Approved 3/26/90
Date

MINUTES OF THE SENATE COMMITTEE ON FINANCIAL INSTITUTIONS AND INSURANCE.

The meeting was called to order by SENATOR RICHARD L. BOND at
Chairperson

9:00 a.m./~~p.m.~~ on FRIDAY, MARCH 23, 1990 in room 529-S of the Capitol.

All members ~~were~~ present ~~except~~:

Senators Karr, Kerr, McClure, Moran, Parrish, Salisbury, Strick and Yost.

Committee staff present:

Bill Edds, Revisors Office
Bill Wolff, Research Department
Louise Bobo, Committee Secretary

Conferees appearing before the committee:
Kathryn Dysart, Wichita Public Schools

Chairman Bond called the meeting to order at 9:20 a.m.

HB 3005 - School district authority to purchase certain insurance.

Kathryn Dysart, Wichita Public Schools, addressed the committee in support of this bill. She requested the committee's support of this bill which would relieve Wichita Public Schools from having to solicit sealed, competitive bids for cetain types of insurance and allow them to operate in the same venue as the other 302 school districts in the state. (Attachment 1)

Senator Yost made a motion to approve this bill favorably and ask that it be placed on the Consent Calendar. Senator Salisbury seconded the motion. The motion carried.

HB 2992 - Banks: limitations on loans.

Staff explained that this bill would correct an oversight in the language when the bill was passed last year and would place the language referring to limited partners and partnership, throughout the statute. Staff further explained that the bill would allow exemptions to lending limitations for officers and other employees of a bank. Jim Maag, Kansas Bankers Association, presented a technical amendment to the bill prepared by Charles Henson, Legal Counsel for KBA, in cooperation with the Bank Commissioner. The amendment adds language throughout the bill which was omitted in the original draft. (Attachment 2)

Senator Salisbury made a motion that the amendment be adopted. Senator Yost seconded the motion. The motion carried.

Senator Karr made a motion to pass HB 2992, as amended, out of committee with a favorable recommendation. Senator Strick seconded the motion. The motion carried.

HB 3052 - UCC: funds transfers.

In the absence of conferees, Chairman Bond requested Dr. Bill Wolff to explain this proposal to the committee. Dr. Wolff informed the committee that this bill relates only to the business transactions between financial institutions throughout the state and around the world and not to consumer transactions. He further stated that all financial institutions would be regulated by this bill and also had a part in developing the language of the bill. Dr. Wolff advised the committee that the only trouble with this bill was that the effective date of this Act should be delayed until January 1, 1991, in order to give everyone involved the time to prepare for its enforcement. (Attachment 3)

MINUTES OF THE SENATE COMMITTEE ON FINANCIAL INSTITUTIONS AND INSURANCE,

room 529-S, Statehouse, at 9:00 a.m. on FRIDAY, MARCH 23, 1990.

A brief discussion ensued with Jim Maag, Kansas Bankers Association, informing the committee that Senator Winter and Representative O'Neal attended the Uniform Commissioners Conference last summer and were convinced that Kansas needed this law and Professor Barkley Clark strongly urged its adoption.

Senator Salisbury made a motion to adopt the proposed amendment to the bill. Senator Karr seconded the motion. The motion carried.

Senator Salisbury made a motion to pass HB 3052 out favorably, as amended. Senator Karr seconded the motion. The motion carried.

The meeting adjourned at 9:50 a.m.

GUEST LIST

COMMITTEE: FINANCIAL INSTITUTIONS & INSURANCE COMMITTEE DATE: Fri. Mar 23, 1990

NAME (PLEASE PRINT)	ADDRESS	COMPANY/ORGANIZATION
Tim Maag	Topeka	KBA
Kathryn Grant	Wichita	USD 259
Stan Brooks	Topeka	KS Banking Dept.
Bill Curtis	Topeka	Ks Assoc. of School Bds.

