

## Indorsement of Corporate Checks by Corporate Officers

Henry J. Plitkin

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## INDORSEMENT OF CORPORATE CHECKS BY CORPORATE OFFICERS.

The courts of this state have generally held, where an officer or agent of a corporation transferred by indorsement checks payable to the corporation to his individual bank account, that the bank receiving the deposit was liable to the true owner.<sup>1</sup> These decisions are grounded on the fact that the form of the check was notice to the bank that the officer or agent contemplated diversion of the corporate property to his own use, thus placing upon the bank the duty of making inquiry so as to ascertain the extent of the agent's authority. In a recent New York case, a check was diverted into the account of another corporation of which the endorsing officer was also the president and the question there raised was whether such facts sufficiently warned the bank of an impending diversion so as to render it liable for failure to make due inquiry.<sup>2</sup>

In *Wen Kroy Realty Co., Inc. v. The Public National Bank and Trust Company of N. Y.*, the plaintiff corporation had entrusted its president with the general management of its business. He indorsed a check payable to it in its corporate name, placed his own signature beneath as president and procured his son to sign as secretary. In fact, his son was not and never had been secretary of the plaintiff corporation. This check he then indorsed in the name of the Silvo Amusement Corp. of which he was also the president and deposited it in this corporation's account with the defendant bank. It was collected by the defendant through the regular channels. Silverman, the president, withdrew the funds through the Amusement Company's account and appropriated the avails to his own use. The plaintiff sought to hold the defendant liable for the conversion of the check, and was permitted to recover. The Court held that "the defendant bank receiving a check purporting to be indorsed by two officers could not have relied upon an apparent power of the president which the president did not represent that he was exercising."<sup>3</sup>

"The president of a business corporation has prima facie authority to do any act in the ordinary conduct of the business which the board of directors could have authorized him to do, where the persons with whom he deals have no knowledge of an actual lack of authority, and no sufficient reason for doubt."<sup>4</sup> This rule pre-

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<sup>1</sup> *Wagner Trading Co. v. Battery Park Nat. Bank*, 228 N. Y. 37, 126 N. E. 347 (1920); *Weissman v. Banque de Bruxelles*, 254 N. Y. 495, 173 N. E. 837 (1930); *Moch Co. v. Security Bank*, 176 App. Div. 842, 163 N. Y. Supp. 277 (1st Dept. 1917); *Buckley v. Lincoln Trust Co.*, 72 Misc. 218, 131 N. Y. Supp. 105 (1911).

<sup>2</sup> *Wen Kroy Realty Co., Inc. v. The Public National Bank and Trust Company of New York*, 260 N. Y. 84, 183 N. E. 93 (1932).

<sup>3</sup> *Ibid.* at 92, N. E. at 76.

<sup>4</sup> *ELLIOT, PRIVATE CORPORATIONS* (5th ed.) §529A; *ROSBROOK, NEW YORK CORPORATIONS* §417; *Hardin v. Lithographic Co.*, 247 N. Y. 332, 160 N. E. 388 (1928).

supposes that the agent is acting in the interest of his employer and the scope of the authority may not be enlarged by implication to justify the diversion to the agent himself of the principal's property.<sup>5</sup> Thus, the right to indorse corporate paper is limited to indorsement for corporate purposes.<sup>6</sup> But if the officers or agents of the corporation have authority to transfer corporate paper by the form of indorsement used, such indorsement by such officers or agents transfers the title of the corporation to the paper, even though the transfer is not made in furtherance of corporate purposes.<sup>7</sup> So, an officer or agent of a corporation authorized to indorse corporate paper in blank although only for the purposes of deposit in the corporation's bank account, can pass good title to such paper to a bona fide purchaser;<sup>8</sup> but where the authority was restricted to indorsing for deposit only, an indorsement in blank constituted a forgery so that no title could pass thereby.<sup>9</sup> It is clear then that where no actual authority exists the attempted transfer constitutes a conversion and no title will pass unless the transferee is entitled to rely upon the apparent authority of the agent.<sup>10</sup>

