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Banks and Banking—Collection Items as Preferences.

Plaintiff drew a sight draft on C. The collecting bank accepted as payment a check from C, a depositor, on itself, and then forwarded to plaintiff its own draft on a St. Louis bank. Payment of the draft was refused because of the collecting bank's subsequent insolvency. *Held*, plaintiff had no preferred claim against the collecting bank,¹ although plaintiff had stipulated that the proceeds of the draft were to be treated as a trust² fund.³ The court declared that such stipulation did not contemplate that the collecting bank should hold the proceeds as a bailment and remit the specific funds collected; hence, on collection, a debtor-creditor relationship superseded the agency relationship of plaintiff and the collecting bank.⁴ Further, since the assets of the bank were not augmented, there were no funds to which a trust aspect could attach.

The possible efficacy of any stipulation attempting to impress a trust on the proceeds of a collection item seems to depend on the individual court's reasons for denying trusts in such proceeds generally. Trusts⁵ have been held to exist on the grounds of an intended agency relationship if the owner of the item is not a general

¹ *Allied Mills v. Horton*, 65 F. (2d) 708 (C. C. A. 7th, 1933).

² In this comment, and for that matter, in most cases in which it is sought to establish a preferred claim *in re* proceeds of a collection item, the word "trust" is used, although a "trust" in the usual sense of the word almost never exists. "Trust" under these circumstances is a label attached *after* the court has decided a preferred claim should exist rather than a means of determining whether a preference should be allowed. Thus "trust" as used in this comment merely means "grounds for a preferred claim." TOWNSEND, *Insolvent Banks and Collection Preferences: The Heaven of Psychophoros Revisited* (1932) 6 TULANE L. R. 643.

³ The specific statement is: "This draft a cash item and not to be treated as a deposit. The funds obtained through its collection are to be accounted for to us and are not to be commingled with the other funds of the collecting bank."

⁴ When the collecting bank remits by a draft on a third bank and such draft is refused payment because of the collecting bank's insolvency, some courts have held that the draft constitutes an equitable assignment of funds received in trust. Hence collection may be enforced against the third bank on the theory of a constructive trust. *Carson Nat. Bank v. American Nat. Bank*, 225 Mo. App. 64, 34 S. W. (2d) 143 (1930); *Central Trust Co. v. Bank of Mullens*, 108 W. Va. 12, 150 S. E. 137 (1929).

⁵ Only illustrative cases are cited below. For a collection and discussion of cases upholding and cases denying the existence of a trust in the proceeds of a collection item Townsend, *Constructive Trusts and Bank Collections* (1930) 39 YALE L. J. 980; (1896) 32 L. R. A. 715; (1912) 38 L. R. A. (N. S.) 146; (1917) L. R. A. (1917F) 603; (1923) 24 A. L. R. 1152; (1926) 42 A. L. R. 754; (1927) 47 A. L. R. 761; (1931) 73 A. L. R. 71; (1932) 77 A. L. R. 473.

depositor,⁶ if the owner instructs the bank "to collect only,"⁷ "to collect and notify,"⁸ "to collect and remit,"⁹ to treat as a trust;¹⁰ statutory regulations impose a trust in some jurisdictions.¹¹ The existence of a trust has been denied on the grounds that a debtor-creditor relationship arises after collection by virtue of an express agreement,¹² or because customary,¹³ or because the stipulation of the owner fails *in fact* to change the collecting bank's method of handling the proceeds,¹⁴ and on the grounds that the bank's assets

⁶ *Piano M'fg. Co. v. Auld*, 14 S. D. 512, 86 N. W. 21 (1901); *Skinner v. Porter*, 45 Idaho 530, 263 Pac. 993, (1928) (In the absence of reciprocal accounts, the only duty of the collecting bank is to remit; hence a trust in the proceeds of the collection item).

⁷ *State v. Bank of Commerce*, 61 Neb. 181, 85 N. W. 43 (1901).

⁸ *Guignon v. First Nat. Bank*, 22 Mont. 140, 55 Pac. 1051 (1899).

⁹ *Hall v. Beymer*, 22 Colo. App. 271, 125 Pac. 561 (1912); *Federal Reserve Bank v. Millsbaugh*, 275 S. W. 583 (Mo. App. 1926) (no reciprocal accounts); *Vermont Loan and Trust Co. v. First Nat. Bank*, 37 Wyo. 216, 260 Pac. 534 (1927).

