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Florida Supreme Courts Limits Defenses Available to Banks in Refusing to Honor Their Cashier's Checks

Laura L. Giorgolo

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Electronic Fund Transfer Act

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after the bank made its decision to restrict the Feinmans' ATM privileges.

Bank Violated Act by Failing to Remove Restriction Promptly, But Customers Failed to Prove Actual Damages

The court next considered the Feinmans' claim that the bank violated their rights under the Act by failing to remove the restriction on February 29 when Jeff Feinman first requested that the restriction be removed. The Act stated that a bank would be liable if it failed "to make an electronic fund transfer . . . in the correct amount or in a timely manner when properly instructed to do so by the consumer." 15 U.S.C § 1693h(a)(1). The bank routinely lifted "deny access" restrictions after the account holder contacted the bank, corrected the imbalance, and convinced the bank that no future ATM overdrafts would occur. Jeff Feinman contacted the bank and made these assurances on February 29. However, due to a bank error, the restriction remained in effect until Jeff Feinman's second request on March 2.

The court found the bank's failure to remove the restriction on February 29 amounted to a clear, but unintentional, violation of the Act. The court noted that section 1693h(c) of the Act limited recovery for the unintentional violations to actual damages. The court held that because the Feinmans had failed to prove that they suffered any actual damages during the two days between their first request and the day their ATM privileges were restored, they could not recover.

Mark G. Sheridan

FLORIDA SUPREME COURT LIMITS DEFENSES AVAILABLE TO BANKS IN REFUSING TO HONOR THEIR CASHIER'S CHECKS

In *Warren Finance v. Barnett Bank of Jacksonville*, 552 So. 2d 194 (Fla. 1989), the Florida Supreme Court held that a bank may assert only its real and personal defenses in refusing payment upon presentation of a cashier's check that it has issued. The bank may not assert the defenses of a third party to the check. The court stated that, in order to preserve the cash-like attributes of cashier's checks, a bank should not be required to evaluate the validity of the third party's defenses and thereby act as an intermediary between parties disputing ownership rights to cashier's checks.

Background

Pursuant to a finance agreement, Warren Finance, Inc. ("Warren") advanced funds to Redan Engineering ("Redan"), in return, for which Redan assigned to Warren the rights to payments due Redan under construction contracts Redan held with Blossam Contractors, Inc. ("Blossam"). Blossam issued checks to Redan, and Redan tendered the checks to Warren. Warren then asked to receive cashier's checks instead of personal checks, to avoid collection problems. Redan and Warren went to Blossam's depository bank, Barnett Bank of Jacksonville ("Barnett bank"), and exchanged Blossam's checks for cashier's checks that named Redan as the payee. Redan endorsed the checks over to Warren, and Warren deposited them in its account in another bank.

Redan claimed that, in exchange for assigning the Blossam checks to Warren, Warren had promised to forward additional funds to Redan to cover checks Redan had written to suppliers. Warren subsequently refused to advance these additional funds to Redan, and Redan

sought to stop payment on the cashier's checks. Redan contacted Blossam, and Blossam, as purchaser of the cashier's checks, telephoned Barnett bank to stop payment on the checks. Barnett bank refused to honor the cashier's checks when they were tendered by Warren.

Warren brought an action against Barnett bank in the Circuit Court of Duval County, Florida, alleging that Barnett bank had wrongfully dishonored the cashier's checks. Barnett bank defended its refusal to honor the cashier's checks on the grounds that (1) Warren was not a holder in due course, and (2) Warren committed fraud against Redan in the underlying transaction. The trial court ruled in favor of Warren.

The First District Court of Appeal

Reversing the trial court, the First District Court of Appeal stated that if Warren was not a holder in due course, Barnett bank properly refused to pay the checks based upon Barnett bank's assertion of fraud. The court remanded the case for the trial court to determine whether Warren qualified as a holder in due course. The First District certified to the Florida Supreme Court the question of whether the issuing bank may assert the defenses of a payee against the right of a subsequent endorsee to receive payment on a cashier's check.

The Florida Supreme Court Decision

The supreme court initially noted that the purpose of cashier's checks was to act as a cash substitute. Unlike a personal check, which requires that the individual have adequate funds, the bank is personally liable for paying on its cashier's checks. Parties desire cashier's checks to avoid the risk of nonpayment due to insufficient funds in the account, a stop payment order, or insolvency. The court then discussed two theories developed under common law to identify and analyze these circumstances. They are the "cash equivalent theory" and the "note theory."

Most courts have adopted the

"cash equivalent theory" based on the common law rules that a cashier's check is the equivalent of cash. Under this rule, once a bank has issued a cashier's check, the bank may not subsequently refuse to honor the check. These courts recognize and uphold the important role of cashier's checks in promoting certainty in commercial transactions.