It has been held that the payee of corporate checks who receives them from the treasurer of the corporation in payment of the officer's individual debt is chargeable with notice of the agent's incapacity to issue them and is bound to inquire as to the real situation.<sup>11</sup> So, too, where the president of a corporation procured a check payable to its order, and having endorsed it in the corporate name, by himself as president, delivered it to the defendant in payment of a personal loan, the Court held the defendant liable on the

<sup>5</sup> *Porges v. United States Mtge. and Trust Co.*, 203 N. Y. 181, 96 N. E. 424 (1911).

<sup>6</sup> *Wagner Trading Co. v. Battery Park Natl. Bank*, *supra* note 1.

<sup>7</sup> *Salen v. Bank of New York*, 110 App. Div. 636, 97 N. Y. Supp. 361 (1st Dept. 1906); *Cluett v. Couture*, 140 App. Div. 830, 125 N. Y. Supp. 813 (3d Dept. 1910); *McCabe v. Chelsea Exchange Bank*, 183 App. Div. 441, 170 N. Y. Supp. 759 (1st Dept. 1918).

<sup>8</sup> *Cluett v. Couture*, *ibid.*

<sup>9</sup> *Standard S. S. Co. v. Corn Exchange Bank*, 220 N. Y. 478, 116 N. E. 386 (1917); Judge Pound states the rule to be, at 481, N. E. at 387:

"Any person taking checks made payable to a corporation which can act only by agents, does so at his peril and must abide by the consequences if the agent who indorses the same is without authority, unless the corporation is negligent or is otherwise precluded by its conduct from setting up such lack of authority in the agent.

"If the original indorsement was authorized, the diversion of the funds after indorsement would not make it a forgery; but if the original indorsement was unauthorized, parties dealing with the wrongdoer and innocent parties alike were bound to know the lack of the agent's authority to convey title away from the true owner to anyone."

<sup>10</sup> *Wagner Trading Co. v. Battery Park National Bank*, *supra* note 1.

<sup>11</sup> *Rochester R. R. v. Paviour*, 164 N. Y. 281, 58 N. E. 114 (1900); the Court said at page 285, N. E. at 115: "There was a shadow on the checks, and the defendant could not, in good faith, accept them until it disappeared."

theory that the presumption arising from the face of the check was that it belonged to the corporation and that its president had no right to use it to pay his personal debt.<sup>12</sup>

The deposit of a corporate check in the personal account of the indorsing officer has been held, from the very nature of the transaction, to be notice to the bank of an unwarranted diversion.<sup>13</sup> Based on this rule was the result reached in a case where a check entrusted by a corporation to its treasurer for deposit was cashed for the treasurer, the bank being rendered liable on the theory that one who accepts checks payable to a corporation does so at his peril and must abide by the consequences if the agent who indorses the same is without authority.<sup>14</sup> Where the deposit has been to the indorsing officer's personal account, other jurisdictions have generally held the bank liable on the theory that the form of the check was notice sufficient to put it on guard or that its act in receiving the check amounted to negligence.<sup>15</sup>

It is apparent that in all the cases discussed, the transferee had constructive notice, at least, at the time of the transfer, that the agent purporting to act on his principal's behalf or with his authority, was himself an interested party. This follows from the nature of the transaction itself, as where the check is received in payment of or as security for a personal debt, or to deposit in a personal account. But where the check is deposited in the account of another corporation of which the indorsing officer is an interested member, the dual interest of the officer does not appear on the check itself, and extrinsic circumstances must be proven to show the bank had notice. In *Niagara Woolen Co. v. Pacific Bank*,<sup>16</sup> two corporations were involved. But in this case some ninety-odd checks were diverted, not a single, isolated transaction as in the *Wen Kroy* case. Moreover, the name of the corporation in whose account the checks were deposited was that of the indorsing officer. These were the grounds upon which Justice McLaughlin concurred, while two

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<sup>12</sup> *Ward v. City Trust Co.*, 192 N. Y. 61, 84 N. E. 585 (1908).

