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A Jurisprudential Perspective for the True Codification of Payment Law

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A JURISPRUDENTIAL PERSPECTIVE FOR THE TRUE CODIFICATION OF PAYMENTS LAW

PETER A. ALCES *

INTRODUCTION

INCREASED technological sophistication[1] and evolving financial institution procedures[2] have created a gap between commercial practices and the codified law of payments. Article 4 of the Uniform Commercial Code (UCC) does not contemplate the likes of check truncation,[3] access

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1. *See* National Comm'n on Elec. Fund Transfers, EFT in the United States 1 (1977) ("EFT systems and services represent an alternative that will operate side-by-side with the traditional cash and check payment systems.") [hereinafter cited as EFT in the U.S.]; N. Penney & D. Baker, The Law of Electronic Fund Transfer Systems iii (1980) (discussing the "technological revolution at work in banking").

2. It has been estimated that by 1985 banks will process sixty billion checks annually. *See* Brennan, *Better Resting Place for Bank Checks?*, ABA [Am. Bankers Ass'n] Banking J. 47, 47 (May 1980); *see also* Leary & High, *The Place of EFT and Check Truncation in Corporate Payment Systems*, 5 Del. J. Corp. L. 1, 6 n.31 (1980) (noting that one bank processed two billion checks in 1977). Procedures intended to streamline the collection process include check truncation, see *infra* note 3, computer sorting and posting, magnetic encoding of checks, and off-premises data processing centers. *See* B. Clark, The Law of Bank Deposits, Collections and Credit Cards ¶ 10.1 (rev. ed. 1981). For an excellent history of the banking industry's response to the technological revolution of the past 30 years, see N. Penney & D. Baker, *supra* note 1, ¶ 1.01. Of course this has not been the first time technological change has affected commercial law. Grant Gilmore commented in 1948 that "[t]echnological changes in the methods of production and distribution of goods have over the last hundred and fifty years rendered the . . . common law of sales quaint and archaic." Gilmore, *On the Difficulties of Codifying Commercial Law*, 57 Yale L.J. 1341, 1343 (1948) [hereinafter cited as Gilmore I].

3. Check truncation occurs when a bank retains paper checks rather than returning them to the customer. N. Penney & D. Baker, *supra* note 1, ¶ 1.01, at 1-13. In this process, electronic or computer data are substituted for paper in the processing system. (Credit card slips are also often truncated.) In the check truncation system most widely used today, the drawee bank keeps the check and sends the customer a detailed periodic statement. Some drawee banks send their customers an "Account Reconciliation Statement," containing a description of each payment—amount, date, check number and a special number for retrieval purposes. A copy of the original check is forwarded to the customer upon request. Other drawee banks supply their depositors with checkbooks that make a carbonless copy of the check as it is written. *See id.* ¶ 2.01, at 2-2 to -4. A more complex truncation system, within the current technology but not yet fully implemented, is depositary bank retention of checks. After receiving the items, the depositary bank microfilms the checks and electronically sends the vital information (amount and account number) to the drawee bank. If the drawee bank agrees to pay, settlement is made and after a period of time the depositary bank destroys the original check. The use of an intermediary bank is eliminated by this procedure. *See* Arthur D. Little, Inc., The Consequences of Electronic Funds Transfer 73 (1975); D. Baker & R. Brandel, The Law of Electronic Fund Transfer Systems ¶ 2.03, at S2-4 (1983 cum. supp. to N. Penney & D. Baker, *supra* note 1); B. Clark, *supra* note 2, ¶ 10.6. For a more detailed discussion of

devices,[4] automated teller machines[5] or wire transfers,[6] and is therefore

check truncation, see N. Penney & D. Baker, *supra* note 1, ¶¶ 2.01-.03; Leary & High, *supra* note 2; White, *Legal Guidelines for Check Truncation*, 2 Computer L.J. 115 (1980); Note, *Alternatives to the Present Check-Collection System*, 20 Stan. L. Rev. 571, 575-81 (1968); Kutler, *Truncation's Bark is Worse than its Bite*, Am. Banker, Aug. 15, 1980, at 1, col. 2.

Because check truncation is a modification of the traditional check system intended to increase efficiency, the question arises as to its impact on specific provisions of the UCC. Section 4-406, for example, imposes a duty on the customer to exercise "reasonable care and promptness to examine the statement and items to discover his unauthorized signature or any alteration of an item." U.C.C. § 4-406(1) (1977). If the bank establishes that the customer breached that duty, the Code may preclude the customer's assertion of forgery or alteration against the bank. Under UCC § 4-406(1), the customer has no duty to act, however, unless the bank (1) sends the statement and items to him; or (2) "holds the statement" pursuant to the customer's request; or (3) "otherwise in a reasonable manner makes the statement and items available to the customer." *Id.* There is disagreement over whether any of the three tests can be satisfied by truncated statements. *Compare* N. Penney & D. Baker, *supra* note 1, ¶ 2.02, at 2-7 to -9 (none of the three tests can be satisfied; therefore, the issue turns on the bank's ability to impose a contractual duty on customers to report forgeries and alterations) *with* B. Clark, *supra* note 2, ¶ 10.4, at 10-7 (the "availability test" would cover the case where the drawee bank keeps the checks and the customer has knowledge of his right to examine them).

The Uniform New Payments Code (UNPC), Unif. New Payments Code (Perm. Editorial Bd. Draft No. 3, 1983) [hereinafter cited as U.N.P.C.], provides a solution. UNPC § 203 requires a customer to "exercise reasonable care and promptness to examine any statement furnished or made available . . . and to discover any orders not authorized by it or materially altered." U.N.P.C., *supra*, § 203. The comments following the section explain how UNPC § 203 departs from UCC § 4-406:

> First, the general obligation of subsection (1) applies whether or not the actual checks are returned to the customer . . . . Second, given the applicability of the Section to all orders, the Section speaks of orders unauthorized by the customer rather than unauthorized signatures or alterations. Third, the proposed draft extends the 14 day period now provided in UCC 4-406(2)(b) to 60 days where written orders or copies are not returned. This follows the 60 day period allowed for EFT transactions under § 909(a) of the [Electronic Funds Transfer Act].

U.N.P.C., *supra*, § 203 comment 1 on existing law. For a thorough discussion of the effect of check truncation on a customer's duty to correct a statement, compare Penney, *Bank Statements, Cancelled Checks, and Article Four in the Electronic Age*, 65 Mich. L. Rev. 1341, 1358 (1967) (recognizing problems occasioned by check truncation) with Clarke, *An Item is an Item is an Item: Article 4 of the UCC and the Electronic Age*, 25 Bus. Law. 109, 109 (1969) (suggesting that UCC Article 4 is responsive and applicable to all banking issues presented by new payments systems).

4. An "access device" is typically a plastic card issued by the financial institution to the customer, along with a personal identification number. *See* Note, *EFTS: Consumer Protection under the UCC*, 10 U. Mich. J.L. Ref. 497, 500-01 (1977). The device provides access to automated teller machines (ATMs)—customer activated terminals enabling the customer to make deposits, obtain cash and initiate payments at all hours. See *infra* note 5. The Federal Electronic Fund Transfer Act (EFTA), 15 U.S.C. §§ 1693-1693r (1982), defines the term "accepted card or other means of access" as "a card, code, or other means of access to a consumer's account . . . for the purpose of transferring money between accounts or obtaining money, property, labor or services." *Id.* § 1693a.

5. An automated teller machine is a customer-bank communication terminal designed to provide many routine banking services for customers. *See* Arthur D. Little, Inc., *supra* note 3, at 239; N. Penney & D. Baker, *supra* note 1, ¶ 6.01. Banks place ATMs both on and off bank premises. Thus, "[t]he ATM supports both the old and the new payment systems. By supplying cash, it aids paper-based systems; by making depos-

unresponsive to many issues of increasing concern.[7] Moreover, the efficacy of Article 4 answers to commercial paper problems is eroding. For example, the *Price v. Neal*[8] rule, which establishes a drawee's liability for

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its, transfers from savings to checking accounts, and payments, ATMs aid in the development of [electronic funds transfer] systems." *Id.* ¶ 6.01, at 6-2. For other discussion of ATMs, see EFT in the U.S., *supra* note 1, at 234; Budnitz, *Problems of Proof When There's a Computer Goof: Consumers Versus ATMs*, 2 Computer L.J. 49 (1980); Winter, *Banking by Blip*, 69 A.B.A. J. 263 (1983); Howard, *Get Ready for The 'Smart Card'*, Dun's Bus. Month, May 1982, at 88.

6. A wire transfer system is an electronic transfer of information and money between financial institutions. It has been estimated that wire transfers account for the movement of $117 trillion each year. Arthur D. Little, Inc., Issues and Needs in the Nation's Payment System 12, table 1 (1982) [hereinafter cited as Little Report]. While the average check is $570 and average bank card transaction $38, the average wire transfer is $2 million. *Id.* There are several methods by which wire transfers can originate. Transfers can be made by written instructions, repetitively or by customer order to transfer funds to another bank. In addition, banks send wires to the Federal Reserve to replenish their reserve accounts or to other banks to settle interbank obligations. Scott, *Corporate Wire Transfers and the Uniform New Payments Code*, 83 Colum. L. Rev. 1664, 1668-69 (1983) [hereinafter cited as Scott I]. The principal wire systems in the United States are BankWire II, CashWire, CHIPS (Clearing House Interbank Payment System), S.W.I.F.T. (Society for Worldwide Interbank Financial Telecommunication), FedWire and telex. *Id.* at 1669. Although all systems provide a communications network, some (S.W.I.F.T., BankWire II and telex) leave settlement arrangements to the parties. Among the systems that do provide for settlement, two (CHIPS and CashWire) defer settlement to the end of a specified period, and in one (FedWire) settlement is instantaneous. Two of the systems (FedWire and telex) are not owned by their users and thus the users lack rule-making authority over the way the system is governed. The systems "fail to provide adequate solutions to the *ultimate* liability of participants, or their customers, for failures to settle obligations, fraud or mistake." *Id.* (emphasis in original). *See generally* EFT in the U.S., *supra* note 1, at 338-39 (discussing FedWire and BankWire); N. Penney & D. Baker, *supra* note 1, ¶¶ 9.01-.14 (discussing FedWire, BankWire II, CHIPS and S.W.I.F.T.); Trotter, *Is Corporate EFT Coming of Age?*, 2 Computer L.J. 87, 93 (1980) (chart describing various wire transfer systems); Comment, *Risk Allocation in International Interbank Electronic Fund Transfers: CHIPS & SWIFT*, 22 Harv. Int'l L.J. 621 (1981) (discussing CHIPS and S.W.I.F.T.).

7. *See* Dunne, *The Checkless Society and Articles 3 and 4*, 24 Bus. Law. 127, 128 (1968); Dunne, *Variation on a Theme by Parkinson or Some Proposals for the Uniform Commercial Code and the Checkless Society*, 75 Yale L.J. 788, 791 (1966); Penney, *Articles 4 and 8 of the Uniform Commercial Code*, 26 La. L. Rev. 259, 259 (1966); Penney, *supra* note 3, at 1367-60.

The conclusion that Article 4 is inapplicable to evolving payment systems is based primarily on the view that a stored electronic payment message does not fit the UCC definition of an "item": "any instrument for the payment of money even though it is not negotiable but does not include money." U.C.C. § 4-104(1)(g) (1977). Once a check is truncated, can the resulting "electronic blip" be categorized as an item? One state has amended the UCC definition to include a "stored electronic message unit." Ga. Code Ann. § 11-4-104(g) (1982). Article 4 has been held inapplicable to wire transfer systems because of the § 4-104(1)(g) definition of an "item." *See* Evra Corp. v. Swiss Bank Corp., 673 F.2d 951, 955 (7th Cir.), *cert. denied*, 459 U.S. 1017 (1982); Delbrueck & Co. v. Manufacturers Hanover Trust Co., 609 F.2d 1047, 1051 (2d Cir. 1979); Jetton, Evra Corp. v. Swiss Bank Corp.: *Consequential Damages for Bank Negligence in Wire Transfers*, 9 Rutgers Computer & Tech. L.J. 369, 398 & n.27 (1983).

8. 3 Burr. 1354, 97 Eng. Rep. 871 (1762); *see* W. Britton, Handbook of the Law of Bills and Notes §§ 133-136 (2d ed. 1961).

paying over a forged drawer's signature[9]—at one time a reasoned conclusion consistent with commercial practices—lacks logical foundation in this age of computerized check processing.[10] In addition, bank counsel are looking for solutions to problems such as the treatment of "through us" items,[11] and find none in the Bank Deposits and Collections provi-

9. The *Price v. Neal* rule is codified in UCC §§ 3-418 ("Finality of Payment or Acceptance") and 4-207 ("Warranties of Customer and Collecting Bank on Transfer or Presentment of Items; Time for Claims"). Section 3-417 ("Warranties on Presentment and Transfer") provides the same warranties outside the bank check context. The rule is predicated on the drawee bank's superior position to detect a forgery because of the drawee's supposed knowledge of the customer/drawer's signature, and also on a desire to end the transaction on an instrument when it is paid rather than reopen and upset a series of commercial transactions at a later date when the forgery is discovered. U.C.C. § 3-418 official comment 1 (1977). For exhaustive treatment of the rule, see Edwards, *Recovery of Final Payments Under the Uniform Commercial Code,* 6 Ohio N.U.L. Rev. 341 (1979); Note, *The Doctrine of* Price v. Neal, 4 Harv. L. Rev. 297 (1891); Note, *Finality of Payment and the Uniform Commercial Code*, 32 Temp. L.Q. 182 (1959); Note, *Allocation of Losses from Check Forgeries Under the Law of Negotiable Instruments and the Uniform Commercial Code*, 62 Yale L.J. 417 (1953).