WICHITA PUBLIC SCHOOLS
Unified School District No. 259
ADMINISTRATION CENTER
217 N. WATER
WICHITA, KANSAS 67202

Kathryn Dysart, Supervisor
Intergovernmental Affairs
Telephone 316-833-4135
FAX 316-833-4100

House Bill 3005
Testimony before the Senate Committee on Financial Institutions & Insurance
March 23, 1990

We ask you strike the language from KSA 72-8404 which is specific only to the Wichita Public Schools. We find it cumbersome and unrealistic to operate under the restrictions of this section which require sealed, competitive bids to procure certain types of insurance. We do not believe we should be required to initiate expensive advertisement and bid procedures if the same measures are not required of the other 302 school districts in this state.

As you are no doubt aware, there are not very many insurance companies who handle insurance for school districts or other governmental units. Any agency which bids for our business is licensed with all the same big companies and the agency must increase its service or cut its commissions to win our bid. We don't actually bid the insurance itself.

We request that you relieve us of the restrictions of Section 1 (b) and allow us to operate in the same venue as other districts.

Attachment 1
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3/23/90

As Amended by House Committee

Session of 1990

HOUSE BILL No. 2992

By Committee on Commercial and Financial Institutions

2-13

AN ACT relating to banks and banking; concerning limitations on loans; amending K.S.A. 1989 Supp. 9-1104 and repealing the existing section.

Be it enacted by the Legislature of the State of Kansas:

Section 1. K.S.A. 1989 Supp. 9-1104 is hereby amended to read as follows: 9-1104. (a) The total liability to any bank of any person, copartnership, association or corporation, including in the liability of a copartnership or association the greatest of the individual liabilities of the respective members thereof other than limited partners who, under the limited partnership agreement, are not liable for the debts or actions of the limited partnership, and, except as provided herein for the liability of a limited partner, including in the liability of a member of a copartnership or association the liability of the co-partnership or association, shall not at any time exceed 15% of the amount of the capital stock paid in and unimpaired and the unimpaired surplus fund of such bank. If under the limited partnership agreement a limited partner is not liable for the debts or actions of the partnership, the liability of the limited partnership shall not be included in the liability of the limited partner. These limitations on total liability to any bank are subject to the following:

(1) So long as the obligation of a drawer, endorser or guarantor remains secondary, it shall not be included within the meaning of the term liability; but the discount of bills of exchange, whether or not accepted by the drawee, drawn in good faith against actual existing values, loans upon produce in transit, loans upon bonded warehouse receipts issued to the borrower by some other person, firm or corporation as collateral security, the discount of commercial or business paper actually owned by the person negotiating the same, loans secured by not less than a like amount of treasury bills, certificates of indebtedness, or bonds or notes of the United States of America or instrumentalities or agencies thereof, or those fully guaranteed by them, or general obligation bonds or notes of the state of Kansas, or of any municipality or quasi-municipality thereof, or

Attachment 2
H I I
3/23/90

of other states of the United States, or of any municipality or quasi-municipality thereof, shall be exempt from any limitation;

(2) the whole or that portion of any loan which is secured or covered by a guaranty, or by a commitment or an agreement to take over or to purchase, made by any federal reserve bank, or by the United States of America, or any department, bureau, board, commission, agency or establishment of the United States of America, including any corporation wholly owned, directly or indirectly by the United States, shall be exempt from any limitation if such guaranty, agreement or commitment must be performed by the payment of cash or its equivalent within 60 days after demand;

(3) the total liability in the form of notes or drafts to any bank of any person, copartnership, association or corporation, including in the liability of a copartnership or association the greatest of the individual liabilities of the respective members thereof *other than limited partners who, under the limited partnership agreement, are not liable for the debts or actions of the limited partnership, and, except as provided herein for the liability of a limited partner*, and including in the liability of a member of a copartnership or association the liability of the copartnership or association, may equal but not exceed 25% of the amount of the capital stock paid in and unimpaired and the unimpaired surplus fund of such bank provided such liability is secured by shipping documents or instruments transferring or securing title covering readily marketable nonperishable grains, seeds or livestock or giving a lien on readily marketable nonperishable grains, seeds or livestock having a market value at all times of not less than 115% of the amount by which such total liability exceeds 15% of the amount of the capital stock paid in and unimpaired and the unimpaired surplus fund of such bank, which market value in the case of livestock is supported by written appraisal of an officer of the bank or an independent professional appraiser made not more than six months previously, and which grains and seeds are adequately insured;