Courts justify the cash equivalent theory by relying upon section 4-303 and 3-411 of the Uniform Commercial Code ("U.C.C."). Under section 3-411, a certified check is accepted when certified. Under section 4-303, once a bank has accepted a check, any stop payment order comes too late to relieve the bank's obligation to pay. By analogizing certification of a check to issuance of a cashier's check, the "cash equivalent theory" courts conclude that a bank may not stop payment on its cashier's check based either upon its own defenses or those of another party to the check.

Although the supreme court acknowledged the need to preserve the cash-like attributes of cashier's checks, it refused to characterize a bank's refusal to pay on a cashier's check as a "stopping payment." According to the court, the concept of stop payment only applies to relations between the bank and a customer, as in the instance of personal checks. A personal check is a customer's order to the bank to draw on the customer's own account to effect a payment; until the bank actually carries out that order by paying on the check, the customer may revoke the order by "stopping payment." In contrast, a cashier's check is the bank's obligation on its own account, and the bank is drawer as well as drawee; thus, a bank cannot be liable to itself for failing to stop payment on the check. Similarly, the purchaser of a cashier's check does not have the right to stop a bank's payment on its own check. Thus, the supreme court rejected the "cash equivalent theory."

Some courts apply the "note theory" approach to cashier's checks. Note theory courts begin their analysis with U.C.C. section 3-118, which deems any draft

drawn on the drawer to be effective as a note. Viewing cashier's checks as notes, these courts apply to the cashier's checks the U.C.C. provisions dealing with ordinary negotiable instruments.

Under the U.C.C., a bank in some circumstances may refuse to honor a note without incurring liability. What defenses the bank may assert depend upon the status of the check holder. Specifically, if a payee or endorsee of a cashier's check is a holder in due course, section 3-305 of the U.C.C. limits the bank's defenses to those that are real to the bank. If the payee or endorsee is not a holder in due course, however, section 3-306 of the U.C.C. permits the bank to assert both real and personal defenses.

In the instant case, Barnett bank argued that because section 3-306 permits a bank to assert its real and personal defenses, under 3-306(4) the banks should be able to assert any third party's defenses to the check. Accordingly, Barnett bank claimed it properly refused to honor the check based upon Redan's claim of fraud in the underlying transaction.

The supreme court rejected this argument, stating that it was not a bank's role to determine the rights of parties to a cashier's check, i.e., whether Warren defrauded Redan, before the bank pays on the check. Barnett bank's issuance of the cashier's checks to Redan was an entirely separate transaction, bearing no relation to the underlying dispute between Warren and Redan. In support of this proposition, the supreme court quoted from comment 5 of section 3-306, which, in effect, states that the contract of the obligor bank is simply to pay the holder of the instrument; other persons' claims against the holder are not the obligor's concern. The obligor need not offer a third party's claim as a defense, according to comment 5, because the obligor usually lacks satisfactory evidence to decide the issue. In addition, Barnett bank should not be required to act as an intermediary between Warren and Redan.

The court then refused to adopt the "note theory" approach be-

cause categorizing a cashier's check as a simple note fails to take into account its cash-like attributes. The court reiterated that a cashier's check is intended to be a cash substitute, immune from the difficulties encountered in collecting an ordinary note. In effect, the "note theory" approach permits a bank to refuse payment to an endorsee or payee based upon the holder's status and requires the holder to litigate to obtain payment on the check. This counter-venes the very purpose of cashier's checks, which is to eliminate the risk of litigation to obtain payment.

In rejecting both the "cash equivalent theory" and the "note theory," the supreme court chose to focus on the purpose and use of cashier's checks, rather than their effect. As support for its approach, the court cited U.C.C. section 1-103, which allows for supplementing U.C.C. provisions with principles of law and equity. Additionally, the court cited sections 1-102(1) and (2)(b), which mandate liberal construction and application of the Code to promote its underlying purposes and policies and to provide for expanding commercial practices through custom, usage of trade, and agreement between parties.

The supreme court determined that, in order to reflect the commercial practice of using cashier's checks as cash substitutes, the defenses available to a bank to avoid payment must be narrowly construed. The court, however, declined to completely preclude banks from refusing to honor such checks in all circumstances. The court thus held that although a bank may not assert the defenses of a third party, the bank may assert its own real and personal defenses. Accordingly, when presented with a cashier's check, a bank only may inquire as to whether the payee or endorsee is a legitimate holder. That is, whether the presenter has stolen the check, or simply found a lost check, or whether the check has been materially altered.

