers carried out by means of the system. Subsection (a) [subsection (1)] states residual rules if no choice of law has occurred under subsection (b) [subsection (2)] or subsection (c) [subsection (3)].

2. Subsection (a) [subsection (1)] deals with three sets of relationships. Rights and obligations between the sender of a payment order and the receiving bank are governed by the law of the jurisdiction in which the receiving bank is located. If the receiving bank is the beneficiary's bank the rights and obligations of the beneficiary are also governed by the law of the jurisdiction in which the receiving bank is located. Suppose Originator, located in Canada, sends a payment order to Originator's Bank located in a state in which Article 4A [Article 4-A] has been enacted. The order is for payment to an account of Beneficiary in a bank in England. Under subsection (a)(1) [subsection (1)(a)], the rights and obligations of Originator and Originator's Bank toward each other are governed by Article 4A [Article 4-A] if an action is brought in a court in the Article 4A [Article 4-A] state. If an action is brought in a Canadian court, the conflict of laws issue will be determined by Canadian law which might or might not apply the law of the state in which Originator's Bank is located. If that law is applied, the execution of Originator's order will be governed by Article 4A [Article 4-A], but with respect to the payment order of Originator's Bank to the English bank, Article 4A [Article 4-A] may or may not be applied with respect to the rights and obligations between the two banks. The result may depend upon whether action is brought in a court in the state in which Originator's Bank is located or in an English court. Article 4A [Article 4-A] is binding only on a court in a state that enacts it. It can have extraterritorial effect only to the extent courts of another jurisdiction are willing to apply it. Subsection (c) [subsection (3)] also bears on the issues discussed in this Comment.

Under Section 4A-406 [section 4-1406] payment by the originator to the beneficiary of the funds transfer occurs when the beneficiary's bank accepts a payment order for the benefit of the beneficiary. A jurisdiction in which Article 4A [Article

2 4-A] is not in effect may follow a different rule or it may not  
3 have a clear rule. Under Section 4A-507(a)(3) [section  
4 4-1507(1)(c)] the issue is governed by the law of the  
5 jurisdiction in which the beneficiary's bank is located. Since  
6 the payment to the beneficiary is made through the beneficiary's  
7 bank it is reasonable that the issue of when payment occurs be  
8 governed by the law of the jurisdiction in which the bank is  
9 located. Since it is difficult in many cases to determine where  
10 a beneficiary is located, the location of the beneficiary's bank  
11 provides a more certain rule.

12 3. Subsection (b) [subsection (2)] deals with choice-of-law  
13 agreements and it gives maximum freedom of choice. Since the law  
14 of funds transfers is not highly developed in the case law there  
15 may be a strong incentive to choose the law of a jurisdiction in  
16 which Article 4A [Article 4-A] is in effect because it provides a  
17 greater degree of certainty with respect to the rights of various  
18 parties. With respect to commercial transactions, it is often  
19 said that "[u]niformity and predictability based upon commercial  
20 convenience are the prime considerations in making the choice of  
21 governing law . . . ." R. Leflar, American Conflicts Law, § 185  
22 (1977). Subsection (b) [subsection (2)] is derived in part from  
23 recently enacted choice-of-law rules in the States of New York  
24 and California. N.Y. Gen. Obligations Law 5-1401 (McKinney's  
25 1989 Supp.) and California Civil Code § 1646.5. This broad  
26 endorsement of freedom of contract is an enhancement of the  
27 approach taken by Restatement (Second) of Conflict of Laws  
28 § 187(b) (1971). The Restatement recognizes the basic right of  
29 freedom of contract, but the freedom granted the parties may be  
30 more limited than the freedom granted here. Under the  
31 formulation of the Restatement, if there is no substantial  
32 relationship to the jurisdiction whose law is selected and there  
33 is no "other" reasonable basis for the parties' choice, then the  
34 selection of the parties need not be honored by a court.  
35 Further, if the choice is violative of a fundamental policy of a  
36 state which has a materially greater interest than the chosen  
37 state, the selection could be disregarded by a court. Those  
38 limitations are not found in subsection (b) [subsection (2)].

39 4. Subsection (c) [subsection (3)] may be the most  
40 important provision in regard to creating uniformity of law in  
41 funds transfers. Most rights stated in Article 4A [Article 4-A]  
42 regard parties who are in privity of contract such as originator  
43 and beneficiary, sender and receiving bank, and beneficiary's  
44 bank and beneficiary. Since they are in privity they can make a  
45 choice of law by agreement. But that is not always the case.  
46 For example, an intermediary bank that improperly executes a  
47 payment order is not in privity with either the originator or the  
48 beneficiary. The ability of a funds transfer system to make a

2 choice of law by rule is a convenient way of dispensing with  
3 individual agreements and to cover cases in which agreements are  
4 not feasible. It is probable that funds transfer systems will  
5 adopt a governing law to increase the certainty of commercial  
6 transactions that are effected over such systems. A system rule  
7 might adopt the law of an Article 4A [Article 4-A] state to  
8 govern transfers on the system in order to provide a consistent,  
9 unitary, law governing all transfers made on the system. To the  
10 extent such system rules develop, individual choice-of-law  
11 agreements become unnecessary.

12 Subsection (c) [subsection (3)] has broad application. A  
13 system choice of law applies not only to rights and obligations  
14 between banks that use the system, but may also apply to other  
15 parties to the funds transfer so long as some part of the  
16 transfer was carried out over the system. The originator and any  
17 other sender or receiving bank in the funds transfer is bound if  
18 at the time it issues or accepts a payment order it had notice  
19 that the funds transfer involved use of the system and that the  
20 system chose the law of a particular jurisdiction. Under Section  
21 4A-107 [section 4-1107], the Federal Reserve by regulation could  
22 make a similar choice of law to govern funds transfers carried  
23 out by use of Federal Reserve Banks. Subsection (d) [subsection  
24 (4)] is a limitation on subsection (c) [subsection (3)]. If  
25 parties have made a choice-of-law agreement that conflicts with a  
26 choice of law made under subsection (c) [subsection (3)], the  
27 agreement prevails.

28 5. Subsection (e) [subsection (5)] addresses the case in  
29 which a funds transfer involves more than one funds transfer  
30 system and the systems adopt conflicting choice-of-law rules.  
31 The rule that has the most significant relationship to the matter  
32 at issue prevails. For example, each system should be able to  
33 make a choice of law governing payment orders transmitted over  
34 that system with regard to a choice of law made by another system.

35 **Sec. 3. Legislative Intent.** This Act is the Maine enactment of  
36 the Uniform Commercial Code, Article 4A as adopted by the  
37 National Conference of Commissioners on Uniform State Laws. The  
38 text of that uniform act has been changed to conform to Maine  
39 statutory conventions. Unless otherwise noted in a Maine  
40 comment, the changes are technical in nature and it is the intent  
41 of the Legislature that this Act be interpreted as substantively  
42 the same as the uniform act.

#### STATEMENT OF FACT

43 This bill enacts the Maine Revised Statutes, Title 11,  
44 Article 4-A, which is the State's version of the Uniform  
45 Commercial Code, Article 4A, governing the transfer of funds

2 between banks by wire or by written instructions. The article is  
3 based on an article adopted by the National Conference of  
4 Commissioners on Uniform State Laws and has been technically  
5 revised to conform to the Legislature's conventions for usage and  
6 numbering. Uniform law comments are included without any change  
7 except that cross-references to the uniform law are followed by  
8 cross-references to the Maine version in brackets.