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Negotiable Instruments--Misapplication of Funds by Use of Checks--Recovery from Payee

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perpetually restraining the defendant from the use, as part of its corporate name, the words constituting the plaintiffs' trade-name.

"With the attention of legislatures throughout the country focused upon emergency measures necessitated by current economic and financial conditions, it is not surprising that but few statutes were passed dealing with unfair competition." [15] However, the numerous recent decisions indicate that the day has passed when developments in this field await the process of change in the judicial concepts of fair trade.

BEATRICE R. RAPOPORT.

NEGOTIABLE INSTRUMENTS—MISAPPLICATION OF FUNDS BY USE OF CHECKS—RECOVERY FROM PAYEE.

The courts of this state have adopted certain rules to protect corporations and trusts from misapplication of funds by persons authorized to issue checks of such corporation or trust. The general rule of law on this subject is that even when the officer has authority to issue checks, a person who receives a check drawn on the funds of the corporation or trust, to satisfy a debt of the officer, is put on notice to inquire if his authority extends to such use of the corporation or trust funds. This question has generally come before the courts in cases where the officer has deposited in his own account a check drawn by him on the corporation or used the check to reimburse the bank for a personal obligation. Another variation is where the officer has used a corporation check drawn by himself to reimburse a debtor.[1]

In *Aneless Corporation* v. *Albert E. Woodward*,[2] an officer of the plaintiff was indebted to the defendant and, in order to discharge this obligation, issued a check of the plaintiff to the order of defendant. He then deposited the check in a bank in the name of defendant, having endorsed it "for deposit to the account of" defendant and signed the name of the corporation and his own as treasurer. He then delivered the duplicate deposit slip to defendant, who was thereby enabled to obtain the funds from the collecting bank. The plaintiff sought to recover the funds so acquired by the defendant. The Court of Appeals *held* "that we cannot hold that the actual facts, one of the essentials being unknown to the principal and the other unknown to the agent, can be so combined as to impute to the principal knowledge of the whole transaction."

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[15] (1933) 46 HARV. L. REV. 1194.

[1] Cohnfeld v. Tanenbaum, 176 N. Y. 126 (1903).

[2] Aneless Corporation v. Woodward, 262 N. Y. 326, 186 N. E. 800 (1933).

In dealing with agents a person is bound by the extent of authority actually granted to the agent and any apparent authority which he might have.[3] A person may accept a check of a corporation signed by its authorized agent subject to facts of which he has notice either actual or which is apparent from the face of the check. In this case the check was drawn by the treasurer, who had authority to draw checks for corporate purposes, and was certified by the bank so that the check was apparently issued for corporate purposes. The indorsement upon the check was ostensibly an instruction to the receiving bank, by the corporation acting through its agent, to receive the deposit for the account of defendant. The receiving bank acted as agent in a restricted capacity, namely, to collect the funds and place them at the disposal of defendant.[4] Only actual knowledge on the part of the agent would be imputed to the principal, although constructive knowledge might be imputed to principal if agency had been of a more general nature.

The treasurer in this case abused his authority in issuing such a check, inasmuch as it was not for corporate purposes. However, this was a latent defect as there was nothing about the instrument to put the collecting bank on notice. A question, however, might be raised as to the effect of the endorsement which the treasurer made for the purpose of depositing the check to the credit of defendant. There is no evidence that the corporation gave such power to the treasurer. In *Wen Kroy Realty Co., Inc.* v. *The Public National Bank & Trust Company of N. Y.*,[5] the plaintiff was allowed to recover when two signatures appeared upon a check, the signature of one person having authority to sign the check while the other signature was that of a person who was not connected with the corporation. The Court, holding that the officer did not represent that he was acting under the authority granted, namely, that he was empowered to issue checks of the corporation by his signature alone. If in that case the corporation can recover because one of the persons whose signature appeared on the check was not authorized, it would seem logical to assume that a corporation should not be bound by an act of an agent outside of the scope of his agency when the acts of the agent were not even apparently within the scope of his authorized agency.

The rule laid down in *Aneless Corporation* v. *Woodward*[6] is probably more satisfactory than that in the *Wen Kroy Realty* case, from a practical viewpoint. As business is now transacted and in view of the large volume of instruments handled by the financial institutions, it does not seem feasible to impute notice to them from instruments which contain defects of a very latent character. There are other cases which have followed the same rule, where a third

[3] McGoldrick v. Willets, 52 N. Y. 612 (1873).
[4] NEGOTIABLE INSTRUMENTS LAW, §350-c.
[5] 260 N. Y. 84, 183 N. E. 93 (1932); Note (1933) 7 ST. JOHN'S L. REV. 293.
[6] *Supra* note 2.

party has obtained a check from a person who has misused checks of a corporation by depositing them in an account and then issuing checks against such deposits.[7]

In the *Nassau Bank* v. *National Bank of Newbury, et al.*,[8] one G. B. Taylor drew checks against an estate account carried by the defendant bank. Subsequently, G. B. Taylor forged a draft on a New York City bank, the proceeds of which he deposited with plaintiff. He then drew a check against the deposit to reimburse the trust fund which he had previously depleted. The bank on which the forged draft was drawn recovered from plaintiff in another action and plaintiff seeks to recover the amount that was deposited to the credit of the estate account with defendant. The Court of Appeals decided in favor of defendant and set forth the following rule: "When money has been received by a person in good faith in the usual course of business and for a valuable consideration, it cannot be pursued into his hands by one from whom it has been obtained through the fraud of a third person."

In Michigan a similar rule is followed. In *McIntosh* v. *Detroit Savings Bank*,[9] a member of a partnership endorsed partnership checks and received cash for them from the defendant bank. He then proceeded to convert the funds to his own use and recovery against the bank was not allowed because the transactions were in the regular course of business and the bank had no notice of any diversions made by the partner securing the funds.

These cases support the general rule that where a person has misappropriated funds they cannot be followed into the hands of an innocent third party who obtains such funds. To be thus protected the party must not have any knowledge of the fraudulent source of the funds. If he receives a check which has been erroneously drawn by his creditor he will be held liable because the courts have held that in such cases although the creditor may not have knowledge of any fraud he is put on notice as to whether or not the debtor has authority to draw checks of the corporation for the purpose it is being used.

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[7] Justti v. The National Bank of the Commonwealth, 56 N. Y. 478 (1874); Stephens v. The Board of Education of the City of Brooklyn, 79 N. Y. 183 (1879); Southwick v. The First National Bank of Memphis, 84 N. Y. 434 (1881); Newhall v. Wyatt, 139 N. Y. 452, 34 N. E. 1045 (1893); Nassau Bank v. National Bank of Newbury, 159 N. Y. 456, 54 N. E. 66 (1899).

[8] *Supra* note 7.

[9] 247 Mich. 10, 225 N. W. 628 (1929).