<sup>13</sup> *Moch Co. v. Security Bank*, *supra* note 1.

<sup>14</sup> *Staten Island Lodge v. Staten Island Savings Bank*, 223 App. Div. 859, 228 N. Y. Supp. 859 (2d Dept. 1928); but where a check made payable to cash is presented by an officer of a corporation authorized to sign checks for such corporation, to a bank for payment in cash, a bank has no means of knowing from a mere inspection of the check that the proceeds are going to be subjected to larceny or conversion by the one presenting the check for payment—*Broadway Boxing Club, Inc. v. Bushwick National Bank*, 127 Misc. 515, 216 N. Y. Supp. 713 (1926).

<sup>15</sup> *Toronto Club v. Imperial Trust Co. of Canada*, 25 Ont. L. R. 330 (1911); *Underwood, Ltd. v. Bank of Liverpool*, 1 K. B. 775 (1924); *Dennis Metal Mfg. Co. v. Fidelity Union Trust Co.*, 99 N. J. L. 365, 123 Atl. 614 (1924); *McIntosh v. Detroit Savings Bank*, 247 Mich. 10, 225 N. W. 628 (1929); *cf. Parker Gordon Cigar Co. v. Liberty National Bank*, 134 Okla. 286, 273 Pac. 269 (1928).

<sup>16</sup> 141 App. Div. 265, 126 N. Y. Supp. 890 (1st Dept. 1910).

judges dissented entirely.<sup>17</sup> It will thus be seen that although the bank was held liable, the majority of the court did not assent to the proposition that the mere form of the check was sufficient to put the bank on inquiry, but on the contrary, expressly negated such a view. In *Bank of Benson v. Gordon*,<sup>18</sup> two corporations were also involved. A note payable to one corporation was left as collateral security for a loan to another corporation. Here the bank, however, had actual knowledge through its cashier that the officer who indorsed the note to the bank was the president and principal stockholder of both corporations, and that he was using the property of one corporation to secure the debt of another.

On the other hand, other jurisdictions have not subjected subsequent takers to the duty of making inquiry under such circumstances. It has been held where a note was drawn by one firm and indorsed by a member thereof to another firm of which the indorsing officer was also a member, that subsequent holders of the note did not take with notice of any contemplated diversion or defect in the title thereto.<sup>19</sup> It has also been held where an officer of a corporation indorses corporate papers to a partnership of which he is a member, that subsequent takers did not have sufficient notice of any diversion of corporate property to impose liability upon them.<sup>20</sup> In a case decided in our own state it was held that the blank indorsements of corporate officers following their official signature upon a check payable to the corporation and which was thereafter diverted into the account of a third person, did not constitute notice to the bank receiving the check.<sup>21</sup> Judge Page affirming the decision said,<sup>22</sup> "The mere fact that the check bore the personal indorsement of the officers of the corporation did not show an appropriation of the proceeds thereof to their own personal use, nor was that fact alone sufficient to put the defendant upon inquiry and charge it with knowledge of any fact such inquiry would have disclosed."

The Court in the *Wen Kroy* case has in effect gone further than the prevailing rule. The decision as a practical matter places

<sup>17</sup> *Ibid.* at 271, N. Y. Supp. at 894, the dissent went upon the ground that, "in all the cases relied upon to sustain the rule which it is proposed to apply in this case, there has been present the important fact, which is absent here, that the bank or individual to whom the diverted money was paid received it in payment of a debt, or in some other way reaped a benefit from the payment, thus becoming with notice, an active participant in the diversion. Where that fact has been absent, as for instance in a case like the present, where the bank was a mere conduit or collecting agency, asserting no title to or right to retain the money for its own advantage, a different rule has uniformly been adopted."

<sup>18</sup> 103 Neb. 508, 172 N. W. 367 (1919).