(4) the discount of bills of exchange drawn against or issued against a consignee or purchaser for materials or commodities previously sold and shipped, and which materials or commodities, or the proceeds thereof, are in the possession, control or custody of the purchaser or consignee shall be considered as the discount of bills of exchange drawn in good faith and against actual existing values, without the necessity of the acceptance of a draft or the necessity of a lien on the materials or commodities, or their proceeds; but such bills shall be subject to a limitation of 15% of such capital stock and unimpaired surplus fund for and upon each purchaser or

and

If under the limited partnership agreement a limited partner is not liable for the debts or actions of the partnership, the liability of the limited partnership shall not be included in the liability of the limited partner;

consignee;

(5) the total liability in the form of notes or drafts to any bank of any person, copartnership, association or corporation, including in the liability of a copartnership or association the greatest of the individual liabilities of the respective members thereof *other than limited partners who, under the limited partnership agreement, are not liable for the debts or actions of the limited partnership, and, except as provided herein for the liability of a limited partner*, and including in the liability of a member of a copartnership or association the liability of the copartnership or association, may exceed limitations otherwise imposed by this ~~section~~ subsection by 10% of the amount of the capital stock paid in and unimpaired and the unimpaired surplus fund of such bank provided that such total liability is secured as to payment by first lien or liens upon real estate in fee simple, to the extent of the value thereof, having an appraised value of not less than twice the amount by which such total liability exceeds limitations otherwise imposed by this section, and where such excess liability is secured by lien instrument under the terms of which any installment payments are sufficient to amortize the entire principal amount of such excess liability within a period of not more than 20 years;

(6) the limitations of this ~~section~~ subsection shall not apply to time deposits which are considered to be loans to the extent such time deposits are insured by: (A) The federal deposit insurance corporation or its successors; or (B) the federal savings and loan insurance corporation or its successors.;

~~(7) the legality of a loan hereunder shall be determined as of the date the loan is made.;~~

~~(8)~~ (7) the whole or that portion of any loan which is secured as to payment by a time deposit of the borrower in the bank in an amount equal to 115% of the amount of the indebtedness shall be exempt from any limitation under this subsection ~~(a).~~.

~~(b) (9) the~~ (b) The liability of any active officer or employee of any bank shall not exceed 5% of the amount of its paid-in and unimpaired capital stock and unimpaired surplus fund. Any loan made to any officer first must be approved by the board of directors and entered upon their minutes where the total liability of the officer to the bank, including the loan made, will exceed $10,000. The limitations on liability of any active officer or employee under this subsection, shall be subject to the provisions of paragraphs (1) through (7) of subsection (a).

(c) The legality of a loan or written commitment to advance funds, under the provisions of subsection (a) or (b), whichever occurs

and

If under the limited partnership agreement a limited partner is not liable for the debts or actions of the partnership, the liability of the limited partnership shall not be included in the liability of the limited partner;

first, shall be determined as of the date the loan or written commitment to advance funds is made.

~~(c)~~ ~~(b)~~ (d) For purposes of this section, the term "unimpaired surplus fund" includes all capital accounts (other than capital stock) derived from either paid-in capital funds or retained earnings, not subject to known charges, and which are considered interchangeable by resolution of the bank's board of directors. The state bank commissioner, with approval of the state banking board, may further define the term "unimpaired surplus fund" by regulation, and the provisions of article 4 of chapter 77, of the Kansas Statutes Annotated shall not be applicable to such regulation or regulations.

~~(d)~~ ~~(c)~~ (e) The commissioner may order any excess loan reduced to the legal limit, and after 60 days from the receipt of the commissioner's order no bank shall carry the excess of such loan and a failure to comply with any order made hereunder shall be grounds for the hearing provided in K.S.A. 9-1805, and amendments thereto.

Sec. 2. K.S.A. 1989 Supp. 9-1104 is hereby repealed.

