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Banks and Banking - Validity of Exculpatory Clauses in Stop-Payment Orders

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BANKS AND BANKING—VALIDITY OF EXCULPATORY CLAUSES IN STOP-PAYMENT ORDERS—Plaintiff, a depositor in defendant commercial bank, in seeking to stop payment of his check, executed and left with the bank a printed form supplied by the bank, entitled "Request to Stop Payment of Check." Among the terms of the paper was a provision which constituted a release of the bank from all liability should it pay the check through "inadvertence, accident or oversight." The bank subsequently honored the check and charged its amount against the plaintiff's account. Plaintiff demanded that the defendant refund this amount, but the defendant refused to do so. Plaintiff thereupon brought an action against the bank to recover the amount of the check. The trial court's judgment for the plaintiff was reversed by the intermediate appellate court. On appeal to the Pennsylvania Supreme Court, *held,* the trial court's judgment reinstated. An exculpatory clause in a stop-payment order like the one in the present case is void as against public policy. *Thomas v. First National Bank of Scranton,* 376 Pa. 181, 101 A. (2d) 910 (1954).

At common law, when a depositor has given his bank notice not to honor a check drawn upon it and the bank thereafter inadvertently pays the holder, the bank may not charge the depositor's account for that amount.[1] In many jurisdictions the bank may not even have recourse against the person to whose benefit the mistaken payment has enured.[2] As a consequence banks have tried various methods to limit this absolute liability. One of the most widely used plans is to require all stop-payment orders to be in writing on a form prepared by the bank. This form includes a clause releasing the bank from liability if the

[1] American Defense Society, Inc. v. Sherman Nat. Bank, 225 N.Y. 506, 122 N.E. 695 (1919); 1 MORSE, BANKS AND BANKING, 6th ed., §397 (1928).

[2] 39 A.L.R. 1239 (1925). The Uniform Commercial Code allows the banks an action against the wrongdoing party where it has suffered a loss. A.L.I. UNIFORM COMMERCIAL CODE §4-407 (1952).

check is thereafter negligently paid.[3] There has been a wide dispute among the courts on the question of whether the policy reasons for refusing to allow banks to escape from liability are overbalanced by the desirability of letting the parties voluntarily adapt their needs to the particular situation.[4] The rule is well settled with respect to common carriers that they cannot by contract limit their liability for the consequences of their own negligence,[5] and recent cases indicate a trend toward extending this rule to other businesses "affected with a public interest."[6] It seems clear that banking is such a business.[7] As one court has said, "The bank has been entrusted with an important franchise to serve the public and has received broad legislative protection. Might it not be appropriate to apply to banks the legal doctrine which has deprived quasi-public enterprises of the power to require such release clauses?"[8] It has been implied that the public interest of a bank is not as strong as, e.g., that of a public utility, because the depositor has the privilege of doing his business elsewhere,[9] which is something the utility customer cannot do. This position becomes much less forceful when applied to communities having only one or two banks, or even to larger areas where all the banks use similar exculpatory clauses. The monop-

[3] The form prepared and recommended by the American Banker's Association reads as follows: ". . . the undersigned agrees . . . not to hold you liable on account of payment contrary to this request if same occur through inadvertence, accident, or oversight. . . ." 3 PATON'S DIGEST 3474 (1944). The phrase "inadvertence, accident or oversight" is merely a euphemistic way of saying "negligence" since the word inadvertence embraces the effect of inattention, carelessness, and heedlessness. Cohen v. Noel, 21 Tenn. App. 51 at 58, 104 S.W. (2d) 1001 (1937); Tremont Trust Co. v. Burack, 235 Mass. 398, 126 N.E. 782 (1920).