10. *See* Murray, Price v. Neal *in the Electronic Age: An Empirical Study*, 87 Banking L.J. 686 (1970). The UNPC may sound the death knell for Lord Mansfield's 1762 *Price v. Neal* opinion. Section 204 provides that each customer or transferor of an unauthorized draw order is liable to all transferees who pay on the order in good faith. U.N.P.C., *supra* note 3, § 204(1). The UNPC would abolish *Price v. Neal* because "the rule has no convincing justification and some significant costs in today's high speed check processing environment." *Id.* § 204 comment 2. "[T]he traditional justification that the drawee is in a superior position to detect the forgery seems dubious today" in view of computerized check processing, which makes it uneconomical to verify all signatures. *Id.* The "finality" rationale, which imposes liability on the payor bank to avoid reopening the transaction, is no longer relevant "in cases of forged endorsements where warranties are now given to the payor bank." *Id.* The UNPC drafters viewed *Price v. Neal* "as not giving adequate incentives to payees to check on the bona fides of people drawing checks to them." *Id.* Moreover, the rule "makes no sense in cases of check truncation," see *supra* note 3, because "the drawer's signature is not available for inspection by the payor account institution." U.N.P.C., *supra* note 4, § 204 comment 2; *see* B. Clark, *supra* note 2, ¶ 10.6, at 10-15 (justification that drawee is in superior position to detect forgery is no longer applicable when depositary bank retains check). *But see* The New York Clearing House, Statement on the Proposed Uniform New Payments Code 14 (Sept. 29, 1983) (elimination of *Price v. Neal* may make financial institutions more cautious in dealing with potential customers) (available in files of *Fordham Law Review*) [hereinafter cited as NYCH Statement]. A drawee bank that has paid over a forged drawer's signature may in some circumstances proceed against a prior party on a restitution theory. *Compare* Leary & Schmitt, *Some Bad News and Some Good News from Articles Three and Four*, 43 Ohio St. L.J. 611, 620-24 (1982) (payor bank may have right to recover payment from recipient who was neither holder in due course nor person who changed position in good faith reliance on payment) *and* Phillips, *The Commercial Culpability Scale*, 92 Yale L.J. 228, 238-39 & n.57 (1982) (same) *and* Note, *Commercial Paper and Forgery: Broader Liability for Banks?*, 1980 U. Ill. L.F. 813, 836 (same) *with* J. White & R. Summers, Handbook of the Law Under the Uniform Commercial Code § 16-2, at 613-18 (2d ed. 1980) (construing UCC §§ 4-213 and 4-302 as an "obstacle to the drawee's restitutionary recovery [under §] 3-418"). The crux of the issue is clearly presented, if not clearly addressed, in First Nat'l City Bank v. Altman, 3 U.C.C. Rep. Serv. (Callaghan) 815 (N.Y. Sup. Ct. 1966), *aff'd mem.*, 277 N.Y.S.2d 813 (N.Y. App. Div. 1967).

11. A "through us" item or "payable through draft," unlike a check, is not drawn on the drawer's bank account with a direction to the bank as drawee to pay the item. "Instead, it merely designates the bank as a collection agent to present the draft to the

sions of the UCC.

In response to this dearth of statutory guidance, the Permanent Editorial Board[12] of the UCC in 1977 directed the 3-4-8 Committee[13] to consider modifications and additions to Article 4. The Committee found myriad shortcomings in the current law and began drafting a Uniform New Payments Code (UNPC) to improve and make consistent existing payments law and to provide statutory law where none now exists.[14] In

drawer-drawee for payment, thus giving the drawer a second look before finally approving payment through the bank." B. Clark, *supra* note 2, ¶ 3.7[2], at 3-43. "Payable through" drafts are recognized in UCC § 3-120: "An instrument which states that it is 'payable through' a bank or the like designates that bank as a collecting bank to make presentment but does not of itself authorize the bank to pay the instrument." U.C.C. § 3-120 (1977). This device is usually used by organizations that wish to give to their customers check writing capability without participating in the bank processing system. One example would be Merrill Lynch's Cash Management Account. The "drawer" has the account with the brokerage firm, not the bank that actually processes the checks. *See* Mittelsteadt, *The Stop Payment Right in an Electronic Payment Environment: An Analysis of the Transition Problems Involved when Integrating a Traditional Right into New Value Transfer Systems,* 17 New Eng. L. Rev. 355, 402 & n.274 (1982). "Through us" items pose analytical problems because the drawer is not a customer of the bank and, therefore, the UCC may not apply to some aspects of the transaction. *Id.* at 402.

12. Chaired by Professor Herbert Wechsler, the Permanent Editorial Board of the UCC is a joint committee of the National Conference of Commissioners on Uniform State Laws (NCC) and the American Law Institute (ALI). Both the NCC and ALI were created in response to the need for unification and betterment of law in the United States. The NCC was founded in 1892. The Conference, made up of unpaid commissioners appointed by state governors, primarily prepares acts in the commercial field for possible adoption by state legislatures. W. Twining, Karl Llewellyn and the Realist Movement 272 (1973). In its early years, the NCC restricted itself to areas "where Congress had no jurisdiction." Dunham, *A History of the National Conference of Commissioners on Uniform State Laws,* 30 Law & Contemp. Probs. 233, 237 (1965).

The ALI, responsible for the first "Restatements," had its beginnings in a 1921 project—a "juristic centre for the betterment of the law"—proposed by the Association of American Law Schools. The recommendation of the project was that the ALI should be initiated and "that its first major undertaking should be to prepare a 'restatement of the law.' " W. Twining, *supra*, at 273-74. *See generally* Goodrich, *The Story of the American Law Institute,* 1951 Wash. U.L.Q. 283; Lewis, *History of the American Law Institute and the First Restatement of the Law,* in Restatement in the Courts 1 (perm. ed. 1945).

13. The 3-4-8 Committee was created by the Permanent Editorial Board in 1974 to study Articles 3, 4 and 8 of the UCC. The Committee is a combination of academicians and practicing commercial lawyers, some of whom have represented consumer groups. Federal Reserve Board Staff members have attended Committee meetings. *See* Memorandum from Hal Scott to National Conference of Commissioners on Uniform State Laws (June 15, 1983) (introduction to UNPC, P.E.B. Draft No. 3) (available in files of *Fordham Law Review*) [hereinafter cited as 1983 Memorandum].

14. In 1978, Professor Hal Scott, Reporter to the 3-4-8 Committee, prepared a report discussing the conceptual feasibility of a new payments code. *See* H. Scott, New Payment Systems: A Report to the 3-4-8 Committee of the Permanent Editorial Board for the Uniform Commercial Code (Feb. 8, 1978) (available in files of *Fordham Law Review*) [hereinafter cited as 1978 Report]. The report was evaluated in the spring of 1978 at an invitational conference in Williamsburg, Virginia attended by bankers, lawyers, academicians, consumer advocates and state and federal regulators. Based on this meeting the Permanent Editorial Board authorized the 3-4-8 Committee to draft an outline of a Uniform New Payments Code. For a history of the three drafts of the UNPC, see 1983 Memorandum, *supra* note 13, at 1-3.

June 1983, the 3-4-8 Committee released for public consideration P.E.B. Draft No. 3 of the UNPC.[15] Passage of the UNPC as either federal or state law[16] is not imminent.[17] The seriousness of the Committee's efforts and the perseverance of the interested parties, however, justify consideration of the UNPC's scope and provisions at this time. Even though the UNPC is not likely to be enacted into law in its present form,[18] it may very well have a profound impact on the law of payments devices.[19]

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15. On June 26, 1983, P.E.B. Draft No. 3 was presented to the NCC. Committees of the American Bankers Association, the New York Clearing House Association, and various Federal Reserve Banks have reviewed the draft. In addition, three committees of the American Bar Association (Uniform Commercial Code Committee, Consumer Financial Services Committee, and an Ad Hoc Committee on the Uniform New Payments Code) are currently studying the drafts of the proposed code.

For further discussion of the proposed UNPC, see 1983 Memorandum, *supra* note 13; 1978 Report, *supra* note 14; Benfield, *The New Payments Code and the Abolition of Holder in Due Course Status as to Consumer Checks*, 40 Wash. & Lee L. Rev. 11 (1983); Geary, *One Size Doesn't Fit All—Is a Uniform Payments Code a Good Idea?*, 9 Rutgers Computer & Tech. L.J. 337 (1983); Pape, *Stop Payment in the New Uniform Payments Code*, 9 Rutgers Computer & Tech. L.J. 353 (1983); Scott I, *supra* note 6; Scott, *The Risk Fixers*, 91 Harv. L. Rev. 737 (1978) [hereinafter cited as Scott II]; Vergari, *A Critical Look at the New Uniform Payments Code*, 9 Rutgers Computer & Tech. L.J. 317 (1983).

16. In his 1978 Report, Professor Scott gave three reasons why the Code should be adopted at the federal level rather than in the states by amendments to Articles 3 and 4: the necessity of integrating existing federal law of credit cards; the guarantee of uniformity at the federal level; and the desire to allow some federal regulatory body to flesh out the basic statutory provisions. 1978 Report, *supra* note 14, at 253-54. "Of course, the federalizing of payment law, including check law . . . may offend those who believe commercial laws should be a state concern, but they must recognize the reality of increasing federal intervention in this area." *Id.* at 254. In the 1983 Memorandum, however, Professor Scott recognized that the federal government has "demonstrated an unwillingness to preempt state law [on consumer issues]. . . . It may make sense, therefore, to pursue both federal and state enactment of the Code." 1983 Memorandum, *supra* note 13, at 46-47. He also recognized the possibility of either coordination of state and federal enactment or amendment of federal acts to defer to state legislation. *Id.*

Similar concerns also attended the enactment of the UCC. The predecessor to Article 2 of the UCC was the aborted effort to pass a Federal Sales Bill in Congress, which would have remedied some of the inconsistencies of the Uniform Sales Act. Karl Llewellyn and others supported such federal legislation on the ground that if Congress acted, it would be difficult for the states not to follow. The President of the NCC, William Schnader, however, supported maintenance of a decentralized government and was suspicious of congressional intervention. W. Twining, *supra* note 12, at 277-78; *cf.* Gilmore I, *supra* note 2, at 1358 (predicting increase of governmental intervention in commercial agreements).

17. Before promulgation and approval, the NCC requires two "readings." National Conference of Comm'rs on Uniform State Laws, Constitution § 8.1-.3, *reprinted in* Handbook of the National Conference of Commissioners 254, 260-61 (1979). The ALI must also approve the draft. American Law Inst., Bylaws, Part V, *reprinted in* 58 A.L.I. Proc. 667, 672 (1982); Scott I, *supra* note 6, at 1665 n.10.

18. There are indications that the 3-4-8 Committee has already begun work on a new draft of the UNPC. Letter from Marion W. Benfield, Jr., member, Permanent Editorial Board, to Professor Peter A. Alces (Jan. 27, 1984) (available in files of *Fordham Law Review*).

19. Due to the pervasive nature of the proposed UNPC and the recognized inapplicability of the UCC to the new payments systems, the mere existence of the draft payments code will likely have an impact on the evolving law of payments systems. In addition to

Professor Hal Scott, Reporter for the UNPC, has asserted that there is no real jurisprudence of commercial law.[20] Such a view ignores the work of the UCC drafters, who expended considerable effort formulating a jurisprudence of commercial codification and applying it to the provisions of the UCC. Their perspective was founded on concepts of legal realism and, as a result, they established commercial procedures that make the UCC more a restatement of expedient commercial practices than an effort to modify business custom.