Sec. 3. This act shall take effect and be in force from and after its publication in the statute book.

ABA Newsletter

ABA Board Supports UCC Article 4A

ABA's Board of Directors has endorsed the addition of Article 4A to the Uniform Commercial Code—the model set of laws governing commercial transactions—and urged state legislatures to adopt it.

A resolution approved by the body states: "The Board of Directors has reviewed the report of ABA's Ad Hoc Payment Systems Laws Task Force and recognizes the need for comprehensive and uniform law to govern wholesale funds transfers."

The UCC is a complex set of legal rules which has been approved by all 50 state legislatures, in part or in its entirety. The code structures the relationship of parties in a variety of commercial transactions, including contracts, letters of credit, and check collection.

While check and other payments are covered by state and federal laws, there is no comprehensive body of law governing the rights and obligations of parties to wire transfers. These are some of the issues addressed in Article 4A:

- Rules governing the time and manner of execution of payment orders.
- Determination of damages for late execution or failure to execute.
- Resolution procedures for erroneous transfers, as well as allocation of risk of loss from unauthorized payment orders.
- Clarification of the customer's duty to discover and report erroneous or unauthorized payments.
- Duties of a beneficiary's bank to the beneficiary.

In a report to the ABA Board, the Ad Hoc Task Force said, "...the present lack of comprehensive rules governing funds transfers must be remedied if this method of payment is to remain a fast, reliable, and low-cost system of transmitting large sums."

The task force went on to state that 4A represents a concerted effort by the National Conference of Commissioners on Uniform State Laws, the providers of funds transfer services, and corporate users to draft uniform rules which equitably balance the interests of all affected parties.

ABA has been active in the development of Article 4A since 1985. Task Force Chairman W. Robert Moore and other bankers had numerous opportunities to review and comment on the various drafts of Article 4A. Moore, who is retired, had been a senior vice-president of Chemical Bank, New York. In addition, ABA held a one-day symposium on Article 4A last November to help educate bankers on the proposed changes.

(For an in-depth description of the provisions of UCC 4A, see *ABA BJ*, Dec. 1989, p.20.)

Trust and Securities Ops Meeting

At a conference this month, bankers will look at the impact of the shrinking workforce, the internationalization of the securities market, mergers and acquisitions, and insider trading legislation on the trust and securities operations areas.

sion called "The Human Side of Mergers" will explain how bankers can plan for and overcome employees' feelings of resentment, resistance, and revenge, and instill a sense of loyalty to the new organization in those who are retained. At another session attendees will learn how to detect substance abuse and to assist employees in regaining control of their lives.

Clarification coming for wire transfers

By Thomas J. Greco

Over 30 years have passed since there have been any major changes to the Uniform Commercial Code's provision on payment. On Aug. 3, however, the status of this area of commercial law changed with the approval of Article 4A by the National Conference of Commissioners on Uniform State Laws.

Article 4A, when enacted into law, will govern a class of transactions commonly referred to as wholesale wire transfers.

The new article will not have an effect on wire transactions until it is enacted into state law. It is likely that some states will begin considering 4A for adoption as early as 1990.

Mr. Greco is associate general counsel for the American Bankers Association. He also served as an advisor to the drafting committee that produced Article 4A for the National Conference of Commissioners on Uniform State Laws.

Scope Of 4A

Payments made by check or credit card are more numerous than those made by wire, but the greatest dollar value is transferred by wire. In fact, the volumes sent over the two major wire transfer systems—Fedwire, the Federal Reserve's network, and CHIPS, the New York Clearing House Interbank Payment System—routinely exceed $1 trillion daily.

Check and credit card payments are covered by federal or state law, yet there is no comprehensive body of law governing the rights and obligations of participants to wire transfers. Thus, one of the major goals of the drafters of 4A was to alleviate uncertainties caused by the spotty coverage provided by existing laws, system rules, and participants' agreements. At the same time, they wanted to preserve the speed and relatively low cost of wire transfers.

Definitions. Article 4A introduces new terminology into the lexicon of banking law.

