

# Why Should a Legal Scholar Care About Bank Deposits?

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Nothing in this presentation is necessarily the opinion of the Federal Reserve Bank of New York or any other component of the Federal Reserve System.

# My Goal Today

- I want to sell you on opportunities in legal scholarship in bank deposits.
- This helps me in two ways:
  - Helps my statutory project on bank deposits.
    - Creates “buzz” to start and sustain the project
    - Creates more knowledgeable participants and better rules
  - Creates competition in the intellectual project.
    - Competition is better and faster than solitary work.
    - Academic scholars have many relevant intellectual tools that I do not have: *e.g.*, social theory, computer science.

# Why do we need a statute?

- Only major established field of business law to never have been codified or *Restatement*-ed.
  - Three centuries of contradictory case law to draw from.
  - Substantial interstate variation, *e.g.*:
    - Setoff against fiduciary accounts
    - Adverse claims statutes
    - Civil (CA, LA) v. common-law setoff
    - Claims on joint accounts
    - Creditor process (*e.g.*, is it only effective against balance at the time of service, or does it affect subsequent incoming payments?)
  - Has not been adjusted for computerization.
    - *E.g.*, creditor process name rules.
    - Notice inquiry
  - Not seriously examined since Great Depression bank insolvency cases.

# Why do we need a statute? (II)

- Modern courts are confused by it.
  - Musty old confusing common law.
    - Judicial discomfort with uncodified commercial law.
  - Asset forfeiture law.
    - Modern courts are quite familiar with this. Too familiar.
    - Asset forfeiture is at odds with much of commercial law.
- There is no satisfactory framework
  - Lack of *Restatement* or codification
  - Lack of scholarly interest
    - Resistance to economic analysis
- Wacky cases, *e.g.*:
  - Pioneer Commercial Funding Corp. v. American Financial Mortgage Corp., \_\_ Pa. \_\_, 855 A.2d 818 (2004), *rev'g* 2002 Pa. Super. 68, 797 A.2d 269, 47 U.C.C. Rep. Serv. 326 (2002)
  - Winter Storm Shipping, Ltd. v. TPI, 310 F.3d 263 (2d Cir. 2002)
  - Waelder Oil v. Southwestern Glass, 332 F.3d 513 (8th Cir. 2003)

# Why do we need a statute? (III)

- Weird sovereign risk rules.
  - Does anybody understand 12 USC § 633?
- A neglected--but potentially very useful--law of “special deposits.”
  - Paying agents on securities
  - Payment systems (CHIPS, CLS Bank)
  - Tri-party repos
  - Payroll and tax funding
  - Escrows
- A frustrating law of tracing.
- An impossible law of banks as fiduciary-depositories.
  - The *Restatement (Second) of Trusts* § 87 comm. b gets it right.
  - But the courts don't. Nor do agreement drafters.
- **SYSTEMIC RISK (and liquidity) CONCERNS**