The portions of the UNPC that are consistent with notions of legal realism work well. Payments laws drafted along the lines suggested by the established dynamics of the payments process will more likely attain the type of symmetry that the UCC achieves. By focusing on particular sections of the current draft UNPC, this Article will demonstrate the benefits of codifying payments law in a manner consistent with the jurisprudential perspective of the attorneys and academicians responsible for the UCC. It is when the drafters of the UNPC forsake that perspective that the draft payments code fails. Confronted by a payments code that does not work, the constituencies primarily concerned with payments law will withhold their approval of offending provisions and prevent passage of comprehensive legislation.[21]

The thesis of this Article is that only a "true code" that accommodates diverse and often divergent interests will improve payments law. To achieve that goal a payments code must be comprehensive; that is, it must be pervasive in scope, codifying the general law of payments systems, paper-based as well as electronic. It should follow the example set by the UCC and respond to current legislative deficiencies by clarifying the law of payments devices rather than by attempting to change the habits of the financial community. The new code should be no more

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the several articles that the draft uniform payments code has occasioned, see *supra* note 15, courts confronted with the shortcomings of current payments law have cited the draft UNPC. *E.g.*, Santos v. First Nat'l State Bank, 186 N.J. Super. 52, 71 n.25, 451 A.2d 401, 410 n.25 (1982) (UNPC would clarify status of cashier's checks as cash equivalents). Similar references were made when the proposed UCC was first drafted. *See, e.g.*, Steller v. Thomas, 232 Minn. 275, 278 n.3, 45 N.W.2d 537, 539 n.2 (1950) (sic) (cite to sales provision of draft UCC); Welch v. Schiebelhuth, 11 Misc. 2d 312, 314, 169 N.Y.S.2d 309, 311 (Sup. Ct. 1957) (discussing implied warranty provisions of proposed UCC).

20. Scott II, *supra* note 15, at 737. In a later article, however, Professor Scott states that in some situations the proposed UNPC "abandons contractual principles for allocating the risk of liability among the drawer and payor and transmitting account institutions, and applies principles drawn from tort law." Scott I, *supra* note 6, at 1699.

21. Indeed, there are indications that the financial community's uneasiness with the current draft UNPC treatment of consumer issues may require the deletion of those provisions from future drafts of the UNPC. The 3-4-8 Committee asked Professor Scott to rework P.E.B. Draft No. 3 and to "leave consumer protection measures to federal enactments." Leary & Fry, *A "Systems" Approach to Payment Modes: Moving Toward a New Payments Code*, 16 U.C.C. L.J. 283, 286 n.8 (1984). A UNPC devoid of consumer provisions would render impotent any effort at comprehensive codification of payments law. A statute that ignored the special equities attending consumer drawers could in no way be a pre-emptive enactment, a true code. Professor Scott expressed just such a concern at the 1983 Uniform New Payments Code Invitational Conference.

ambitious than absolutely necessary, and should represent an evolutionary rather than a revolutionary step in the development of payments law.

Payments legislation should not impose artificial legal distinctions among the various payments media. Before providing one transactor liability rule for checks and a different rule for credit cards, there must be a substantial reason for doing so. The desirability of such uniform treatment is the guiding philosophy of the UNPC effort: "[T]he new legal framework should not distort user choices among different payment systems, whether they be paper or card based, or electronic. . . . [T]he same legal consequences [should] attach to all kinds of transactions, where technology and the nature of the transaction [permit]."[22] That guiding philosophy may be termed "internal uniformity." This Article will suggest the proper balance of internal uniformity and variety of transactor choice by reference to code-drafting methodology. Insofar as the right to stop or reverse payments lends itself to controversy, focus on the stop payment and reversibility sections of the UNPC offers a dynamic context in which to appraise the success of the drafters' ambitious efforts.

The first section of this Article suggests the jurisprudential predisposition of the UCC drafters. The arguments for and against the codification of payments law are then evaluated by reference to the goals of commercial codification. Next, the UNPC drafters' identification of "common denominators" is presented as a necessary prerequisite to understanding the UNPC formulation of the right to stop or reverse payment, as well as to appreciating the efficacy of a provision of those rights by reference to essential principles of payments law. Finally, a proposal is made to overcome commentators' reservations with the UNPC provision for reversal of payment.

I. UNIFORM COMMERCIAL LAW AS A RESPONSE

Over twenty years ago, in an article concerning the "true code" nature of the UCC, William Hawkland explained the significance of codification.[23] He suggested that a code, unlike a mere statute, is a "pre-emptive,

22. 1983 Memorandum, *supra* note 13, at 1.

23. Hawkland, *Uniform Commercial "Code" Methodology*, 1962 U. Ill. L.F. 291. Hawkland's article shares many of the views adressed in Beutel, *The Necessity of a New Technique of Interpreting the N.I.L.—The Civil Law Analogy*, 6 Tul. L. Rev. 1 (1931). Professor Beutel suggested that if a proper science of interpreting uniform laws is to be developed, a new system must be built that recognizes the statute and not the decisions as the basic source of law. *Id.* at 19 & n.61. *See generally* State of N.Y. Law Revision Comm'n, Study of Uniform Commercial Code: Problems of Codification of Commercial Law, Legislative Doc. No. 65(A), at 11 (1955) (considering codification of commercial law of N.Y.), *reprinted in* 1 State of N.Y. Law Revision Comm'n, Report of the Law Revision Comm'n for 1955, at 41; Franklin, *On the Legal Method of the Uniform Commercial Code*, 16 Law & Contemp. Probs. 330 (1951) (discussing codification of commercial law); Gilmore, *Legal Realism: Its Cause and Cure*, 70 Yale L.J. 1037 (1961) (same).

At the time he wrote the "Methodology" article, Hawkland was a Professor at the University of Illinois College of Law. Currently he is Chancellor and Professor, Louisisystematic, and comprehensive enactment of a whole field of law,"[24] and argued the merits of codification in the commercial context.

The composition and promulgation of the UCC were a jurisprudential experiment.[25] The UCC drafters focused on the purposes of commercial codification and ordered the essential principles[26] to realize certain controlling objectives: clarity, simplicity, convenience, fairness, completeness, accessibility and uniformity.[27] A code that reflects an accommodation of those seven goals would be pre-emptive, systematic

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ana State University Law Center. Chancellor Hawkland is also an Alternate Member of the Permanent Editorial Board for the UCC and a member of the National Conference of Commissioners on Uniform State Laws.

24. Hawkland, *supra* note 23, at 292. Hawkland placed the proper emphasis on "comprehensiveness" by focusing on the "operational-body-of-law" concept, which "dictates that the set [of laws] be sufficiently inclusive and independent to enable it to be administered in accordance with its own basic policies." *Id.* at 310. It is premature to pass final judgment on the scope of the current draft UNPC. The draft excepts two-party credit cards (for example, department store accounts) from its coverage and may thereby run afoul of the "operational body of law" requirement. The UNPC "applies to any orders . . . payable by or at, or transmitted by or to, an account institution, and Articles 3 and 4 of the Uniform Commercial Code do not apply even though the order meets the requirements of those Articles." U.N.P.C., *supra* note 3, § 2(1). The "Purpose" statement following the provision explains that two-party merchant credit cards are "not covered unless used to access an account for payment to a party other than the issuer. . . . The drawer does not initiate a direction to pay but requests the delivery of merchandise against a line of credit or a cash balance held with the merchant." *Id.* § 2 comment 1 on purpose. "An order is a complete and unconditional direction by a person to pay . . . from an account which may be accessed to pay a person other than the drawer or the drawee . . . ." *Id.* § 10(1)(b).

Hawkland's impatience with "supplemental" and "fragmentary" enactments has evidently not been appreciated by the American Bankers Association Uniform Payments Code Committee. *See* Letter from W. Robert Moore, Chairman of the American Bankers Association, to Robert Haydock, Chairman of the 3-4-8 Committee (July 15, 1983) (discussing deficiencies in Permanent Editorial Board Draft No. 3) (available in files of *Fordham Law Review*).

25. Professor Karl Llewellyn, the Chief Reporter of the Uniform Commercial Code, wrote extensively in the area of jurisprudence. *See, e.g.*, K. Llewellyn, The Bramble Bush (1951); K. Llewellyn, The Common Law Tradition: Deciding Appeals (1960); K. Llewellyn, Jurisprudence: Realism in Theory and Practice (1962). Several of the attorneys who were brought together to work on the UCC have claimed that they lacked any particular expertise in commercial law prior to their association for the UCC project. *See, e.g.*, Coogan, *Reflections of a Drafter*, 43 Ohio St. L.J. 545, 545 (1982) ("Soia [Mentschikoff] says that she got into the Code by accident."); Leary, *Reflections of a Drafter*, 43 Ohio St. L.J. 557, 557 (1982) (described as one who was accepted for the Code's drafting staff "because I knew absolutely nothing about it."); Mentschikoff, *Reflections of a Drafter*, 34 Ohio St. L.J. 537, 542 (1982) ("There wasn't a single expert on the editorial board.").

26. For discussions on the role of "essential principles" in commercial law, see Gilmore I, *supra* note 2, at 1348 (thrust of law was to conform increasingly intricate transactions to simple basic formula); Gilmore, *The Uniform Commercial Code: A Reply to Professor Beutel*, 61 Yale L.J. 364, 365 (1952) (UCC should "state basic principles under which business transactions can be carried out") [hereinafter cited as Gilmore II]; Llewellyn, *Problems of Codifying Security Law*, 13 Law & Contemp. Probs. 687, 696 (1948) (should seek to develop "relatively simple set of basic legal patterns which can meet the essential needs of . . . a welter of variant practice") [hereinafter cited as Llewellyn I].

27. *See* Llewellyn I, *supra* note 26, at 687-90.

and comprehensive. It is inappropriate to conclude, however, that the success of the UCC experiment mandates code treatment of each and every piece of legislation affecting commerce. Indeed, the efficacy of codification in a particular commercial context must be demonstrated in light of current circumstances. Whether a true payments code is desirable necessarily depends on whether the problems to which the UCC drafters were responding are present now with regard to payments systems.

The UCC drafters encountered a body of commercial law comprised of multifarious "uniform" acts, which had not achieved pervasive acceptance,[28] and vague "law merchant" principles.[29] These laws lacked the precision and predictability that the drafters deemed vital to the interests of those engaged in commerce.[30] Karl Llewellyn, the principal draftsman of the UCC, recognized that the several uniform acts had been composed one-by-one, presented for adoption at different times in different jurisdictions, and, consequently, contained "clashes of theory and uncovered gaps."[31] The commercial law was "haphazard" and lacked coherence, as different frames of reference had produced legislation that ran in "perplexingly different directions."[32] Piecemeal amendment of existing laws would only have exacerbated the problem. Such patchwork readjustment, guided only by "legal patterns of happenstance origin,"[33] could not have improved but would merely have changed the existing law.[34] What was needed was a comprehensive focus responsive to the real deficiencies in commercial law and sufficiently flexible to accommodate both technological innovation and the increasing sophistication of commercial

28. The NCC promulgated other uniform acts, which achieved some success. *See* Braucher, *The Legislative History of the Uniform Commercial Code*, 58 Colum. L. Rev. 798, 799 (1958). The task of adopting any of the uniform acts proved arduous. It took 47 years for every state to adopt the Uniform Stock Transfer Act. W. Twining, *supra* note 12, at 272-73. After fifty years, only 35 states had adopted the Uniform Sales Act. *Id.* "[It has] never taken less than ten years between the date of promulgation of an act and its adoption by a majority of the states." *Id.* at 273.

29. *See* B. Cardozo, The Nature of the Judicial Process 61 (1921) (law merchant is not fixed or stereotyped). *See generally* Corbin, *The Uniform Commercial Code—Sales; Should it be Enacted?*, 59 Yale L.J. 821, 822-24 (1950) (discussion of law merchant principles). The "law merchant" was the system of rules, customs and usages that developed in England to regulate dealings among merchants and traders. The use of documents such as negotiable notes and bills became so prevalent that law merchant rules became applicable to most commercial transactions. *Id.* at 823-24.

30. *See* Hawkland, *supra* note 23, at 299 ("[U]ncomprehensive and unsystematic commercial statutes, even if widely enacted, inevitably result in lack of uniformity and certainty."); *see also* F. Beutel, Brannan's Negotiable Instruments Law 89 nn.38-40 (7th ed. 1948) (citing over 75 instances where, on identical problems, courts interpreted sections of the Negotiable Instruments Law inconsistently); Corbin, *supra* note 29, at 834-35 (old law of sales needed improved rules, analysis, organization and remedies); Gilmore II, *supra* note 26, at 367 (many conflicts arose in judicial construction of earlier acts).

31. Llewellyn I, *supra* note 26, at 690.

32. Llewellyn, *Why We Need the Uniform Comercial Code*, 10 U. Fla. L. Rev. 367, 371 (1957) [hereinafter cited as Llewellyn II]; *see* Gilmore I, *supra* note 2, at 1342.

33. Llewellyn I, *supra* note 26, at 688.

34. *See id.*

practices.[35]

Experience prior to the UCC and a sense of the needs of the business community enabled the drafters to "distinguish passing fad from the more permanent trend,"[36] and to identify certain fundamental principles crucial to the success of pre-emptive codification. They focused on existing commercial practices and prepared the several articles to give effect to the intentions, expectations and objectives of the transactors. Changes in the law were not made for the sake of making changes. Because they were properly mindful of the appropriate (conservative) contours of the endeavor, the drafters composed a code that has since been recognized as benchmark commercial codification. This Article assumes the success of the UCC experiment and considers the desirability of a payments code drafted from the same jurisprudential perspective.