The basic element of 4A is the "payment order." This is defined as an instruction to a bank to pay—or to send an instruction to another bank to pay—a fixed or determinable amount of money to a beneficiary.

For the instruction to qualify as a payment order, the bank which receives the instruction must be reimbursed by the sender of the instruction (either by debiting the sender's account or otherwise). Further, the sender must give the instruction directly to the bank or to a communications system which then transmits the instruction to the bank.

(Note that throughout this article, the term "bank" should be interpreted to mean any financial institution engaged in the business of banking. The word "bank" is used for clarity's sake.)

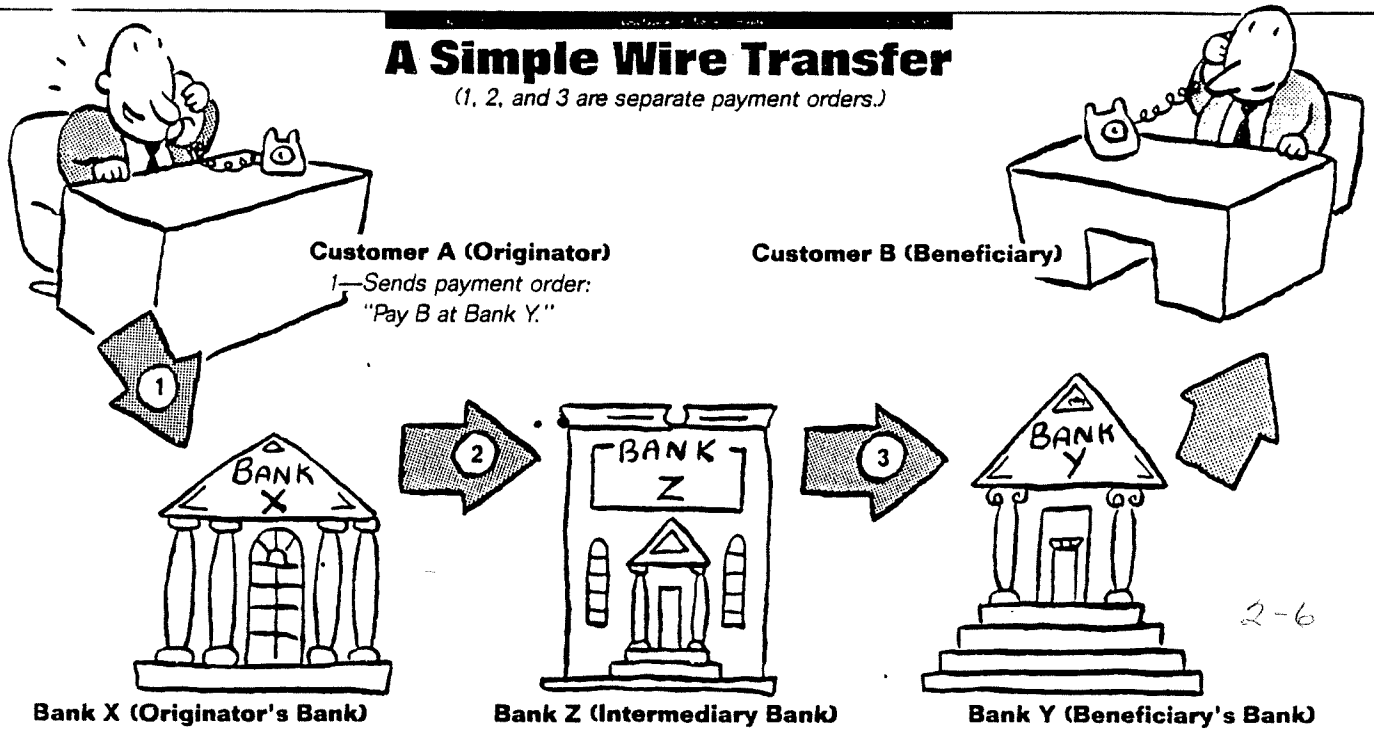
Other essential points to note from 4A's definition of payment order are:

(1) Payment orders only cover payments made through the banking system. Transfers through an entity such as Western Union are excluded.