[4] Cases holding exculpatory clauses are not opposed to public policy: Tremont Trust Co. v. Burack, note 3 supra; Gaita v. Windsor Bank, 251 N.Y. 152, 167 N.E. 203 (1929); Hodnick v. Fidelity Trust Co., 96 Ind. App. 342, 183 N.E. 488 (1932). *Contra:* Hiroshima v. Bank of Italy, 78 Cal. App. 362, 248 P. 947 (1926) (based upon California statutory provisions); Speroff v. First-Cent. Trust Co., 149 Ohio St. 415, 79 N.E. (2d) 119 (1948); Reinhardt v. Passaic Clifton Nat. Bank & Trust Co., 16 N.J. Super. 430, 84 A. (2d) 741 (1951). Many of these same courts have invalidated such clauses on the additional ground of lack of consideration. This question has been fully dealt with in numerous law review notes and articles, e.g., 34 MINN. L. REV. 330 (1950); 27 N.Y. UNIV. L. REV. 345 (1952); 28 NEB. L. REV. 437 (1949); 23 CONN. B.J. 346 (1949). In Pennsylvania lack of consideration is not a ground for avoiding a release such as that in the principal case.

[5] 6 WILLISTON, CONTRACTS, rev. ed., 4971-4973 (1938).

[6] Public utilities: Collins v. Va. Power & Electric Co., 204 N.C. 320, 168 S.E. 500 (1933); telegraph companies: Western Union Telegraph Co. v. Priester, 18 Ala. App. 531, 93 S. 231 (1922); telephone companies: Emery v. Rochester Telephone Co., 156 Misc. 562, 282 N.Y.S. 280 (1935); bailees in the course of a general dealing with the public: Dieterle v. Bekin, 143 Cal. 683, 77 P. 664 (1904).

[7] Runcie v. Bankers Trust Co., 11 N.Y.S. (2d) 924 at 927 (1939). "The cases where a business has been regarded as affected with a public interest have been cases . . . where, from the nature of the business, . . . the person carrying it on was necessarily entrusted with the property or money of his customers, or where the business has been conducted in such a manner that the public . . . have adapted their business to the methods used. . . ." People v. Steele, 231 Ill. 340 at 347, 83 N.E. 236 (1907).

[8] Reinhardt v. Passaic-Clifton Nat. Bank & Trust Co., note 4 supra, at 436.

[9] See Gaita v. Windsor Bank, note 4 supra, at 155.

olistic tendency of commercial banking[10] often makes it necessary for the depositor either to accept the bank's terms or to be deprived of banking facilities altogether. This factor is the basis for the second major reason why courts have held such release clauses to be opposed to public policy, i.e., the inequality of bargaining power between the parties. While some courts jealously guard "freedom of contract,"[11] no such freedom actually exists between a bank and its depositor. Ordinary contract principles are inapplicable where genuine bargaining is unlikely. The wording of the release clauses is carefully arranged by the bank's attorneys to achieve a desired legal effect. The banks require the depositor to sign the stop-payment form as a prerequisite to revoking the check and the typical depositor, even if he reads the printed form, generally fails to understand the legal terms involved.[12] While the courts should not impede desirable banking practices, neither should the banks be permitted to escape their common law liability by taking advantage of uninformed and reliant depositors. The present disagreement among the courts may be resolved to a large degree by the provisions of the Uniform Commercial Code. It attempts to obtain a uniform result in this situation by declaring that ". . . no agreement [of the bank] can disclaim a bank's responsibility . . . for its own lack of good faith or failure to exercise ordinary care."[13] To the extent that some agreements will still be valid under the code, a problem will arise in defining what constitutes "ordinary care" on the part of a bank. Nevertheless, the provision does put to an end the controversy over whether the type of exculpatory clause used in the principal case is opposed to public policy.

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[10] Chandler, "Monopolistic Elements in Commercial Banking," 46 J. POL. ECON. 1 (1938).

[11] Gaita v. Windsor Bank, note 4 supra, at 155.

[12] "Since the depositor surrenders a valuable right in these cases for no benefit in return, it would seem that the success of the bank in obtaining the depositor's signature on the stop-payment form depends upon the latter's ignorance of his right to insist on absolute performance of the order to stop payment of the check." 34 MINN. L. REV. 330 at 331 (1950).

[13] A.L.I. UNIFORM COMMERCIAL CODE §4-103(1) (1952). The code was inapplicable in the principal case because it was not effective in Pennsylvania until July 1, 1954. See Pa. Stat. Ann. (Purdon, 1954) tit. 12A, §4-103(1).