A caveat is in order. While this Article will argue the merits of payments law codification (perhaps the more accurate term is re-codification),[37] the case will not be made for the promulgation of P.E.B. Draft No. 3 of the UNPC. It is premature to jump to any such conclusion. Rather, the instant inquiry treats those considerations which are, or, it is urged, should be prerequisite to true codification of this area of commercial law.

II. SHOULD CURRENT PAYMENTS LAW BE CODIFIED?

The present law of payments devices is convoluted, but that state of affairs is not universally lamented. Change is resisted both by those who represent financial institutions and by those who would safeguard the interests of consumers. The arguments for and against true codification of payments law are now sufficiently developed to accommodate inquiry into their comparative merits in light of the goals of "code" methodology.

A. *Existing Law*

The current law of payments systems is at times contradictory,[38] occasionally merely inconsistent,[39] and too often virtually nonexistent.[40] The

35. *See id.*

36. Llewellyn II, *supra* note 32, at 372. Llewellyn reasoned that statutes should be written in terms of the modern and foreseeable needs of the commercial world. *Id.*

37. Articles 3 and 4 of the UCC were, at the time they were enacted, supposed to be the "uniform payments code."

38. "Visa checks" are one type of modern payment device as to which current law is uncertain and contradictory. They are furnished to a cardholder by the issuer/financial institution. The cardholder can write checks against his line of credit. Substantial questions have been raised as to the law applicable to this new payment device. *See* Memorandum from Donald J. Rapson to the 1983 Uniform New Payments Code Invitational Conference (Sept. 30, 1983) (should "MasterChecking" be treated as a method of payment or an extension of credit, a check loan or a credit card cash advance?) (available in files of *Fordham Law Review*).

39. A classic example of such inconsistency is "double forgery" under Article 4,

law is nevertheless familiar to commercial attorneys: There is a body of financial institution protection legislation;[41] a separate body of consumer protection legislation;[42] and, finally, a payments system governed only by common law contract and tort principles.[43] A comparison of the two legislative perspectives (pro-bank and pro-consumer) with regard to stop payments manifests the incoherence of current payments law.

Uniform state law—Articles 3 and 4 of the UCC—governs check transactions.[44] Article 4, "Bank Deposits and Collections," was drafted with the interests of bank counsel in mind. The drafters' initial attempts to place heavy responsibilities on the banks and to limit contractual exoneration from liability were vigorously opposed by bank counsel. At times it appeared that the conflict could only be settled by dropping Article 4 from the Code, but a draft acceptable to the banks ultimately was

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where a check has both a forged drawer's signature and a forged endorsement. The primary issue is whether the doctrine of final payment under UCC § 3-418 controls, meaning that the drawee bank absorbs the loss, or if the forged endorsement, despite final payment, allows the drawee to place the loss upstream on a breach of warranty of title theory. *See* B. Clark, *supra* note 2, ¶ 6.5, at 6-103 to -104; Note, *Commercial Paper: Double Forgeries and Loss Allocation Under the U.C.C.: The Fork in the Yellow Brick Road*, 7 Stetson Intra. L. Rev. 241, 246-52 (1978). *Compare* Winkie, Inc. v. Heritage Bank, 92 Wis. 2d 784, 285 N.W.2d 899 (Ct. App. 1979), *aff'd*, 99 Wis. 2d 616, 299 N.W.2d 829 (1981) (precluding commercial depositor from asserting any claim against non-negligent bank from forgery losses) *with* Cumis Ins. Soc'y, Inc. v. Girard Bank, 522 F. Supp. 414 (E.D. Pa. 1981) (refusing to give effect to exculpatory clause that shifted forgery losses to corporate drawer; embezzler used signature facsimile machine). The leading case on double forgery is Perini Corp. v. First Nat'l Bank, 553 F.2d 398 (5th Cir. 1977). The court treated the double forgery as a forged drawer's signature, thus placing the loss on the drawee. *Id.* at 414-16. Professor Clark has called *Perini* "one of the most significant Article 4 decisions to date." B. Clark, *supra* note 2, ¶ 6.5, at 6-108. For a detailed analysis of *Perini*, see Baker, *The* Perini *Case: Double Forgery Revisited* (pts. 1 & 2), 10 U.C.C. L.J. 309 (1978), 11 U.C.C. L.J. 41 (1978). For a discussion and analysis of both *Perini* and *Cumis*, see B. Clark, *supra* note 2, ¶ 2.1, at S2-2 to -3 (Cum. Supp. 1983).

40. *See* Scott I, *supra* note 6, at 1664 (fragmentary body of common law governing wire transfers); *see also* NYCH Statement, *supra* note 10, at 7-8 (several problem areas left unresolved by UNPC).

41. Article 4 of the UCC is classified by many commentators as financial institution protection legislation. *See, e.g.*, Beutel, *The Proposed Uniform [?] Commercial Code Should Not Be Adopted*, 61 Yale L.J. 334, 361-62 (1952); Gilmore II, *supra* note 26, at 374-75; Leary & Schmitt, *supra* note 10, at 613-14.

42. The stated purpose of the Electronic Fund Transfer Act, 15 U.S.C. §§ 1693-1693r (1982), is to provide "a basic framework establishing the rights, liabilities, and responsibilities of participants in electronic fund transfer systems . . . [and providing for] individual consumer rights." *Id.* § 1693(b). *See* H.R. Rep. No. 1315, 95th Cong., 2d Sess. 1 (1978). For more on the EFTA, see Brandel & Olliff, *The Electronic Fund Transfer Act: A Primer*, 40 Ohio St. L.J. 531 (1979); Fox, *Another Step Toward the Cashless Society? The 1978 Federal Electronic Fund Transfer Act*, 18 Am. Bus. L.J. 209 (1980); Schellie, *Electronic Fund Transfer Act*, 34 Bus. Law. 1441 (1979); Taffer, *The Making of the Electronic Fund Transfer Act: A Look at Consumer Liability and Error Resolution*, 13 U.S.F.L. Rev. 231 (1979).

43. Scott I, *supra* note 6, at 1676-78.

44. See *supra* note 7 for authorities that have considered the continued vitality of Articles 3 and 4.

included.[45]

There are several examples of the Code's pro-financial institution bias in Article 4, only some of which have been emasculated by consumer protectionist courts.[46] The "balance" struck by Article 4 is perhaps best illustrated by section 4-403, "Customer's Right to Stop Payment; Burden of Proof of Loss,"[47] which has been referred to as a "wonder of bank lobbying."[48] In the event a bank pays an item in violation of a customer's stop payment order, the section places the "burden of establishing the fact and amount of loss resulting from the payment" on the customer.[49] Moreover, section 4-407[50] provides financial institutions with "another strong counterweight to the right of the customer to stop payment under section 4-403":[51] The bank may be subrogated to the rights of a holder in due course, or to the rights of the payee or the drawer, in order "to prevent unjust enrichment."[52]

Predictably, there is no provision for reversal of payment of an

45. Kripke, *The Principles Underlying the Drafting of the Uniform Commercial Code*, 1962 U. Ill. L.F. 321, 326-27.

46. Section 3-419(3), for example, was intended to restrict the conversion liability of depositary and collecting banks. *See* U.C.C. § 3-419(3) & official comment 5 (1977). But, as Professors White and Summers have commented, "the courts have taken up section 3-419(3), and what they have done to it shouldn't happen to a dog." J. White & R. Summers, *supra* note 10, at 591-92. Some courts have remained faithful to the drafters' intent. *See, e.g.*, Keane v. Pan Am. Bank, 309 So. 2d 579, 581 (Fla. Dist. Ct. App. 1975) (bank not liable for processing check after dissolution of partnership). One court simply ignored the section. *See* McConnico v. Third Nat'l Bank, 499 S.W.2d 874, 883-86 (Tenn. 1973). Usually courts avoid the intent of the subsection by finding that the depositary bank did not act in accordance with "reasonable commercial standards." *See* Hanover Ins. Cos. v. Brotherhood State Bank, 482 F. Supp. 501, 508 (D. Kan. 1979); *see also* Note, *Depository Bank Liability Under § 3-419(3) of the Uniform Commercial Code*, 31 Wash. & Lee L. Rev. 676 (1974) (discussing various ways courts have approached § 3-419(3)).

47. U.C.C. § 4-403 (1977).

48. B. Clark, *supra* note 2, ¶ 2.6[2], at 2-48. Any "duty" owed by the bank is effectively eliminated by subsection three. One commentator, however, has somewhat creatively reasoned that this section is consumer-oriented. *See* Pape, *supra* note 15, at 353 n.3. *But see* Beutel, *supra* note 39, at 361-62 (commentator asserting the pro-financial institution bias of Article 4); Gilmore II, *supra* note 26, at 374 (same); Leary & Schmitt, *supra* note 10, at 620 (noting Article 4's support of banking practices).

49. U.C.C. § 4-403(3) (1977).

50. *Id.* § 4-407.

51. B. Clark, *supra* note 2, ¶ 2.6[2],at 2-50.

52. U.C.C. § 4-407 (1977). There is disagreement regarding the meaning of "unjust enrichment." *Compare* J. White & R. Summers, *supra* note 10, at 690 n.134 ("[T]he phrase at best states the purpose of the section, and at worst it adds meaningless confusion.") *with* Leary, *Check Handling Under Article Four of the Uniform Commercial Code*, 49 Marq. L. Rev. 331, 367 (1965) ("[T]he obvious justification [for § 4-407] is the prevention of unjust enrichment at the expense of the payor bank who may be deemed to have paid out its own funds."). *See generally* J. Calamari and J. Perillo, Contracts 571 (2d ed. 1977) (general discussion of unjust enrichment); Restatement of Restitution § 1 (1937) (same); Perillo, *Restitution in a Contractual Context*, 73 Colum. L. Rev. 1208 (1973) (same).

"item"[53] in Article 4. The banking community's interest in finality of payment would likely never have permitted such a provision at the time the UCC was drafted. The existence of a similar right in contemporary credit card law indicates a pro-consumer shift in the mood and predisposition of legislators. While the consumer's power pursuant to Regulation Z[54] and the Fair Credit Billing Act[55] is not absolute, this federal legislation is more solicitous of the buyer's right to utilize payment leverage[56] against vendors than is Article 4. A customer who authorizes a charge to his credit card account (for example, signs the Visa slip) may resist payment to the merchant if the sale is for fifty dollars or more and the consumer's billing address is in the same state as, or within a 100 mile radius of, the merchant-seller's place of business.[57] The credit card law thereby modifies the result under Article 4 and notably eliminates the subrogation theory of UCC section 4-407.

Other consumer protection legislation in the current "patchwork" of payments law—namely the Electronic Fund Transfer Act (EFTA)[58] and the Federal Reserve Board Regulations[59] promulgated pursuant thereto—provides for a consumer's right to stop payment but does not provide a right to reverse.[60] Although the scope of the EFTA appears pervasive, several initial exclusions from its coverage severely curtail the Act's impact on the law of payments devices.[61] The exclusion of wire

53. An "item" is defined in Article 4 as negotiable and non-negotiable paper calling for the payment of money. U.C.C. § 4-104(g) & official comment 4 (1977).

54. 12 C.F.R. § 226.1-.29 (1984). Cardholder liability for a lost or stolen credit card is limited to the lesser of $50 or the amount charged prior to the issuer being notified. *Id.* § 226.12(b)(1). Regulation Z also delineates the procedures for dealing with credit card billing disputes, *id.* § 226.13(c)-(d), and describes the information that must be given to customers in their periodic statements, *id.* § 226.7. *See generally* Weistart, *Consumer Protection in the Credit Card Industry: Federal Legislative Controls*, 70 Mich. L. Rev. 1475 (1972) (discussing statutes and regulations governing credit cards); Note, *Credit Cards: Distributing Fraud Loss*, 77 Yale L.J. 1418 (1968) (discussing federal legislation dealing with credit card fraud).

55. Pub. L. No. 93-495, §§ 301-306, 88 Stat. 1500, 1511-12 (1974) (codified as amended at 15 U.S.C. §§ 1666-1666j (1982)). The Act establishes procedures for the creditor and customer to follow with regard to billing errors. N. Penney & D. Baker, *supra* note 1, ¶ 10.02[2][d], at 10-32 to -34.

56. *See* Nimmer, *Consumer Payment Systems: Leverage Effects Within An Electronic Funds Transfer System*, 17 Hous. L. Rev. 487, 507-09 (1980).

57. *See* 15 U.S.C. § 1666i (1982). For a thorough discussion of that reversibility provision and its similarity to the Federal Trade Commission Rule on Preservation of Consumers' Claims and Defenses, 16 C.F.R. § 433 (1984), see B. Clark, *supra* note 2, ¶ 9.7[2]-[3], at 9-34 to -41.

58. 15 U.S.C. §§ 1693-1693r (1982) (originally enacted as Title XX of the Financial Institutions Regulatory and Interest Rate Control Act of 1978, Pub. L. No. 95-630, § 2001, 92 Stat. 3641, 3728-41). The EFTA governs transactions such as "point-of-sale transfers, automated teller machine transfers, direct deposits or withdrawals of funds, and transfers initiated by telephone." 12 C.F.R. § 205.2(g) (1984).