(2) The instruction must be unconditional, except as to time of payment. (By contrast, an instruction to pay the bene-

A Simple Wire Transfer

(1, 2, and 3 are separate payment orders.)



Customer A (Originator)
1—Sends payment order: "Pay B at Bank Y."

Customer B (Beneficiary)

Bank X (Originator's Bank)
2– Sends own payment order:

Bank Z (Intermediary Bank)
3—Sends own payment order:

Bank Y (Beneficiary's Bank)
Credits B's account and tells B

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Illustration by David Brion

ficiary upon delivery of certain documents would be conditional.)

(3) Credit transfers are covered, but debit transfers (in which the person *receiving* the payment issues the instruction to pay) are not.

(4) Check and credit card transactions are excluded. This is by virtue of the requirement that the instruction be transmitted directly to the receiving bank.

The medium which carries the instruction—be it letter, telephone, fax machine, telex, etc.—is not important for characterizing an instruction as a payment order. The important point is whether the instruction is sent directly to the receiver.

Boundaries and definitions. In addition to the definition of payment order, 4A contains a specific provision which further limits the article's scope. The article does not apply to transactions governed by the federal Electronic Funds Transfer Act. This stipulation eliminates most consumer transactions. Note that 4A *would* cover consumer transfers carried out through Fedwire or similar networks used primarily for transfers between businesses. An example of the latter could arise when a parent wires funds to a son or daughter vacationing in Europe.

Other important definitions in 4A include:

- *Receiving bank*—the bank to which the sender's instruction is addressed.
- *Beneficiary*—the person to be paid.
- *Beneficiary's bank*—the bank identified in a payment order to make payment to the beneficiary, either by crediting the beneficiary's account or by some other method, such as a cashier's check.

The first sender of a payment order is known as the "originator." When the originator is not a bank, the receiving bank to which the originator's payment order is issued is known as the "originator's bank." A "funds transfer" is the series of transactions which begins with the originator's payment order and culminates with acceptance of that payment order by the beneficiary's bank. This includes any payment orders by "intermediary banks" between the originator's bank and beneficiary's bank.

Parties' Duties

Article 4A establishes a complex web of interrelated rights and obligations among the various parties to a funds

How UCC 4A came about

The Uniform Commercial Code forms the foundation of much of this country's commercial law. Yet many bankers don't know how changes in the code come about and who engineers them.

The heart of the process is the National Conference of Commissioners on Uniform State Laws. This group was organized in 1892 to promote uniformity through voluntary state action.

NCCUSL meets annually to consider drafts of proposed uniform laws. Once approved, a uniform act is then available for consideration by the various state legislatures. Until adoption by a state, model laws are just that.

Since 1961 a group known as the Permanent Editorial Board for the Uniform Commercial Code has supervised changes to the code. (The board consists of NCCUSL members and members of the American Law Institute.) Such changes become necessary when new commercial practices have made additional UCC provisions desirable.

First try fails. The adoption of Article 4A marks the culmination of an effort started in 1977 to revise Articles 3 and 4 of the present UCC.

The initial drafting effort produced a work known as the Uniform New Payments Code. This was an attempt to govern all types of payment methods under one uniform law. This effort was criticized by the banking industry and was eventually scuttled.

Second attempt. In late 1985 a new drafting committee was organized to make less sweeping changes to Articles 3 and 4 of the UCC and to develop a new article to govern wholesale wire transfers. This committee consisted of academics, uniform law commissioners, and banking, legal, regulatory, and corporate advisors.

During an intensive three-year drafting process numerous meetings were held by both the drafting committee and groups such as the ABA and the American Bar Association. This deliberative process resulted in the adoption of proposed Article 4A in August.

transfer. Before examining these, it is necessary to explain 4A's concept of "acceptance."

Acceptance is the event which triggers the parties' respective duties. Where there is no acceptance of a payment order by the bank to which it is addressed, that bank will have no liability under 4A.