The court held that because Warren was a legitimate holder and Barnett bank had no real or

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Wrongful Dishonor of Cashier's Checks

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personal defenses to assert against Warren's claim, Warren was entitled to payment upon depositing the checks into its account. Additionally, Warren did not need to prove that it was a holder in due course because Barnett bank had no real or personal defenses on the check. Thus, the supreme court vacated the appellate court's decision and ordered the appellate court to reinstate the decision of the trial court in favor of Warren.

Laura L. Giorgolo

OHIO TENANTS WHO FAIL TO PURSUE STATUTORY REMEDIES DO NOT WAIVE THEIR RIGHT TO RECOVER DAMAGES

In *Miller v. Ritchie*, 543 N.E.2d 1265 (Ohio 1989), the Supreme Court of Ohio held that by continuing to occupy a defective apartment, a tenant neither waives the landlord's duty to maintain the property, nor waives the tenant's right to recover damages for the landlord's breach of that duty. The court also held that damages should be calculated according to the amount by which the apartment's defects and the reduction in use lessened the leasehold's value.

Background

In 1984, Anthony and Belinda Ritchie ("the Ritchies") entered into an oral, month-to-month tenancy lease with Dexter Miller ("Miller"), agreeing to pay \$200 per month rent for an apartment in Bethel, Ohio. During their two year occupancy, the Ritchies complained to Miller of dangerous electrical wiring, holes in the floor, inadequate plumbing, and no heating system. Miller generally ignored the Ritchies' complaints and only made a few repairs.

In February 1987, Miller brought a forcible entry and de-

tainer action against the Ritchies seeking possession of the apartment and payment of back rent. The Ritchies counterclaimed for damages based on Miller's failure to maintain the property as required by Ohio's Landlords and Tenants Act ("the LTA"), Ohio Rev. Code §§ 5321.01-.15 (1974). Thereafter, the Ritchies voluntarily vacated the apartment. The parties stipulated that the Ritchies owed Miller four months' rent, but did not agree on the amount.

The trial court held that Miller had violated section 5321.04(A) of the LTA (Ohio Rev. Code § 5321.04(A)) by failing to comply with the Ohio building code, failing to make reasonable repairs, and neglecting to keep the apartment in a safe and sanitary condition. The trial court granted judgment for the Ritchies in the amount of \$3,000 plus interest and costs, and awarded Miller \$800 for four months' unpaid rent.

The Ohio Appellate Court reversed, holding that the Ritchies were not entitled to damages because they had occupied the apartment for a lengthy period without pursuing the statutory remedies established section 5321.07 of the LTA (Ohio Rev. Code § 5321.07).

The Ohio Supreme Court Opinion

The Ohio Supreme Court decided three issues upon review: (1) whether the Ritchies waived their right to recover damages by paying rent and declining to pursue statutory remedies under section 5321.07 (Ohio Rev. Code § 5321.07); (2) whether the Ritchies waived their right to recover damages under section 5321.04 (Ohio Rev. Code § 5321.04) by continuing to occupy the apartment after notifying the landlord of its defective condition; and (3) whether the trial court applied the proper measure of damages.

Paying Rent Does Not Waive Right To Recover Damages. In analyzing the first issue, the Ohio Supreme Court looked to the purpose of the LTA. The LTA placed duties upon a landlord that did not exist at common law. Section 5321.07 of the LTA provided to tenants a method to redress

ANNOUNCEMENT

Child Restraints

The Center for Auto Safety published a new report on car child restraints. *Children At Risk: Failure of the Federal Child Restraint Compliance and Recall Program* details the results of the Center's study of the National Traffic Safety Administration's records concerning child restraints. The report found that child restraints are inadequate and that the National Traffic Safety Administration did not adequately enforce and oversee the use of child restraints.

A copy of the report is available by sending \$35.00 to:

Center for Auto Safety
Publication Department
2001 S. St., N.W. Suite 410
Washington, D.C. 20009

breaches of those duties. If a landlord failed to meet his statutory or contractual obligations, the tenant had three options: the tenant could (1) deposit the rent owed with the court; (2) apply for a court order directing the landlord to remedy the condition; or (3) terminate the rental agreement. In order to utilize these remedies, a tenant had to give the landlord written notice of the violations and to have made all rent payments.

The Ohio Supreme Court initially observed that the remedies created by the LTA were not the only recourse for tenants alleging a landlord's breach of duty. Section 5321.07 of the LTA stated that a tenant "may" implement the statutory remedies, provided the tenant has notified the landlord of the code violations and the tenant is current in rent. However, the LTA did not limit the tenant to these remedies because the LTA was intended to supplement other remedial measures.

Although the tenant risks being evicted by failing to pursue one of the LTA remedies, the tenant does not thereby waive his right to recover damages for the landlord's