59. 12 C.F.R. § 205.1-.14 (1984).

60. *See* 15 U.S.C. § 1693e (1982); 12 C.F.R. § 205.10(c) (1984). States are permitted to increase but not to restrict the EFTA's provision of consumer rights. *See* 15 U.S.C. § 1693q (1982).

61. The EFTA excepts "check guarantee or authorization services," "wire transfers,"

transfer systems[62] is perhaps most noteworthy. This lack of comprehensive legislation in the stop payment area thus evidences the inconsistencies and incoherence of current payments law.

B. *"Risk Fixing" and Other Arguments for a Comprehensive Payments Code*

Professor Scott recognized the necessity—indeed, inevitability—of a payments code in a 1978 article[63] in which he stated: " The commercial law of bank collection . . . reflects the desire of transactors to alter the competitive effects of the existing allocation of risk. Commercial legislation becomes the method by which particular interests achieve their substantive objectives, instead of a means by which society develops a rational payments system."[64] Once the affected transactors perceive a risk allocation system to be unfavorable to them, they will endeavor to fix the risks to which they are exposed in order to establish the most desirable "competitive" environment. Professor Scott argued that the American Bankers Association Bank Collection Code (Bank Code)[65] was a

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"certain securities or commodities transfers," "certain automatic [credit-debit] transfers," "certain telephone-initiated transfers," "trust accounts" and "pre-authorized transfers to small financial institutions." 12 C.F.R. § 205.3 (1984).

62. *See* 15 U.S.C. § 1693a(6) (1982); 12 C.F.R. § 205.3(b) (1984). The application of EFTA consumer protection mechanisms to such commercial (wholesale) payments systems would be enormously wasteful. It would also duplicate existing private contracts and association rules. The mechanics of the individual wire transfer systems (FedWire, BankWire II, CHIPS and S.W.I.F.T., see *supra* note 6) are governed by separate "operating rules." *See* Scott I, *supra* note 6, at 1669-74. *See generally* 12 C.F.R. § 210.25-.38 (1984) (rules governing FedWire); Rules Governing the Computerized Clearing House Interbank Payment Systems (1974) (CHIPS Rules) (available in files of *Fordham Law Review*); N. Penney & D. Baker, *supra* note 1, ¶¶ 16.01-.04, at 16-1 to -13 (discussing wire transfer rules). Moreover, federal regulations already govern wire transfers accomplished by FedWire, the communications and settlement system operated by the Federal Reserve Banks. *See* 12 C.F.R. § 210.25-.38 (1984). The Federal Reserve System requires rapid movement of messages between the various banks and branch offices. Currently, each Federal Reserve district office has communications switches to which Reserve Banks, branches, offices, the Treasury and member banks are interconnected by way of a computer message switching complex in Culpepper, Virginia. This allows administrative and research information to be sent quickly and accurately. *See* N. Penney & D. Baker, *supra* note 1, ¶ 9.02, at 9-3. FedWire effects bilateral net settlement at the end of each banking day. Scott I, *supra* note 6, at 1670. S.W.I.F.T. has no settlement capacity. N. Penney & D. Baker, *supra* note 1, ¶ 9.05, at 9-14. For a thorough treatment of the application of the UNPC to wire transfers, see Scott I, *supra* note 6.

63. Scott II, *supra* note 15.

64. *Id.* at 792.

65. Drafted by Thomas Paton, counsel for the American Bankers Association, and completed in 1929, the Bank Code was a direct predecessor of Article 4 of the UCC. *See* U.C.C. § 4-101 official comment (1977) ("This article adopts many of the rules of the [Bank] Code . . . ."). Comments to several sections of Article 4 mention the Bank Code. Scott II, *supra* note 15, at 761 n.80; *e.g.*, official comments to U.C.C. §§ 4-201 to -204, 4-207 to -208, 4-211 to -214, 4-301 to -302 (1977). *See generally* Beutel, *The Proposed Uniform Bank Collections Act and Possibility of Recodification of the Law on Negotiable Instruments*, 9 Tul. L. Rev. 378 (1935) (discussing ABA Code); Bogert, *Failed Banks, Collection Items, and Trust Preferences*, 29 Mich. L. Rev. 545 (1931) (same); Paton,

response to the "risk distortion" imposed on the check collection system by the courts and the Federal Reserve System during the early part of this century.[66] The Bank Code was "principally a mechanism for eliminating the risk differential between participant and nonparticipant banks by allocating all significant collection risks to depositors . . . [and] clearly served the interests of banks."[67] It had been adopted in eighteen states by 1932.[68] Many of its provisions were restatements of bank-customer contract terms[69] that several courts had determined to be unconstitutional sometime before the Bank Code's promulgation.[70] Moreover, the Bank Code experiment was a not-so-covert attempt to undermine application of the Sherman Act:[71] "Since they could not fix prices, banks turned to risk fixing."[72] Because financial institutions promulgated the Bank Code in an effort to avoid "risk differentials" among participant

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Bank Collection Legislation, 46 Banking L.J. 508 (1929) (same); Steffen, *The Check Collection Muddle*, 10 Tul. L. Rev. 537 (1936) (same); Townsend, *The Bank Collection Code of the American Bankers' Association*, 8 Tul. L. Rev. 21 (1933) (same).

66. In the late 1800's and early 1900's, financial institutions attempted to impose the risks of the check collection process on their customers by contract. Courts responded by construing the contracts against the banks. *See, e.g.*, Harter v. Bank of Brunson, 92 S.C. 440, 444, 75 S.E. 696, 697 (1912). At the same time, private clearinghouse associations, mostly in Boston and New York, were fixing prices on collection charges. Member banks were required to charge their customers a fixed rate for collection of out-of-town-items. Scott II, *supra* note 15, at 747. Because of these abuses and inefficiencies the Federal Reserve Board, created in 1913, became part of the check collection process. *Id.* at 747-48; *see* Federal Reserve Act, ch. 6, § 16, 38 Stat. 251, 268 (1913) (codified at 12 U.S.C. § 248(o) (1982)). This federal intrusion affected bank charges as well as the four major collection risks: "(1) nonpayment in direct forwarding, (2) negligent collecting practices of intermediate banks, (3) acceptance of worthless remittance in payment, and (4) nonpayment attributable to circuitous routing." Scott II, *supra* note 15, at 756. The financial institutions then attempted to avoid the risk-shifting of the Federal Reserve by fixing the prices that they charged for assuming certain risks, but this exposed the banks to sanctions for violating the antitrust laws. *Cf.* Standard Oil Co. v. United States, 221 U.S. 1, 58 (1911) (holding price fixing illegal).

67. Scott II, *supra* note 15, at 762.

68. *See* F. Beutel, *supra* note 30, at 133; Steffen, *supra* note 65, at 540 n.20.

69. Scott II, *supra* note 15, at 762 ("[Bank] Code incorporated the provisions of the [American Bankers Association] standard form contract.").

70. *See* Beutel, *supra* note 41, at 358; Scott II, *supra* note 15, at 761. The court in Bank of Rocky Mount v. Floyd, 142 N.C. 187, 55 S.E. 95 (1906), after overriding a clear contractual provision, commented:

> While the convenience of persons and corporations engaged in particular lines of business, and the general custom recognized and acted upon, are properly given consideration in the construction of contracts and fixing rules of duty and liability, elementary principles of law founded upon the wisdom and experience of the ages should not be violated.

Id. at 198, 55 S.E. at 99.

71. It was estimated that in 1913, 91 of the 242 clearinghouse associations in the country fixed collection charges. *See Money Trust Investigation: Before the Subcomm. of the House Comm. on Banking and Currency Reform*, 62d Cong., 3d Sess. 216, 218 (1913). "[T]he potential application of the Sherman Act probably made overt attempts to reach such [agreements] unfeasible." Scott II, *supra* note 15, at 760. By 1924, these collection charges had disappeared principally because of their increased vulnerability to antitrust attack. *Id.*

72. Scott II, *supra* note 15, at 760.

and nonparticipant banks, Professor Scott concluded that the risk differential among new payments systems would occasion a similar reaction from financial institutions today.[73] We might, therefore, assume that financial institutions would be at the forefront of the UNPC movement, but this is not the case.[74]

The financial community may not be convinced of the need for a payments code that attempts to adjust risks in the same way the Bank Code did. Professor Scott reported that because of antitrust law developments, banks determined that they could not fix the prices of customer services.[75] The Bank Code was a statutory attempt to do to consumers what the American Bankers Association had been unable to do through the use of form contracts.[76] The Bank Code's anti-competitive effects did not go unnoticed.[77] Confronted with the risk differential produced today by new payments systems, financial institutions could very well hesitate to endorse legislation that almost certainly would conflict with antitrust principles and would invite judicial as well as legislative scorn in the contemporary pro-consumer environment.

Furthermore, financial institutions have good reason to feel comfortable with the current risk differentiation. The allocation of risk provided by Article 4 (with regard to checks) and the common law of contract (with regard to wire transfers) better serves banks than would a regime that would extend some of the consumer protection provisions of debit and credit card law to check and wire transactions.[78] If financial institutions were content with the allocation of risks among transactors, a statute that had as its premise the elimination of that allocation would not necessarily gain the support of the financial community. To the extent that the risk-fixing hypothesis is invalid or disfavored by financial institutions, the foundation of the UNPC's unitary treatment of different payment systems is compromised.

In his 1978 Report to the 3-4-8 Committee, Scott described five needs, in addition to risk-fixing, which could be served by the codification of payments law: consumer protection controls on contract;[79] solution of third party problems;[80] control of natural monopolies;[81] economies of

73. *Id.* at 792; 1983 Memorandum, *supra* note 13, at 43.

74. See *infra* notes 94-103 and accompanying text.

75. Scott II, *supra* note 15, at 760.

76. See *supra* note 70 and accompanying text.

77. See *supra* note 65 for authority criticizing the Bank Code. Professor Beutel described it as a vicious type of class legislation in that it attempted to throw all the risk of the collection process on the depositors and at the same time preserve for intermediate banks all the rights of the holders in due course of the paper that they are collecting. Beutel, *supra* note 41, at 357-58.

78. It has been estimated that each year $136 trillion is transferred by checks and wire transfers, while credit cards account for only $49 billion annually. *See* Little Report, *supra* note 6, at 12, table 1. Banks are well protected in the check context by UCC Article 4 and by their ability to contract out of risks in wire transfers.

79. 1978 Report, *supra* note 14, at 31-35.

80. *Id.* at 40.

scale in risk allocation;[82] and supplementation of contract.[83] Even if the risk-fixing hypothesis cannot support the UNPC predisposition toward internal uniformity, Scott's five additional arguments suggest that codification of payments law is commercially expedient. Indeed, in some instances, compromising the internal uniformity of the draft UNPC may not impair but rather may better serve the goals of commercial codification perceived by the drafters of the UCC.[84]

Controls on contract—the first of Scott's five additional reasons for codification—are necessary because many private contracts prepared by financial institutions for execution by consumers have been and will likely continue to be largely unacceptable to courts and legislatures. This conclusion is supported by experience prior to the promulgation of the Bank Code and is clearly indicated by the contemporary "consumer protectionist" mood of recent payments legislation.[85] Another shortcoming of private contract would be its inability to bind absent third parties. A contract between customer and bank would not affect the rights of attaching creditors or possible preferences among claimants to funds held by a failed financial institution. Codification could overcome this shortcoming as well.

Additionally, in the absence of statutory guidance, natural monopolies could emerge to structure risk allocations "undisciplined by competitive forces."[86] Scott argued that although there is no evidence of price-fixing in new payments systems, risk-fixing might exist.[87] Electronic fund transfer and credit card payment systems may already be dominated by only one or two major transactors.[88] Scott warned that we will have to determine whether those interests may be trusted with private rule-making authority without the interposition of comprehensive payments

81. *Id.* at 35-38.

82. *Id.* at 40-45.

83. *Id.* at 45-47.

84. See *supra* notes 23-27 and accompanying text.

85. The limits of private contract between banks and their customers are presently established with regard to checks by UCC § 4-103(1), which prohibits a bank from contractually disclaiming its duties of good faith and ordinary care. The parties may, however, agree on standards to be used to measure such duties, so long as those standards are not "manifestly unreasonable." U.C.C. § 4-103(1) (1977). Professor Gilmore has expressed reservations: "The feature of Article 4 as it appears in the final version of the Code which is enough to make the entire Article objectionable is the freedom of contract section, § 4-103." Gilmore II, *supra* note 26, at 375.

The EFTA is more solicitous of the rights of consumers. It forbids "a waiver of any right conferred or cause of action created by this subchapter . . . [except] a waiver given in settlement of a dispute or action." 15 U.S.C. § 1693*l* (1982).

86. 1978 Report, *supra* note 14, at 35.