# *Deposits as Symbols*

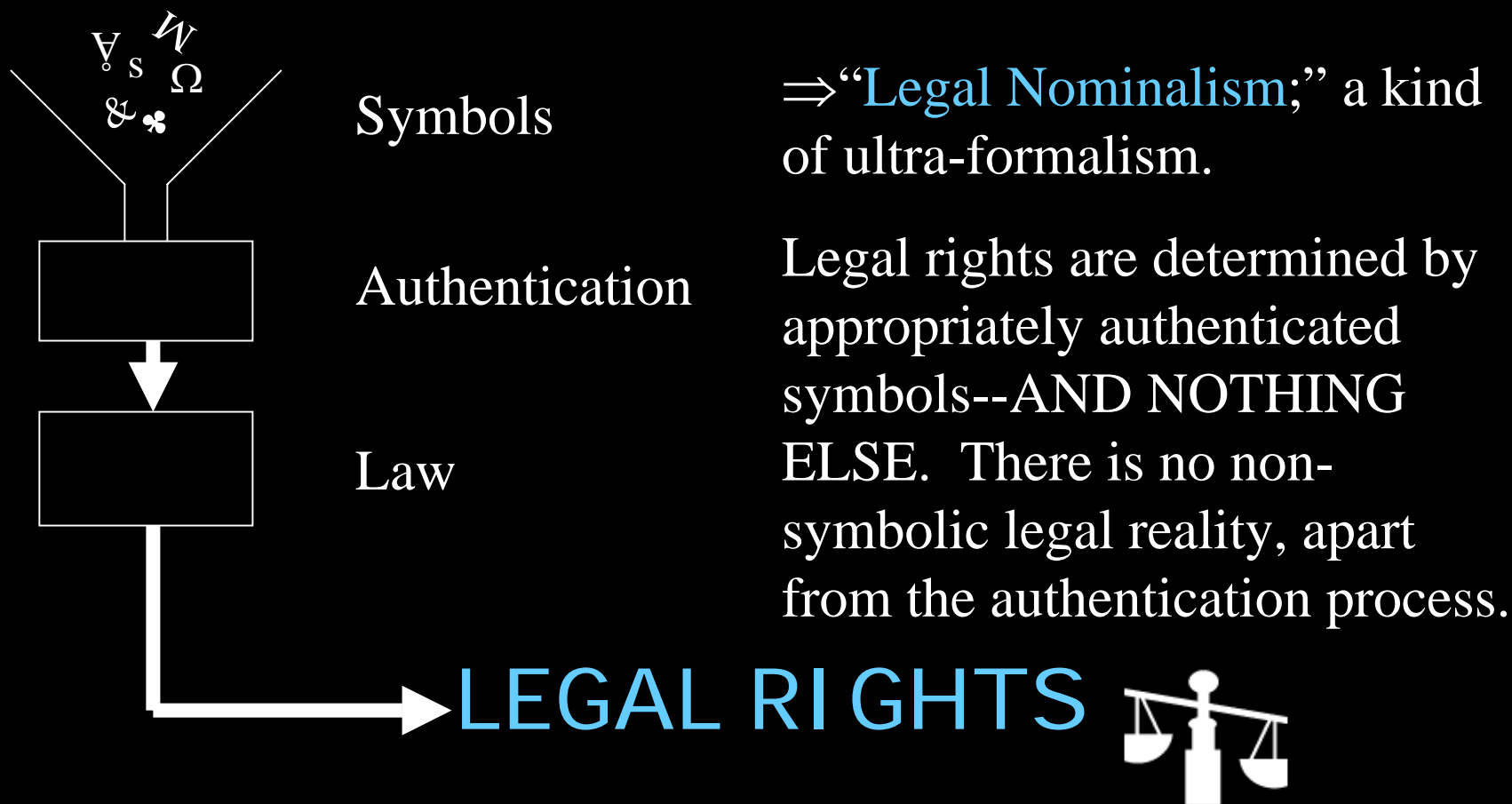
(Design Principles for a New Statute)

# Deposits as Symbols

- Bank deposits are species of bank debt; debt=contract.
- Bank deposits are a peculiar contract
  - They are nothing but talk
    - They are *created* by symbolic performance (*e.g.*, agreement or operation of payment system).
      - NB: The payment system is implemented on symbol-processing machinery: computers, check sorters, ATM machines, etc.
    - They are *discharged* only by symbolic acts of the payment system
      - Even tender of currency is a a symbolic performance
  - They are circular. Almost all other contracts refer to something other than themselves (*e.g.*, airline ticket)
    - But debt refers only to debt: turtles all the way down.
- => The law of bank deposits is a law of authenticated communications.

# HOLD THAT THOUGHT!

“The law of bank deposits is a law of authenticated communications.”



# This ain't nothing new

To fit [money] for its purpose, the stamp denotes its value, and possession alone must decide to whom it belongs.

Wookey v. Pole [1820] 4 B & Ald, 1, 106 E.R. 839, 841

## But nominalism is important

- Operational efficiency *and*
- The law of meaning.

