

community BANKER

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Welcome to the November/December issue of the COMMUNITY BANKERS' ADVISOR.

The ADVISOR is prepared by attorneys at Olson & Burns P.C. to provide information pertaining to legal developments affecting the field of banking. In order to accomplish this objective, we welcome any comments our readers have regarding the content and format of this publication. Please address your comments to:

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The attorneys at Olson & Burns represent a wide range of clients in the financial and commercial areas. Our attorneys represent more than 30 banks throughout North Dakota.

YOU ARE ASKING

Q: What sort of tips can we give our tellers for reviewing IDs? We have caught a few fakes in the past few months and wonder if we might have missed others.

A: The P.L.E.A.S.E. reminder is one that comes to mind. Tellers can use this memory aid to remember to review IDs:

- P- Picture - compare this to the individual presenting the ID;
- L- Logos/holograms present on the ID?;
- E- Expiration date? An expired ID means it is not a valid ID;
- A- Age - compare the date of birth with the apparent age of the individual;
- S- Signature - compare the signature on the ID to the signature on the item presented;
- E- Evidence of tampering? Look at it closely to see if there are any alterations.

Also, North Dakota licenses and identification cards have these anti-counterfeiting measures:

- a "ghost image" of the holder on the bottom of the card;
- the state seal overlapping the portrait; and
- a transparent hologram with alternating images of a meadowlark and a prairie rose. Go to <http://www.dot.nd.gov/divisions/driverslicense/dlnewlicense.htm> to see images of the new drivers licenses and non-drivers identification cards.



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Q: Our customer has an existing, long-time business account in her (first) married name, opened under her social security number; she was divorced about three years ago. She recently remarried, and now she wants to open a personal account under her new married name and with her social security number. Our policy is that there will be only one customer file for a social security number, not different accounts with different names but the same social security number. She's not interested in changing the name on her business account. Thoughts?

A: Your policy is correct. First, determine what her legal name actually is. All accounts should be styled using her legal name, and you should have one customer record. You can point out that the Patriot Act/Bank Secrecy Act require *legal* names on bank accounts, and once you determine what her legal name is, that's the name on the account.

A Run-Down on Forged Maker Checks

Along with the good comes the bad, and we have heard of the bad from many banks. Forged maker checks now rank near or at the top of the bad things North Dakota banks have to deal with. As a general rule, a customer is not liable for a check drawn on his account if he didn't sign the check or benefit from its proceeds - without a customer's authorized signature, the check is not considered to be "properly payable." Also, as between the maker's bank and the depository bank (or any collecting bank), the maker's bank is usually liable for a forged maker signature.

However, there are exceptions to the general rule that "A CUSTOMER IS NOT LIABLE FOR A CHECK DRAWN ON HIS ACCOUNT IF HE DIDN'T SIGN THE CHECK OR BENEFIT FROM ITS PROCEEDS." Under North Dakota law, a customer is liable for a forgery if the customer "ratifies" the transaction.

N.D.C.C. § 41-03-40(1). "*Ratification*" is an after-the-fact adoption of the unauthorized signature by the person whose name is forged and may be found from conduct. For example, the customer may decide not to report the forgery, may decide to retain the benefits of the transaction, or may make explicit statements such as "I will not make a claim against the bank because the forger was my granddaughter." A customer is also liable for a forgery if the customer is "*precluded*" or prevented from denying it. A customer may be precluded from asserting the forgery if his negligence contributed to the forgery. N.D.C.C. § 41-03-43. The customer may also be precluded from asserting the forgery if the customer fails to review the bank statements and returned checks with reasonable promptness and report the forgery in a timely fashion. N.D.C.C. § 41-04-37.

A bank is also not liable for paying a forged check if its customer is precluded from making a claim for reasons such as the customer deliberately fails to report the forgery, asks the bank not to report the forgery to the authorities, or enters into a direct settlement with the forger. In figuring out whether a ratification took place, the bank should consider: (1) Did the customer accept the benefits of the transaction? (2) Did the customer enter into a settlement agreement with the forger? (3) Did the customer previously allow the forger, who was not an authorized signer, to complete incomplete checks or write checks on occasion? (4) Did the customer intentionally fail to report the forgery to the bank for any period of time? (5) Did the customer ask the bank not to file a report with the police or to not attempt to seek restitution from the forger?

A customer has a duty to promptly examine account statements and returned checks, and to notify the bank of any unauthorized signatures. N.D.C.C. § 41-04-37(3). A customer is liable for unauthorized signatures (or alterations) by the same wrongdoer if the customer fails to discover or report the problem to the bank within a reasonable time, not exceeding 30 days, or any shorter period agreed to in the customer's deposit agreement, following the mailing of the first statement or check reflecting the forgery (or alteration). N.D.C.C. § 41-04-37(4)(b) and

N.D.C.C. § 41-04-03(1).