87. *Id.*

88. VISA and MasterCard are the two major national credit card systems used by consumers. Wire transfers are concentrated in BankWire II and FedWire. Additionally, there is only one Automated Clearing House (ACH) per region, and one national system for interchange—the National Automated Clearing House Association (NACHA). *Id.* at 36.

legislation.[89]

Further, a pervasive statute could establish certain economies of scale in risk allocation. If all customers of financial institutions were subject to or protected from the same risks, the industry could structure its processes and services either to absorb or to guard against losses occasioned by the risk. For example, it would be more efficient if either all customers or no customers assumed liability for a forged drawer's signature. This economies of scale rationale favoring the codification of payments law is quite similar to an argument originally made to support the UCC: "Men of commerce want the best laws, but they can live with 'right' laws. And they prefer the right law whose meaning is predictable and whose application is even, to the best law which operates without either uniformity or certainty."[90] Similarly, Scott's final argument in favor of the codification of payments law "has been a traditional justification for the commercial law qua law merchant":[91] Uniform commercial legislation provides a backstop to contract by establishing a legal regime for parties that could be in privity of contract but have failed to make provision by private agreement.[92] Examples of this are found in the several UCC provisions that begin with the phrase "unless otherwise agreed."[93]

Each of Scott's additional five "needs" supports the case for codification of payments law. Only the "risk fixing" argument, however, goes beyond arguing for codification and attempts to establish the desirability of imposing the same legal rules on different payments systems. The financial community may become more disposed toward the adoption of a payments code if a code can be prepared that is consistent with Scott's five additional considerations and thereby serves those interests traditionally served by the codification of payments law.

C. *The Case Against a Comprehensive Payments Code*

Representatives of financial institutions have expressed serious reservations with both the concept and substance of the UNPC. An accessible and complete expression of that community's position is the Statement of the New York Clearing House on the Proposed Uniform New Payments Code.[94] The New York Clearing House (NYCH) analogized the various payments systems to the several available transportation systems. Just as each mode of transport is essentially different in one or more crucial ways, so too are payments devices. The NYCH explained:

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89. *Id.* at 37.

90. Hawkland, *supra* note 23, at 320.

91. 1978 Report, *supra* note 14, at 45.

92. *See* 1978 Report, *supra* note 14, at 45-46.

93. *See, e.g.*, U.C.C. §§ 2-307, 2-308, 2-310, 2-319, 2-322, 2-326, 2-511, 2-513, 2-514, 3-802, 9-112, 9-503 (1977).

94. NYCH Statement, *supra* note 10. "We see no advantage to be derived from casting aside Articles 3 and 4 simply to develop a 'uniform' or 'comprehensive' payments code covering all payment systems." *Id.* at 2.

> While the types of legal issues that must be addressed in fashioning a law to govern each mode of transportation are similar (i.e., who has the right of way; what speed limits, if any, should apply; liability for passengers and parcels), would anyone argue that there is an advantage in calling pilots, captains, engineers and drivers by one functional name . . . or by having one comprehensive code covering all methods of transportation?[95]

Because of the basic differences between payments systems, the NYCH would not subject the various methods of value transfer to unitary treatment. Instead, the organization would "address *separately* the problems identified by the 3-4-8 Committee with electronic funds transfers, Articles 3 and 4 and, if necessary, other payment systems."[96] Such an approach would necessarily preclude codification of payments law in a manner resembling UCC-type "true" codification.

The analogy on which the NYCH argument is founded is, to say the least, far-fetched.[97] Although it would be ludicrous to impose the same speed limits on airplanes and buses, it is correct to impose on airlines and bus companies, as common carriers, the same standard of care toward passengers.[98] Many such elements of transportation systems, which operate as do our laws of tort and contract (rather than physics), are susceptible to codification, but that is not to say that the same tort or contract rules should apply to distinguishable problems. If overbooking is a contract problem in air travel but not in intra-city bus travel, it may not be appropriate to subject both systems to the same overbooking regulation. As the NYCH observed, "differences in operational aspects, frequently reflected in the rights and obligations of the parties, constitute the reason for the utility of one system over another."[99] The inquiry should focus on how best to order the differences in the interest of predictability and certainty. A payments code could formulate the differences to "identify results that can be justified on efficiency or distributional grounds,"[100] without impairing or eliminating transactor choice. Such a comprehensive enactment could solve essentially different problems in different ways but still treat in a single, unitary enactment as many problems of payments law as coherently as possible.

There is a further problem: Reluctant attorneys fear the unknown. Although current payments laws overlap and conflict,[101] they are famil-

95. *Id.* at 10-11. As one commentator has noted, the arguments presented by the financial community closely parallel those made in the 1950's when the New York Study Commission considered and criticized the proposed UCC. Mittelsteadt, *supra* note 11, at 377 n.119.

96. NYCH Statement, *supra* note 10, at 3 (emphasis in original).

97. *But see Id.* at 12 (Notwithstanding protestations to the contrary, "[w]e believe that this analogy is not far-fetched.").

98. *See* R. Hutchinson, A Treatise on the Law of Carriers §§ 893-895 (3d ed. 1906); W. Prosser, Law of Torts § 34 (4th ed. 1971).

99. NYCH Statement, *supra* note 10, at 12.

100. Scott II, *supra* note 15, at 792.

101. See *supra* notes 38-43 and accompanying text.

iar to the lawyers, bankers and the public who work with them regularly. As one commentator queried, "having mastered these legal languages, should we all now be forced to forget them and learn Esperanto?"[102] Arguably we should. Commercial attorneys have been willing to relearn.[103] But they would be ill-advised to forget the "legal languages" they have learned because knowledge of the old rules would aid in construction of a payments code. Moreover, any piecemeal solution to the problems of the currently incoherent payments law will require attorneys to learn the new "patchwork" but will not guarantee consistent treatment of similarly situated transactors.

III. IDENTIFICATION OF COMMON DENOMINATORS

Effective codification depends on the identification of common denominators in seemingly different systems and the development of analytical and definitional tools that emphasize those essential principles while denying legal effect to insubstantial differences. The architects of the UCC set out to formulate, or perhaps more accurately, discover the essential principles of commercial law. Once those essential principles were identified, they served as the foundation on which the UCC experiment has developed. The drafters remained sensitive to the problems that transactors familiar with the established law would encounter with legislation that purported to make drastic changes. The drafters' choice of essential principles was therefore informed by established practices. The same approach is useful in codifying payments law.

It is no longer appropriate, if it ever was, to distinguish between payments systems as either electronic or paper-based. The intrusion of computers into payments procedures has eliminated any bold line that might have separated paper-based devices (checks and notes) from those devices that operate in concert with magnetic tapes or telephonic tones. The corporeal safety paper "item" of Article 4 stands a very good chance of being transformed into an electronic impulse somewhere along its journey from drawer to drawee and perhaps back to drawer.[104] The credit card slip signed by a customer at point-of-sale is even more likely to undergo such a metamorphosis.[105] "The central characteristic of electronic fund transfers . . . is the use of computer and electronic technology *in place of* checks or other paper items to effectuate the transfer of funds."[106]

The UNPC drafters realized that the scope of a uniform payments law

102. Geary, *supra* note 15, at 341. Professor Gilmore confronted this same argument during the UCC debate. *See* Gilmore II, *supra* note 26, at 379 (replying to Professor Beutel's assertions in Beutel, *supra* note 41, at 348).

103. *See* Llewellyn, *supra* note 32, at 368.

104. See *supra* note 3 and accompanying text.

105. *See* 1978 Report, *supra* note 14, at 19-20.

106. 2A F. Hart & W. Willier, Bender's UCC Service, Commercial Paper § 16.01, at 16-8 (1972) (emphasis in original); *see* S. Rep. No. 915, 95th Cong., 2d Sess. 2 (1978).

generally should not be determined by reference to the relative electronic sophistication of the various payments systems. It is inappropriate to suggest that a payments system that operates without indispensable paper should be governed primarily by consumer protection legislation, while the law governing paper-based transactions favors the interests of financial institutions. Distinctions should be drawn only on the basis of differences that matter,[107] and it is better if those "differences" are familiar principles of established law. When the drafters of pervasive legislation identify and give effect to the essential elements of their subject matter, the drafters are better able to compose the type of "pre-emptive, systematic, and comprehensive enactment" envisioned by Professor Hawkland.[108]

The UNPC minimizes the legal effect of noncrucial distinctions between payments systems. Section 51, which defines both "draw" and "pay" orders, contains the primary example of the Draft's formulation of essential principles.[109] A draw order, such as a check, flows from a drawer to a payee and "*pull* [*s*] credits back to the person entitled to payment in a direction opposite to the one in which the order is transmitted."[110] The UNPC comment to this section suggests that, in addition to the familiar check, a draw order may be electronic, such as "a prearranged debit through a clearing house."[111] The student of commercial paper is comfortable following the flow of warranties from endorsee to endorser/presenter to drawee, as payment of the item flows back in the opposite direction.[112] In the automated clearing house setting a prearranged debit works similarly: A depositor of the "receiving" bank authorizes a vendor to debit the depositor's account at the receiving bank; the vendor notifies its bank—the "originating" bank—of the preauthorized debit; the originating bank then credits the vendor's account for the appropriate amount and forwards electronic advice of the transaction to the appropriate regional Automated Clearing House (ACH), which sends the advice on to the receiving bank, which debits the depositor's account. Just as in the check collection scenario, the order goes from debtor (drawer/depositor) to creditor (payee/vendor), and the creditor utilizes its bank (depositary/originating) to effect collection through a centralized medium (Federal Reserve Bank/ACH) and charge the debtor's account institution (drawee/receiving bank).[113]

The pay order denomination also formulates the common characteristics of different payments devices: "The order and the funds are *pushed* from the drawee to the payee, and the order and funds move in the same

107. *See* 1983 Memorandum, *supra* note 13, at 1.
108. See *supra* notes 23-24 and accompanying text.
109. *See* U.N.P.C., *supra* note 3, § 51.
110. *Id.* § 51 comment 1 on purpose and existing law (emphasis in original).
111. *Id.*
112. *See* U.C.C. §§ 3-417, 4-207 (1977).
113. *See* 1978 Report, *supra* note 14, at 13-17.

direction."[114] Wire transfers and prearranged credit orders through an ACH are examples of pay orders.[115] Thus the drafters identified the lowest common denominator in seemingly different systems and developed an analytical and definitional tool that emphasizes that common denominator while denying effect to insubstantial differences.

IV. THE UNPC APPROACH TO STOP PAYMENT AND REVERSIBILITY

The treatment of stop payment and reversibility in P.E.B. Draft No. 3 of the UNPC[116] offers a dynamic context in which to appraise the UNPC's jurisprudential perspective and to seek to identify the essential common denominators. The issues in this area have been around long enough to have come into sharp focus[117] and the elements of the several payments devices are established. The commentators and the drafters of existing payments legislation have identified certain distinctions based on the reasons for the customer's exercise of a right to stop or reverse payment, the type of payment medium and the sophistication of the customer.[118] The rules in force under current law represent the inconsistent conclusions reached as a result of the interaction of those transactional variables and the particular drafter's appraisal of cost[119] and risk[120] considerations. The UNPC drafters would therefore have engaged in an analysis designed to yield state-of-the-art commercial law with respect to the right to stop and reverse payment.

The two primary reasons for a customer's requesting a stop or reversal of payment are loss or theft of the payment device and dispute resolution. The overwhelming majority of stop payment requests in the familiar context of UCC "items"[121] are issued by customers in response to the loss or theft of a check. Nevertheless, insofar as "the party in possession of the funds enjoys an edge in any dispute,"[122] a customer may retain substantial leverage by exercising a stop payment order. In virtually every instance in which the stop payment of an item would be exercised, the right

114. U.N.P.C., *supra* note 3, § 51 comment on purpose and existing law (emphasis in original).

115. *Id.*

116. For discussions of these issues in the context of the various payments systems, see Mittelsteadt, *supra* note 11, at 379-407; Nimmer, *supra* note 56, at 513-15, 524-34.

117. For a description of the genesis of stop payment, see W. Holdsworth, *supra* note 29, at 130-31.

118. *See, e.g.*, Mittelsteadt, *supra* note 11, at 366-78; Nimmer, *supra* note 56, at 488-515; Scott II, *supra* note 15, at 782-92. *See generally* Chin, *Electronic Fund Transfer: A Selected Bibliography*, 13 U.S.F.L. Rev. 555 (1979) (references to materials involving EFT systems); Scott, *Bibliography*, 2 Computer L.J. 183 (1980) (same).

119. Mittelsteadt, *supra* note 11, at 367-69.

120. Other considerations include: operational efficiency of financial institutions; costs to merchants; and the accommodation of users of the systems. *Id.* at 369-79.

121. *See* U.C.C. § 4-104(1)(g) (1977).

122. Mittelsteadt, *supra* note 11, at 364. Retaining possession of the funds may be the only way a party can afford to force the payee into dispute resolution. *Id.*

is aleatory, dependent upon both fortuity[123] and, in the rare case, the sophistication of the drawer.[124] The drafters of the UNPC have recognized the two distinct reasons customers abort payments and, for the most part, treat each separately.