<sup>19</sup> *Miller v. Consolidation Bank*, 48 Pa. 514 (1865); *Walker v. Trenholm and McKee*, 14 S. C. 142 (1880).

<sup>20</sup> *In re Troy and Cohoes Shirt Co.*, 136 Fed. 420, *aff'd*, 142 Fed. 1038 (C. C. A. 2d, 1906).

<sup>21</sup> *Lasker v. Mutual Bank of Roseville*, 194 N. Y. Supp. 379, *aff'd*, 201 App. Div. 333, 194 N. Y. Supp. 381 (1st Dept. 1922), *aff'd*, 234 N. Y. 550, 138 N. E. 442 (1922).

<sup>22</sup> *Ibid.* at 334, N. Y. Supp. at 382.

upon banks the duty of analyzing every check offered for deposit by a corporation, and investigating the purposes of the indorsements thereon. This we submit is placing too heavy a burden upon banks for what in most instances amounts to negligence and laxity upon the part of corporate officers and stockholders. The decision is moreover not in keeping with recent expressions of our courts.<sup>23</sup> The tendency has been to narrow the limits of liability of banks for fraudulent acts of trustees and agents in dealing with their principal's property. The Court does not appear to have given due heed to these warnings nor is the result reached conducive of practical law.

HENRY J. PLITKIN.

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#### MORTGAGES—RECEIVERS—RENTS AND PROFITS.

The mortgagor is entitled to the rents and profits of the mortgaged premises after the institution of foreclosure proceedings and pending a sale therein.<sup>1</sup> This right is consistent with the equitable theory of mortgages adopted in this state<sup>2</sup> and the abolition by statute of the mortgagee's right to maintain ejectment upon the mortgagor's default.<sup>3</sup> There are, however, limitations to this right; for, having acquired jurisdiction over the property the court may appoint a receiver thereof to collect the rents and profits, and hold them for application on account of the debt, in the event of a deficiency.<sup>4</sup> Provision has been made for such appointment, by the legislature in specified instances,<sup>5</sup> but the courts of equity have long exercised the power independent of the provisions, and are not limited in its exercise to the cases there enumerated.<sup>6</sup> The intervention of equity to relieve from forfeiture, resulting in the drastic changes in the law of mortgages, was not designed to secure continued use of the property and drain of the profits, to the default-

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<sup>23</sup> Whiting v. Hudson Trust Co., 234 N. Y. 394, 138 N. E. 33 (1923); Empire Trust Co. v. Cahan, 274 U. S. 473, 47 Sup. Ct. 661 (1927).

<sup>1</sup> Syracuse City Bank v. Tallman, 31 Barb. Ch. 201 (N. Y. 1857); Whalen v. White, 25 N. Y. 462 (1862); Rider v. Bagley, 84 N. Y. 461, 465 (1881); Wyckhoff v. Scofield, 98 N. Y. 475 (1885).

<sup>2</sup> Trimm v. Marsh, 54 N. Y. 599 (1874); Howell v. Leavitt, 95 N. Y. 617 (1884); Barson v. Mulligan, 191 N. Y. 306, 84 N. E. 75 (1908); Becker v. McCrea, 193 N. Y. 423, 86 N. E. 463 (1908).

<sup>3</sup> N. Y. C. P. A. §991.

<sup>4</sup> See cases *infra* note 7; as to application of rents, Syracuse City Bank v. Tallman, *supra* note 1; Cincinnati Nat. Bank v. Tilden, 22 N. Y. Supp. 11, *aff'd*, 140 N. Y. 620, 35 N. E. 891 (1893); Continental Ins. Co. v. Reeve, 149 App. Div. 835, 134 N. Y. Supp. 78 (2d Dept. 1912).

<sup>5</sup> N. Y. C. P. A. §974 (adopted from §713 of N. Y. C. C. P. which is discussed in Hollenbeck v. Donnell, *infra* note 6).

<sup>6</sup> Hollenbeck v. Donnell, 94 N. Y. 342 (1884).