In addition, if the beneficiary's bank does not accept the payment order sent by (or on behalf of) the originator, the general rule of 4A is that the originator, as well as any bank in the funds transfer, is not obligated to pay the payment order it issued. An institution could decline to accept a payment order for any number of reasons; one might be that the name and account identified in the order does not exist at that bank, or that a law or court order blocks payment to the beneficiary's account.

An example. To better understand 4A, consider what is happening during a funds transfer.

Take, for example, the payment of A (buyer) to B (seller). (See illustration.) Say A is a customer of bank X and B is a customer of bank Y. Suppose, also, that banks X and Y do not have a relationship with each other but both have a correspondent relationship with bank Z.

A would send a payment order to bank X, instructing it to pay B at bank Y. To accept this order, bank X would "execute" A's payment order by sending its own payment order to bank Z. That order would instruct bank Z to pay B at bank Y.

Correspondent bank Z, in turn, would accept this payment order by executing bank X's order. This would be done by sending its payment order to bank Y, instructing bank Y to pay B. Bank Y, the beneficiary's bank, could accept this payment order by, among other things, crediting B's account in the amount of the order and notifying B of its right to withdraw the credit.

In our example, the funds transfer involved three payment orders (A to X, X to Z, and Z to Y). In legal terms, the funds transfer might be viewed as a series of instructions which ultimately cause A's indebtedness to B (money owed to the seller) to change into bank Y's indebtedness to its customer, B, for the amount of the payment.

Who pays? The general rule of 4A is that the sender of a payment order is bound only by *authorized* payment orders accepted by the receiving bank. There may be cases—typically involving fraud—where an unauthorized payment order executed by the receiving bank is ultimately accepted by a beneficiary's bank. Article 4A uses the concepts of "commercially reasonable security procedure" and "verified" payment order to determine when the purported sender of an unauthorized payment order will be obligated to pay the order.

Let's assume the sender and the receiving bank have agreed on a commercially reasonable security procedure for checking the authenticity of payment orders. In that case, orders accepted by the receiver in good faith and in accordance with the agreed-upon security method will be binding on the purported sender—*even if the orders are not actually authorized.*

Such instances could arise when a firm breaches security by its own negligence, say by posting passwords in plain view.

"Commercial reasonableness" is determined by weighing such factors as the customer's wishes; the size, type, and frequency of orders the customer normally sends; and the type of security procedures offered to the customer.

A security procedure may also be "deemed" to be commercially reasonable if such a procedure is offered to the customer but the customer refuses it and chooses another method. In this instance, the customer must have expressly agreed, in writing, to be bound by unauthorized orders accepted by the customer's bank in compliance with the security method chosen by the customer.

Not all unauthorized, yet verified, payment orders will result in loss to the purported sender. The receiving bank may, by express written agreement with the sender, limit its ability to enforce or retain payment of the order. In addition, the purported sender can avoid liability if it is able to prove that the unauthorized order was not caused by a person the sender entrusted to issue the sender's payment orders or by a person who obtained information from the customer

which enabled them to breach security.

Erroneous Orders

Sender's errors. As a general rule, 4A provides that senders are responsible for errors made in payment orders. These could include orders naming the wrong beneficiary; giving the wrong amount; or duplicating orders already issued.

In some cases, however, the receiving bank may offer the sender a security procedure designed to detect errors. If that is the case, the receiving bank which executes erroneous orders would then bear the loss—if the sender can prove that it complied with the procedure and that the error would have been detected had the receiving bank also complied.

Any loss faced by the receiver in such a case may be reduced if the sender, after receiving notice that its account has been debited, fails to tell the bank of the error within a reasonable amount of time. This period must not exceed 90 days after notification was received by the sender. Under 4A the sender must reimburse the receiving bank to the extent the bank proves the sender's tardiness caused the loss. This reimbursement cannot be greater than the amount of the sender's order.

Execution errors. Article 4A also contains provisions governing erroneous execution of payment orders by the receiving bank.

Where the error involves transferring more funds than the sender requested or sending a duplicate order, the sender is only required to pay the receiving bank for the amount of the order the sender issued. This assumes, of course, that the funds transfer has been completed.