# Symbols, Computers & Efficiency

- To the extent bank operations are computerized (or ministerial), the law *must* be nominalistic.
  - Computers only operate on and produce symbols.
  - Nominalistic payment law is a computer output device; computer states in; legal relations out.
- Computers can be very efficient, in the engineer's sense, if not the economist's.
  - Engineering efficiency is something normally outside the purview of a lawyer and left to clients.
    - Lawyers usually talk about efficient *incentives* created by legal rules, not efficient *processes* enabled by legal rules.
  - But lawyers are responsible for legal nominalism — feasible computer operations. A cyberlaw connection.
  - In other words, lawyers engineer intangibles. *Nominalism is a legal design criterion.*

# Meanings and Symbols

- *Subjective* meaning: classic copyright. My art can be your garbage.
- *Objective* meaning: First Amendment, TM.
  - Does this picture mean “obscenity”?
  - Does this creche mean “Godless kitsch”?
  - Does this mouse mean “Disney”?
- *Intersubjective* meaning: must evoke a shared response to be of any social use.
  - Money.
  - Red lights.
  - Subway tokens, hat check tickets, transferable claims of right, etc.

# Creating Intersubjective Meaning

- The strongest intersubjective meanings are the purely symbolic ones. *E.g.*,
  - Money BTW, Compare marriage (nominalistic) to common-law marriage.
  - “I am entitled to a right to \_\_\_\_\_ because I hold a ticket.”
  - “\_\_\_\_\_ has been elected President.”
- We view these meanings as “natural” and are not likely to question them.
- The social strength frays when the symbols are disputable.
  - *E.g.* Bush v. Gore, 531 U.S. 98 (2000).
- Strong authentication, conjoined to nominalistic legal rules, produces undisputable intersubjective meaning.
  - *Compare* Bush v. Gore, 531 U.S. 98 (2000) *with* your bank balance.

∴ Nominalistic legal rules (& good authentication) *must* underpin any legal system that creates strong intersubjective meaning. *E.g.*,

**Money (=> bank deposits)** *but also*

**Transferable rights (instruments, e-instruments)**

**Traffic lights**

**Voting**

**Creation and Termination of Marriage**

**A "fair" military draft?**

**Additional items "an exercise for readers"**

# Nominalistic Rules in Bank Deposits

- Conflicts of Law
- Security Interests (original collateral)
- Maturity requirement of setoff
- Knowledge exception to fiduciary law
- Creditor process rules
- Account segregation (unlike tracing, uncontroversial)
- Rules that strengthen bank communications systems
  - Account stated doctrine
  - Requirement of bank consent to security interests
  - Adverse claims statutes
  - Various rules exculpating bank from nonuse or misuse of its system:  
*e.g.*, UCC §§ 3-306, 4-406(c), 4A-203(a)(2), *Joachimson v. Swiss Bank Co.*, [1921] 3 K.B. 110 (C.A.) at 127.

# Exceptions to Nominalism

## Act requirement of setoff:

- NB: No act requirement in CA, LA, English running accounts, civil law.
- Rationale act requirement is uncertain; content can be tenuous.

## Tracing:

- Exception to exception: segregated accounts, which can be nominalistically defined.
- Many commercial law scholars diss tracing: *e.g.*, Markell: 74 Chi-Kent L. Rev. at 1016-17; Rogers, 12 Cardozo L. Rev. at 501; Oesterle, 68 Cornell L. Rev. at 185; 2 Gilmore at 735-36.

## Third-party claim to “funds”:

- Exceptions to exception: creditor process, adverse claim statutes; UCC 9 security interest in original collateral.
- “Conversion of funds” theories deny that deposit is a debt.
- Fiduciary ownership theories are often nominalistic *malgré lui*, because of knowledge requirement in majority rule.

## Acceleration and closeout netting(?):

- Depends on the default conditions and role of notice.
  - If conditions of default are of kind known to both parties, could be considered nominalistic.
  - If notice is conclusive (with improper notice only leading to damages claim), is nominalistic.

**These exceptions are all operational threats to banking and epistemic threats to money. They should be a target of law reform.**

# Issues for Scholarship?

Doctrinal Issues	Conceptual Issues	Banking Issues
<b>Setoff</b>	<b>Property</b>	<b>Liquidity</b>
<b>Special Deposits</b>	<b>Perf'tive Utterances</b>	<b>Systemic Risk</b>
<b>Third-Party Claims</b>	<b>Social Theory(!)</b>	<b>Bank Operations</b>
<b>Law of Money</b>	<b>Computer Science</b>	<b>Risk Mgm't</b>
<b>Payments &amp; Deposits</b>	<b>Cyberlaw</b>	
<b>Consumer Issues</b>	<b>Privity/Negotiability</b>	
<b>Joint Accounts</b>		

**The End**