To determine whether the customer failed to examine statements and report the forgery, consider: (1) When did the first forgery occur and when was the first statement sent that included a forged item? (2) Were there forgeries on any other accounts that happened before the forgery claimed by the customer? Don't assume the customer has notified the bank of the earliest forgery, which could hinder the customer's claim on later checks. (3) Were there other unauthorized transactions involving credit cards, lines of credit, or wire transfers that should have put the customer on notice? (4) Did the customer also have electronic access to the information reflecting the fraud through online systems, telephone banking, etc.? (5) Did the customer check the account balance at an ATM, and should that have put the customer on notice of the problem? (6) Was the customer on notice of the problem because of his receipt of statements from other institutions that reflected similar forgeries or alterations? (7) Were the checks reported out-of-sequence on the account statement? (8) Did the customer maintain a check register? Ask to see it. (9) When should the customer have noticed the forgery? The rule allows up to 30 days, but it may be shorter depending on the circumstances.

If the customer can show that the bank failed to exercise ordinary care, defined at N.D.C.C. § 41-03-03(1)(g) as "observance of reasonable commercial standards prevailing in the area", in paying the item and that the failure contributed to the loss, the loss is allocated between the customer and the bank according to the extent to which each contributed to the loss. N.D.C.C. § 41-04-37(5). If the customer can show that the bank did *not* pay the item in good faith, the customer is *not* precluded from asserting the forgeries by his failure to act in a timely manner. N.D.C.C. § 41-04-37(5).

If the customer's failure to exercise ordinary care substantially contributed to the making of the forged signature, the customer is precluded from

asserting the forgery against the bank, except to the extent that the bank's failure to exercise ordinary care contributed to the loss. When both the customer and the bank fail to exercise ordinary care, the loss is allocated between them according to the extent to which the failure of each to exercise ordinary care contributed to the loss. N.D.C.C. § 41-03-43. The bank should consider: (1) How did the forger get his hands on the checks? (2) What security procedures did the customer follow in storing the checks? If it is a business customer, does it have written procedures, and were they followed? (3) Did the customer discover or report the loss of any blank checks? (4) Did the customer submit a declaration of loss? (5) Has the customer previously had unauthorized transactions regarding its accounts which should have caused him to exercise greater care? (6) Did the customer report the loss in a timely fashion? (7) How long did the forgeries go on? (8) Should the forgeries have been noticed due to the amounts in question? (9) Do the forged signatures resemble the customer's signature? (10) Did the customer actually review statements and/or canceled checks? (11) Did the customer maintain a check register? Ask to see it. (12) Should the customer have noticed the forgeries based on the names of the payees? (13) Were vendors complaining about unpaid bills? (14) Did the customer ignore reports that reflected unauthorized activity, such as ATM balance inquiries?

If it was a dishonest bookkeeper: (1) Did the customer follow careless office procedures? (2) Did the customer separate the check writing and statement review duties? (3) Did the customer adopt and follow audit procedures? (4) Was the customer careless in handling facsimile signature stamps or devices? (5) Did the customer fail to do a background check of the employee or check references, or did he knowingly hire an untrustworthy employee, such as one with a criminal record for financial crimes or theft, and then provide access to checks? (6) Has the customer filed a police report? (7) Did the customer fail to take preventative action after learning of a forgery or alteration, such as conducting an investigation and suspending the employee in question? (8) Did the customer follow

any fraud prevention recommendations made by the bank?

Without regard to care or lack of care by the customer or the bank, a customer who does not discover and report forgeries within one-year (or a shorter period as set out in the customer's account agreement) after the statement or items were made available to him, is precluded from asserting the unauthorized signatures and alterations. N.D.C.C. § 41-04-37(6). Remember that the bank may shorten this one-year period by agreement with its customer - step number one is always check the account agreement! N.D.C.C. § 41-04-03(1); Douglas Companies, Inc. v. Commercial Nat. Bank of Texarkana, 419 F.3d 812 (8th Cir. 2005) (noting that U.C.C. § 4-406 requires a customer to inform a bank within one year after the statement of an unauthorized signature, but that the time limit "for notifying a bank may be, and frequently is, altered by agreement of the parties.")

Finally, know that there is potential bank liability not only for reimbursing the customer's account for the forged check (if that's what the facts show should happen), but banks should be aware that

if the payment of a forged check causes *legitimate* checks to be returned, the bank may be liable for damages proximately caused by that "wrongful dishonor." See N.D.C.C. § 41-04-33. If the forgery is a large amount and its possible that later checks might bounce because that check was paid, think about closing an account that has had forged maker checks. This is not only to prevent processing of additional forged checks, but to prevent the future dishonor of other checks pending the bank's review and possible reimbursement of the account. Review the account agreement (always the first step), contact your customer, notify him or her of the imminent closure, and advise the customer to stop issuing checks against the account. Do not do this without sufficient advance notice, however - sufficient advance notice is necessary if the customer receives electronic deposits of social security or if the customer participates in cash management services such as contract collection or lockbox where an immediate termination might harm the customer.

The above discussion is a very general overview of the law. As is usually the case, it's important to keep in mind that the final answer depends entirely *on the specific facts* in each forged maker case.

DISCLAIMER

COMMUNITY BANKERS' ADVISOR is designed to share ideas and developments related to the field of banking. It is not intended as legal advice and nothing in the COMMUNITY BANKERS' ADVISOR should be relied upon as legal advice in any particular matter. If legal advice or other expert assistance is needed, the services of competent, professional counsel should be sought.