¹⁰ That is, a more detailed and explicit stipulation than a mere "for collection and remittance" is attached to the draft. *First Nat. Bank of Raton v. Dennis*, 20 N. M. 96, 146, Pac. 948 (1915); *Kansas Flour Mills Co. v. New State Bank*, 124 Okla. 185, 256 Pac. 43 (1926) (same stipulation as in principal case, *supra* note 3); *cf. Peters Shoe Co. v. Murray*, *infra* note 20.

¹¹ OHIO CODE (Throckmorton, 1929) §713 applied in *Fulton v. R. Baker-Toledo Co.*, 125 Ohio St. 518, 182 N. E. 513 (1932); S. C. CODE ANN. (Michie, 1932) §6960 held to be constitutional in *Witt v. People's State Bank of S. C.*, 166 S. C. 1, 164 S. E. 309 (1932). Preferred claims would probably be allowed in the following states by virtue of statutes: IND. ACTS (1929) c. 164 §13; MD. CODE ANN. (Bagby, Supp. 1929) art. 11 §95; N. Y. CONSOL. LAWS (Cahill, 1930) c. 39 §350-1; WASH. REV. STAT. (Remington, 1932) §§3292-13; WIS. STAT. (1931) §§220-15.

¹² *Commonwealth v. State Bank of Pittsburg*, 216 Pa. 124, 64 Atl. 923 (1906).

¹³ This view is that while the collecting bank is the agent of the owner of the collection item until proceeds are collected, yet—inasmuch as the bank mingles the proceeds with its own funds as soon as collection is made and sends the owner a cashier's check or its own draft—the agency relationship ceases on collection and that of debtor and creditor arises. *Hecker-Jones-Jewel Mill. Co. v. Cosmopolitan Trust Co.*, 242 Mass. 181, 136 N. E. 333, (1922); *Gordon v. Rasines*, 5 Misc. 192, 25 N. Y. S. 767 (1893). This is held to be true even when the owner is not a depositor in, or has no reciprocal accounts with, the collecting bank for the reason that, as a matter of banking practice, the collecting bank does substitute an obligation of its own for the amount of the proceeds of the collection item rather than remit the specific funds collected, *infra* note 14.

¹⁴ The stipulation is made not in contemplation of any actual change in banking practices or methods, but solely with a view to obtaining a preference in the event of the collecting bank's insolvency. *Lippitt v. Thames Loan and Trust Co.*, 38 Conn. 185, 90 Atl. 369 (1914); *Union Nat. Bank v. Citizens Bank*, 153 Ind. 44, 54 N. E. 970 (1899) ("There was nothing in the transaction . . . which indicated that other than the usual course of dealing was expected by the forwarding bank.") *Leach v. Farmers and Merchants Savings Bank*, 207 Iowa 471, 220 N. W. 10 (1928).

are not augmented,¹⁵ or that, because of mingling, it is impossible to trace the funds.¹⁶

Therefore, if a forwarding bank wishes to have a preferred claim in the event of the collecting bank's insolvency, clearly a statement that only cash was to be collected, and remitted in specie, would certainly be effective,¹⁷ but such a method of remittance is obviously impractical. A use of such stipulation with the tacit understanding that it was only a safeguard, to be disregarded in practice, would probably be held to have no effect.¹⁸ Some state courts which regard the intention of the parties as controlling, and which ordinarily deny a preference, would probably permit even such a stipulation¹⁹ as in the principal case to constitute grounds for allowing a preference.²⁰ A statement accompanying the draft requiring segregation of the general funds of the bank, to the amount of the item, might by some state courts be held to be sufficient to entitle the forwarding bank to a preferred claim.²¹ But it is doubtful if such language