A. *Liability as Drawer For Unauthorized Orders Under the UNPC*

A drawer may avoid liability for an "unauthorized order"[125] pursuant to the provisions of section 200 of the UNPC by issuing the appropriate notice of loss or theft to the "payor account institution."[126] The section encourages customers to notify the drawee to dishonor an order. A consumer who fails to notify his account institution of loss or theft of an access device will be liable for the first fifty dollars (so long as the total loss is less than $500) whether or not his negligence contributed to the loss or theft.[127] This consumer liability ceiling is, as described, limited. In all other cases a drawer, consumer or otherwise, whose negligence "substantially contributed to the order becoming unauthorized," is precluded by section 202(2) from complaining that the order was unauthorized.[128] Although negligence is left undefined, the UNPC drafters explained that "it should generally consist of actions which could be taken by the drawer to prevent the loss at a lower cost than the discounted expectation of loss."[129] There is, then, a very clear incentive for drawers to issue an "unauthorized order" notice, like a loss or theft stop payment order, to avoid the expense of litigation and the vagaries of negligence analysis. Indeed, failure to notify an account institution of sus-

123. The issue is one of timing—whether the customer can exercise his right to stop payment before the check gets to the bank. The more quickly the check is "collected," the less time a customer has to stop payment. UCC § 4-403(1) (incorporating UCC § 4-303(1)) provides that the stop payment order is untimely if the bank has accepted the item, paid the item in cash, settled for the item, or completed posting of the item. *See* U.C.C. §§ 4-303(1), 4-403(1) (1977).

124. The payor bank would argue that under UCC § 4-407(a) it is not liable for wrongful payment over a stop payment order, because the drawer would have been liable in any case to the holder in due course of the item. An intermediary bank may be a holder in due course. To avoid that argument the sophisticated drawer can cross out "the order of" on his check. Without that language the check is not a negotiable instrument under UCC § 3-104(1)(d). Consequently there can be no holder in due course and the drawer is protected against the bank's § 4-407(a) claim.

125. The UNPC defines an "unauthorized order" as "any order which is not authorized." U.N.P.C., *supra* note 3, § 54(2). An order is "authorized" if it is initiated by the drawer or is initiated or paid with the drawer's authorization "and remains so unless . . . materially altered . . . [or] transmitted without any necessary authorization, including, in the case of a written draw order, all valid endorsements." *Id.* § 54(1).

126. *Id.* § 200(1). UNPC § 53(4) defines "payor account institution" as "the account institution which maintains the account directed to be debited by the drawer of an order." *Id.* § 53(4). The comments provide that the term is applicable to both pay and draw orders. *Id.* § 53 comment 3; *cf.* U.C.C. § 4-105(b) (1977) (Payor bank "means a bank by which an item is payable as drawn or accepted.").

127. *Id.* § 200(2)(a).

128. *Id.* § 202(2).

129. *Id.* § 200 comment 3 on purposes.

pected or known loss or theft may very well constitute section 202(2) negligence. Article 4 of the UCC nowhere provides that failure to notify a drawee bank of the loss or theft of a check alone constitutes negligence that would permit the bank to charge the customer's account for the unauthorized order.[130]

Section 200 neither expressly provides that a bank may charge a customer for issuing an unauthorized order notice nor precludes a bank from doing so.[131] The provision does impose on banks costs that arguably ought not to be passed on to all of a bank's customers without reference to whether an individual customer issues a notice. In any event, section 200 would be better drafted if the right to charge were either granted or denied expressly.

Whether banks may, under current check law, charge a customer for exercising the right to stop payment was considered in two opinions of the Michigan Attorney General, whose position changed between April 13, 1981[132] and August 7, 1981.[133] The April Opinion argued that to permit banks to charge a fee would sanction reallocation of risk in a manner contrary to the scheme provided by the UCC. That position was, of course, naive. If banks were precluded from passing on the cost of a stop payment to a particular customer, they would endeavor to spread the cost over all customers. The August Opinion essentially repudiates the Attorney General's earlier remarks by focusing on the freedom of contract sections of the UCC[134] and deciding that customers may agree to pay a stop payment fee. The substance of that "agreement" was given only passing reference. The two opinions are, in reality, irreconcilable, and we may assume that the change of position resulted from the Attorney General's Office coming to terms with economic realities.

UNPC section 200, insofar as it concerns loss or theft of an order, is consistent with the better view concerning risk allocation in the unauthorized order context. "Those risks include liability to the customer for damages suffered as a result of bank negligence or error, and in other

130. *See* U.C.C. § 4-406 (1978)

131. *See* U.N.P.C., *supra* note 3, § 200. UNPC § 425(13) provides that a bank "may require any person directing it to stop or reverse an order to pay any fees or charges for such service which it reasonably believes are necessary to cover the cost of providing the service." *Id.* § 425(13). By application of the construction principle of expressio unius est exclusio alterius (expression of one thing is the exclusion of another), 2A C. Sands, Sutherland's Statutes and Statutory Construction, § 47.23, at 123 (4th ed. 1973), it could be argued that the drafters did not intend to sanction a bank charge for issuance of an authorized order notice, because § 200 contains no language similiar to that in § 425(13).

132. Op. Mich. Att'y Gen. No. 5867 (1981) (bank may not charge customer a fee on stop payment order), *reprinted in* 30 U.C.C. Rep. Serv. (Callaghan) 1626 (1981).

133. Op. Mich. Att'y Gen. No. 5947 (1981) (bank may contract with customer for fee on stop payment order), *reprinted in* 33 U.C.C. Rep. Serv. (Callaghan) 1445 (1981). This opinion addressed the question of enforceability of an express contract between a bank and its customer in which the customer agrees to pay a fee in connection with a stop payment order.

134. See *supra* note 93 and accompanying text.

situations, liability to a third party claim that the stop payment was improper."[135] If an account institution fails to honor a proper unauthorized-order notice, UNPC section 200 shifts the risk of loss on the instrument from the customer to the financial institution. This section departs from current check law by placing the crucial burden of proof on the account institution, which must show, "if the order is unauthorized . . . that the conditions for liability of the drawer . . . have been met."[136] Current check law provides that the drawer bears the burden of proof on the damages issue.[137] The second risk, that of a third-party claim, is inapposite in the section 200 context, in which the loss or theft of the payment medium is a prerequisite to application of the provision. If a third party asserts a claim that the unauthorized-order notice was improperly given effect, the issue is thrown out of section 200 and comes within the scope of section 425, which precludes stop payment with regard to those media that have been issued by the account institution "in payment of its own underlying obligation."[138] That language is intended to include "cashier's checks, bank drafts, 'teller's checks,' money orders, and certified checks."[139] Such media are also referred to as "remittance items."[140]

The basic scheme of section 200 works. The unitary approach, which subjects all nonremittance orders to the same legal rules, is successful in this context because choice among nonremittance items is not important here: No rational transactor would use any conceivable noncash payment medium and not prefer to limit its exposure in the event that the order is lost or stolen. It is therefore not difficult to establish a consistent, acceptable rule for avoiding payment of unauthorized orders. In the terms of the NYCH analogy,[141] if a traveler loses his ticket, a single rule would work as well to minimize the loss whether the ticket was for passage by train, bus or airplane.

UNPC section 200 illustrates that so long as important choice is not impaired, a comprehensive code can order the essential principles of commercial practice to improve the status quo. When meaningful choice is impaired and essential principles are not properly utilized as a foundation, however, the aims of true codification are frustrated. The next portion of the Article evaluates the most recent draft UNPC reversibility provision by reference to that jurisprudential perspective.

B. *Dispute Stop Payment and Reversibility under the UNPC*

Section 425 of the UNPC provides that a customer may stop or reverse

135. Mittelsteadt, *supra* note 11, at 369 (citations omitted).
136. U.N.P.C., *supra* note 3, § 200(3).
137. U.C.C. § 4-403(3) (1977).
138. U.N.P.C., *supra* note 3, § 425(1).
139. *Id.* § 425 comment 7 on purposes.
140. *Id.*
141. See *supra* notes 95-103 and accompanying text.

payment of "authorized" orders[142] to maintain leverage in a contract dispute.[143] Does this section, as a matter of commercial code jurisprudence, represent the proper formulation of essential principles? If the drafters have not identified and made operative the correct bases for distinction, the product of their efforts will frustrate rather than serve the controlling objectives of commercial codification and preclude the enactment of a payments law that is truly pre-emptive, systematic and comprehensive.

In addition to continuing the UCC rule of stop payment, UNPC section 425 also provides consumer drawers a right to reverse an order of fifty dollars or more within three business days after the order has been "finally paid,"[144] so long as the order was not for cash withdrawal or a check transmitted in paper form (in other words, not truncated), and the drawer has not waived the right to reverse orders drawn on the account.[145] Insofar as the section creates a sweeping consumer payment reversal right, it has attracted the displeasure of financial interests.[146] Consumer advocates, on the other hand, would complain that any "right" that consumers may waive is ephemeral.[147]

The arguments against provision of a right to reverse payment focus on the burden that such provision would impose on payments systems. The UNPC section would provide consumers with a pervasive right: Pay as well as draw orders would be subject to reversal.[148] Nevertheless, the section cannot be criticized as eliminating all differences among the affected payment media. Remittance orders, as well as the exceptions noted above,[149] provide transactors a form of "choice." But the consumer's option to waive the reversal right will likely be a function of the choice of the merchant or financial institution, rather than that of the consumer.

Although no distinct interest group has come rushing to the defense of section 425, there are cogent arguments in support of a right to reverse payment. The right now exists in the credit card context.[150] Moreover, many of the arguments in favor of providing a stop payment right are apposite in the reversal context, such as the policy of improving the bar-

142. For the definition of an "authorized order," see *id.* § 54(1).

143. *See* U.N.P.C., *supra* note 3, § 425 & comment1 on purposes.

144. *See id.* § 425(2).

145. *Id.*

146. *See, e.g.*, NYCH Statement, *supra* note 10, at 18.

147. In order to protect consumers some commentators maintain that stop payment or reversibility should be mandated for all EFT systems. *See, e.g.*, Note, *Overcoming the Obstacles to Implementation of Point-Of-Sale Electronic Fund Transfer Systems: EFTA and the New Uniform Payments Code*, 69 Va. L. Rev. 1351, 1369 nn.84-85 (1983).

148. *See* U.N.P.C., *supra* note 3, § 425 comment 1 on purposes.)

149. See *supra* notes 144-55 and accompanying text.

150. See *supra* notes 54-57 and accompanying text. The point-of-sale systems in Michigan and Wisconsin currently provide consumers a right to reverse payment. *See* Mich. Comp. Laws Ann. § 488.16 (West Supp. 1984-85); Wis. Admin. Code § [Commissioner of Banking] 14.09 (1983).

gaining power of a drawer/buyer in a dispute with a payee/seller.[151] The right to reverse is a necessary adjunct to the stop payment right. Insofar as the right to stop payment is cut off after the order is paid, the provision of a right to reverse payment for three business days after final payment replaces the "stop payment window [that] may be appreciably shortened . . . by check truncation [and the] use of on-line debit cards at the point-of-sale."[152] Also, in conjunction with three other UNPC provisions,[153] section 425 avoids the pro-bank result currently guaranteed under UCC sections 4-403 and 4-407 to payor collecting banks and payor banks by subrogation.[154]

Those who generally resist the provision of a right to reverse payment object particularly to section 425's formulation of the right. The objections raise important issues of commercial code jurisprudence and have been urged not only by those with vested interests in the health and welfare of financial institutions, but also by those who are more impartial.

Roland Brandel, a practicing attorney who has been quite active in the evolving law of new payments systems,[155] expressed his uneasiness with both the concept of reversibility and section 425 at the 1983 Uniform New Payments Code Invitational Conference.[156] He argued that the right to reverse fails on a basic fairness level because it gives consumers an absolute right to steal after making a simple phone call. Moreover, he argued that inasmuch as the expense of providing the right would ultimately be shifted to consumers,[157] we should consider that cost before we decide that the provision of such a right is in the best interests of all consumers. Brandel believed that reversibility, to the extent ever desirable, should be a matter of sales law, governed by UCC article 2, rather than payments law. If considered within the Sales Article, reversibility could be treated more directly as a problem of dealing with recalcitrant merchants. Brandel would prefer that the problem be addressed by the use of consumer protection sanctions instead of burdening the payments system. Arguably, the financial institutions may not be the most economically efficient segment of the commercial community to confront

151. *See* U.N.P.C., *supra* note 3, § 425 comment 1 on purposes.

152. *Id.* § 425 comment 2 on purposes.

153. *Id.* §§ 103, 426, 432. Section 103 outlines the rights of a funds claimant with or without limited due course rights. Section 426 deals with competing claims to an account. Section 432 provides a payor account institution's right to subrogation on improper payment.