¹⁵ *Midland Nat. Bank v. Brightwell*, 148 Mo. 358, 49 S. W. 994 (1898); *Com. v. State Bank*, 216 Pa. 124, 64 Atl. 923 (1906); *Harnish, Moore and Porterfield v. Farmers and Merchants Bank*, 56 S. D. 18, 227 N. W. 375 (1929). This has been the principal reason assigned in a long line of federal decisions for refusing to concede a trust. *Amer. Can Co. v. Williams*, 178 Fed. 420 (C. C. A. 2d, 1910). *Larabee Flour Mills Co. v. First Nat. Bank*, 13 F. (2d) 30 (C. C. A. 8th, 1926) (Federal cases supporting this view cited therein by circuits); (1927) 36 *YALE L. J.* 682. Cases holding the opposite view meet the argument that there has been no augmentation of assets by declaring that it would be a useless procedure to cash the check and then return the cash, and that therefore payment by check is the same in its legal effect as payment in cash, *Kansas Flour Mills Co. v. New State Bank*, *supra* note 10; or by holding that in as much as a successful remittance of the proceeds would have decreased the assets of the bank, a retention of these proceeds, therefore, augmented its assets. *Hawaiian Pineapple Co. v. Browne*, 69 Mont. 140, 220 Pac. 1114 (1923).

¹⁶ *State ex rel. N. C. Corp. Com. v. Merchants and Farmers Bank*, 137 N. C. 697, 50 S. E. 308 (1905).

¹⁷ *Union Nat. Bank v. Citizens Bank*, *supra* note 14; *Hallam v. Tillinghast*, 19 Wash. 20, 52 Pac. 329 (1898).

¹⁸ Stipulations are ineffective if the parties do not *in fact* contemplate a change in the bank's method of handling such items, *supra* note 14. Clearly, however, the party stipulating collection in cash does intend just that, in as much as the legal effect of collection in cash would be to impress a trust on such funds since the bank's assets are augmented. But the federal courts ignore this.

¹⁹ *Supra* note 3.

²⁰ *Peters Shoe Co. v. Murray*, 31 Tex. Civ. App. 259, at 260, 71 S. W. 977, at 978 (1903).

²¹ *Hallam v. Tillinghast*, *supra* note 17 (suggests such would be effective).

would be regarded by the Federal Courts as having any effect, in as much as such procedure would hamper banking relations.²²

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Damages—Unauthorized Disclosure of Telegram as Basis of Punitive Damages.

The plaintiff sued for the wrongful disclosure of the contents of a telegram from his divorced wife. The disclosure was made to the plaintiff's fiancée by one of the defendant's employees who had erroneously concluded from the message that the plaintiff was still married. Although the fiancée then knew of the previous marriage and divorce, she immediately broke off the engagement. The plaintiff's recovery was limited to nominal damages. *Held*, a corporate employer is not liable for punitive damages without having participated in or ratified his servant's act.¹

In actions *ex delicto* where the tortious conduct was characterized by malice or wantonness, exemplary damages are discretionary with the jury.² As in the principal case, the wantonness may take the form of a reckless disregard for another's rights.³ Verdicts in excess of the plaintiff's actual loss are the exception rather than the rule.⁴

Concerning the liability of employers for exemplary damages, in most jurisdictions the practice prevails of limiting an individual employer's liability to those acts of his servant in which he has himself participated.⁵ Judicial opinion is rather evenly divided on the question of the liability of corporate-employers.⁶ The federal courts and

²² *Allied Mill v. Horton*, *supra* note 1, at 710. The court states with reference to the stipulation accompanying the draft, *supra* note 3: "If each time such a draft is collected the collecting bank under such notice is required to place the specific funds received in a safe deposit box or in a package for the drawer, the transaction of business through drafts . . . would be quite revolutionized."

¹ *Western Union Telegraph Co. v. Aldridge*, 66 F. (2d) 842 (C. C. A. 9th, 1933).

² *Lake Shore & Michigan Southern R. Co. v. Prentice*, 147 U. S. 101, 13 Sup. Ct. 261, 37 L. ed. 97 (1893). *Contra*: *Boott Mills Co. v. Boston & Maine R. Co.*, 218 Mass. 582, 106 N. E. 680 (1914) (Louisiana, Nevada, and Washington follow Massachusetts in rejecting the doctrine of exemplary damages completely).

³ *Lake Shore & Michigan Southern R. Co. v. Rosenzweig*, 113 Pa. 519, 6 Atl. 545 (1886).

⁴ *Cock v. Western Union Telegraph Co.*, 84 Miss. 380, 36 So. 392 (1904).

⁵ *Haines v. Schultz*, 50 N. J. L. 481, 14 Atl. 488 (1888).

⁶ *McCormick, The Doctrine of Exemplary Damages* (1930) 8 N. C. L. Rev. 129, 132.