154. See *supra* notes 47-52 and accompanying text.

155. *See generally* D. Baker & R. Brandel, The Law of Electronic Fund Transfer Systems (1983 Cum. Supp. to N. Penney & D. Baker, *supra* note 1); R. Brandel, J. Terraciano & B. Abbott, Truth in Lending Compliance Manual (2d ed. 1981); Brandel & Soloway, *Consumer Financial Services*, 38 Bus. Law. 1267 (1983); Brandel, *Electronic Fund Transfers and the New Payments Code*, 38 Bus. Law. 1355 (1983). Mr. Brandel is a partner with the San Francisco firm of Morrison & Foerster.

156. R. Brandel, Remarks at the Uniform New Payments Code 1983 Invitational Conference (Sept. 30, 1983) (available in files of *Fordham Law Review*).

157. *Id.*

the problem of recalcitrant merchants. Indeed, Brandel suggested that small claims courts may provide the best means for consumers to vindicate their rights.[158]

Brandel's criticism of section 425's particular formulation of a reversal right is useful. He raises several fundamental questions. First, how does a consumer or payee know if there is a right to reverse the payment? If a check is used by a consumer drawer and truncated prior to its reaching the drawee, there is a right to reverse for three days after final payment of the item.[159] But if the paper check is not truncated prior to its reaching the drawee, there is no right to reverse. Also, insofar as a consumer will not know precisely when final payment has occurred, he will not know when the right has lapsed. Recall that this problem exists under current check law.[160] Second, how does the payee know whether the account on which the check is drawn provides a right to reverse? Section 425 provides small comfort to the payee in that the comments suggest that "account institutions may specially identify orders drawn on consumer accounts for the convenience of persons taking such orders and for account institutions making availability determinations."[161] Finally, to what extent is the policy in favor of more immediate funds availability in diametric opposition to a reversal right? Recent legislative initiatives have suggested that there will be increasing pressure on financial institutions to make funds available for withdrawal as of right as expeditiously as possible.[162] UNPC section 421(2) provides that funds are not available as of right on consumer orders until three days from final payment have elapsed.[163] But even those banks that are currently willing to expose themselves to insufficient funds risks and permit customers to draw on uncollected funds may not be willing to increase that exposure by permitting withdrawal where there is the additional possibility of reversal. An impartial study conducted by the National Commission on Electronic Fund Transfers (NCEFT) concluded that, in the context of point-of-sale transactions, reversibility should not be required by legislation.[164] The study noted that "the merchants most likely to accept EFT services

158. *Id.*

159. U.N.P.C., *supra* note 3, § 425(2)(b).

160. *See* U.C.C. § 4-303(1) (1977).

161. U.N.P.C., *supra* note 3, § 425 comment 2 on purposes.

162. *See, e.g.*, 1983 N.Y. Laws, Ch. 234 (bill to establish reasonable time period within which bank must permit customers to draw on deposits); 1983 Cal. Legis. Serv., Ch. 1011 (West) (bill to require that credit given by bank for item deposited becomes available to customer for withdrawal as of right); *see also* N.Y. Times, June 18, 1983, at 29, col. 6 (discussing the New York legislation).

163. U.N.P.C., *supra* note 3, § 421(2).

164. EFT in the U.S., *supra* note 1, at 51. The National Commission on Electric Fund Transfers has 26 members drawn from the government, financial institutions and the public. The Commission was directed by Congress to "conduct a thorough study and investigation . . . and to recommend appropriate administrative action and legislation necessary in connection with the possible development of private and public EFT systems." *Id.* at iii.

are the large retailers who generally allow customers to return merchandise within a reasonable period of time . . . [whereas] [d]isreputable merchants are unlikely to accept EFT with required reversibility."[165] If all or nearly all payments media afford consumers a reversal right, consumers would be denied meaningful choice. Although section 425 provides that consumers may waive the right to reverse, a waivable right may be of dubious value. Financial institutions could price the right in such a way as to preclude effectively its exercise, or merchants could refuse to accept media that give access to accounts providing a right to reverse. A waivable right to reverse, then, may do nothing to preserve real consumer choice. The UNPC drafters have failed to identify and utilize the correct essential principles and, therefore, have not formulated an effective reversal provision in section 425.

V. Provision of a Right to Reverse Payment by Reference to Essential Principles

A reversal right drafted in a manner consistent with commercial code jurisprudence could overcome the Brandel and NCEFT reservations. Future drafts of a payments code should provide a right to reverse payments for a specified period only when a consumer uses a payment medium that draws against a prearranged line of credit.[166] This recommendation would modify the P.E.B. Draft No. 3 provision by focusing on the cash/credit distinction, a crucial essential principle, and by serving rather than undermining transactor expectations.[167] Additionally, even if the right is provided only in the credit context, real consumer choice would be maintained so long as the right cannot be waived.

Although proposed section 425 draws distinctions among payments media to some extent, it does not distinguish in terms palatable to a good portion of the commercial community. This is a difficult area in which to establish meaningful differences that will prove tenable over the course of the development of new payments systems. For instance, while it may be desirable at the present time to encourage the development of point-of-sale (POS) systems, a reversal right should not attach to that medium merely for the sake of better marketing that product. Marketing, to the extent of making distinctions to encourage the use of one payment device

165. *Id.* at 51.

166. In the event the UNPC is ultimately prepared as a statute regulating wholesale payment systems and leaves the provision of individual consumer rights to separate federal and state legislation, see *supra* note 21, the reversibility issue does not go away. Future adjustments of consumer protection law will need to come to terms with the right to reverse payment, which is already available in some retail payment systems. See *supra* notes 54-57, 150 and accompanying text.

167. For a case that considers the importance of effectuating transactor expectations, see Santos v. First Nat'l State Bank, 186 N.J. Super. 52, 70, 451 A.2d 401, 410 (1982) ("The [UCC's] ambiguities give us concern, as well as the realization that, because cashier's checks are perceived by the public as cash-like, the [UCC] should be interpreted to limit the defenses that can be raised.").

over another, is not the province of a true commercial code. It may very well be that technology will develop a payments system more desirable than POS. "[I]t is a matter of vital importance that [a code] as a whole be kept in terms of such generality as to allow an easy and unstrained application of its provisions to new patterns of business behavior."[168]

Gilmore argued in favor of recognizing certain strategic strong points[169] that could support a commercial code as business practices developed. The essential principles or strategic strong points identified ought to serve rather than frustrate the elusive goal of simplicity.[170] The credit/cash difference is an essential principle—a crucial basis for distinction—that is certain to endure so long as selling money for "interest" remains popular. The provision of a right to reverse payments only in the credit card context would be consistent with commercial code jurisprudence. Financial institutions could use the same familiar credit evaluation techniques now in use to screen applicants for credit cards and overdraft privileges, thereby further reducing the likelihood that the right to reverse would be exercised irresponsibly. From the drawee bank's viewpoint, reversibility would give rise to increased costs—perhaps no greater and maybe less on a per item basis than those produced by the exercise of a stop payment right—which can be passed directly on to the consumer when the reversal right is exercised. For other banks in the chain of collection, the right to reverse would raise no more than the familiar funds availability issue. The financial community's provision of the right could be used in the give and take of a uniform payments code drafting process as a counterweight to consumers' lobbying for more expeditious availability of credits for withdrawal. Moreover, depositary banks would continue to earn interest on the uncollected or not-yet-reversed funds.

Permitting a right to reverse only in the credit context is consistent with commercial expectations and practical realities. Whether or not this right exists, a consumer who has drawn against a line of credit remains in possession of the funds and the leverage that goes with possession. From the typical consumer's viewpoint, only the identity of the potential plaintiff changes. At the end of the provided reversal period the risk of nonpayment shifts from the merchant to the drawee financial institution, but the credit risk that remains is no more than the drawee bargained for when it issued the credit device and is therefore no longer pertinent to the reversal calculus.

The proposal is also consistent with the needs identified by Professor

168. Gilmore I, *supra* note 2, at 1355. Professor Gilmore also noted that "[c]ommercial codification cannot successfully overparticularize: the penalty for being too precise is that the statute will have to keep coming in for repairs (and amendment is a costly, cumbersome and unsatisfactory process) or else become a dead-letter." *Id.*

169. *See id.* at 1358.

170. *See id.* at 1356.

Scott, which are served by the codification of payments law.[171]

First, provision of an inalienable right to reverse when a line of credit is utilized guarantees real consumer protection controls on contract, which are uncertain if the right may be waived. Financial institutions benefit by charging interest when a payment medium draws on credit, and a right to reverse benefits the consumer. Although reversibility would burden the payments system, account institutions could be (and are under proposed section 425) permitted to charge a consumer for exercising the right. Also, insofar as credit access by use of payment media may increase impulse sales, reversibility is consistent with federal and state laws giving consumers a period of time after an "in-house" sale (usually of the door-to-door variety) in which to withdraw (reverse) the purchase commitment. If increased impulse sales are occasioned by more immediate access to credit, the same consumer protection policies served by statutory "cooling-off periods" in door-to-door sales may be effected by permitting reversibility.

Second, the proposal will provide solutions to third party problems. Merchants and intermediary financial institutions are the affected third parties if reversibility of payments is permitted. The proposal provides law to govern those third party relationships, and may, in fact, supply that allocation of rights and duties for which the parties would bargain in the absence of prohibitive transaction costs.[172] If merchants could gain more from increased sales than they would lose from consumers' irresponsible exercise of a right to reverse, merchants and consumers would agree to the provision of reversibility if they were able to contract on the issue. Financial institutions would contract with both merchants and consumers to permit reversibility if interest revenue exceeded the cost of providing the service. Under current law, national credit card services provide for reversibility, and consumers pay for that right in the form of interest. Although the proposal would not provide banks a right to discount checks as they now do with credit card slips, it would permit banks to charge consumers for exercising the right to reverse, a charge for which current credit card law does not provide.

Third, control of natural monopolies would be facilitated by the proposal. Professor Scott offered the Visa and Master Card systems as ex-

171. *See* 1978 Report, *supra* note 14, at 31-47. See *supra* notes 79-93 and accompanying text.

172. Legal fees incurred in the course of negotiating a contract are an example of transaction costs. *See* W. Baumol, Economic Theory and Operations Analysis 631-32 (4th ed. 1977). It may cost an individual consumer a small amount to find a merchant willing to permit reversal on a particular payments medium, but that small amount multiplied by all consumer purchases accomplished by the use of reversible media would prove burdensome. The proposal avoids that burdensome transaction cost. For a recent, if inconclusive, study of the effects of credit card use on retail sales, see Board of Governors of the Fed. Reserve Sys., Credit Cards in the U.S. Economy: Their Impact on Costs, Prices, and Retail Sales (1983).

amples of a natural monopoly.[173] By guaranteeing consumers a right to reverse and extending reversibility to payment devices other than national credit cards, the anti-competitive effects of such natural monopolies are reduced. Under the proposal, any bank that offers overdraft protection would necessarily offer reversibility, thus giving the consumer greater choice in selecting a payment medium. The provision of an inalienable statutory right to reverse also precludes natural monopolists from denying consumers the right that a truly competitive environment might provide.

Fourth, because the proposed formulation would be mandatory, it may achieve even greater economies of scale in risk allocation than would result were the right to reverse waivable. Finally, it is inappropriate to have a merely supplemental (waivable) rule governing consumer reversibility. Although Professor Scott recognized this in his 1978 Report,[174] proposed section 425 ignores the argument against mere supplementation: "Any rules of merely supplemental nature, which are capable of being varied by private agreement, perform no service to the parties" to transactions achieving economies of scale, such as bank credit card transactions or wire transfers.[175] The proposal of this Article, then, merely brings the reversibility provision in line with the policy of the fifth need by making the right to reverse mandatory in the credit context.

CONCLUSION

A UNPC should serve traditional and proven principles of commercial code jurisprudence in order to improve the current piecemeal legislation governing payments devices. While it is important that the drafters remain sensitive to the common characteristics and problems of diverse payments media, essential principles should be identified and utilized to preserve real choice for transactors. P.E.B. Draft No. 3 of the UNPC alternately succeeds (in the stop payment element of section 200) and fails (in the reversal provision of section 425) to formulate and utilize the correct essential principles. The argument here has suggested that, inasmuch as transactors are almost always more comfortable with the familiar, the addition of a credit component to a payments device should determine the provision of a right to reverse.

The 3-4-8 Committee of the Permanent Editorial Board of the Uniform Commercial Code may be expected to offer a fourth draft of the UNPC. Current credit card law suggests that a right to reverse is both commercially desirable and practical. This Article has urged that the right be maintained in future drafts of the UNPC but limited to the

173. *See* 1978 Report, *supra* note 15, at 35-38. A "natural monopoly" results where one business of efficient size can produce all or more than the market can absorb at a remunerative price. *Id.*; *see* Ovitron Corp. v. General Motors Corp., 295 F.Supp. 373, 377 (S.D.N.Y. 1969).

174. 1978 Report, *supra* note 15, at 46.

175. *Id.* at 45-46.

credit context. It is hoped that the architects of uniform and codified payments legislation will consider the jurisprudential arguments offered here in preparing the black-letter law of the next draft.