The receiver would then have to attempt to recover the overpayment from the beneficiary.

Where the receiver sends an order which is *less* than the amount requested by the sender, the receiving bank would only be entitled to payment from the sender if the receiver corrects the mistake by sending another payment order to the beneficiary making up the deficiency. If the underpayment is not corrected the sender is only obliged to pay the lesser amount sent by the receiving bank.

Should the receiving bank send an order to the wrong beneficiary, the sender (and all previous senders, if any) are not obliged to pay the payment order. The receiving bank which erred must attempt to recover the payment from the unintended beneficiary.

Late or improper execution. If improper execution of the sender's payment order causes payment to the beneficiary to be delayed, the bank committing the error is required to pay interest, as prescribed under 4A, for the period of the delay. Depending upon the circumstances, this interest payment would have to be made to either the originator or the beneficiary.

There are limits, however. Claims for additional, "consequential" damages—such as the loss of a lucrative business deal—may arise because the payment was not completed, or not completed in a timely manner. Typically these may not be recovered. However, they could be required if the receiving bank has *specifically agreed in writing* to undertake such responsibility.

Further, a beneficiary's bank might also be liable for consequential damages in the event that it wrongfully refuses to pay the beneficiary after the payment order has been accepted.

Processing

Accept or reject? As previously noted, obligations under 4A are not triggered until the receiver accepts the sender's order. Unless the receiving bank has expressly agreed to accept the sender's payment orders, it has no duty to do so.

In the usual funds transfer, the receiving bank accepts by executing the sender's order. The receiving bank also has the option of rejecting the order.

Failing to give notice of rejection *does not* imply acceptance by the receiving bank. However, the receiving bank's failure to give timely notice of rejection may lead to interest liability. This could occur if the sender's account has a withdrawable credit balance and the account does not bear interest. By contrast, inaction on the part of a beneficiary's bank and its failure to reject a payment order in a timely manner can result in automatic acceptance of the payment order.

Insolvency risks. An originator's ob-

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ligation to pay the receiving bank which accepts a payment order is excused by 4A in the event that the funds transfer is not completed. If the receiving bank had already received payment in this situation, it would be obliged to refund the payment.

This rule exposes the receiving bank to insolvency risks if, for example, the failure of an intermediary bank in a funds transfer chain prevents the bank from obtaining return of its own payment.

An exception applies if the originator (or other sender) specifically instructs the receiving bank to route the funds transfer through an intermediary which subsequently fails. In that case the receiving bank will not be required to refund the payment. The first sender which specified the routing of the payment order would have to try to recover.

Payment finality. Once the beneficiary's bank has paid the beneficiary, 4A would, as a general rule, prohibit that bank from recovering that payment from the beneficiary. Therefore, a beneficiary bank which permits its customer to use funds from a funds transfer before the bank receives final payment from the sender assumes the risk that the sender may not pay. Two exceptions apply.

The first is designed primarily to address transfers conducted through automated clearing houses. This exception would permit a funds transfer system's own rules to provide that transfers through that system would be considered provisional until the beneficiary's bank received payment.

The second exception addresses transfers through a system such as the one envisioned under the CHIPS proposed loss-sharing rules. The CHIPS rules, when adopted, would permit the system to complete settlement of transactions in the event that one or more participants in CHIPS fails to settle its obligation. If, despite the loss-sharing rules, the system is unable to settle, acceptance by the beneficiary's bank is nullified. The bank could then recover from the beneficiary.

Choice Of Law

The nature of the funds transfer business makes it very likely that a given funds transfer will have interstate or even international participants. Unless the parties agree otherwise, the rights and obligations between the sender and the receiving bank under 4A are governed by the law of the jurisdiction in which the receiving bank is located. However, the rights and obligations between the beneficiary and the beneficiary's bank, and the question of when payment occurs in a wire transfer are determined by the law of the jurisdiction where the beneficiary's bank is located.

Parties may, by agreement, select the law of a particular jurisdiction to control their respective rights even if the jurisdiction selected does not bear any relationship to the payment order or funds transfer. Rules of a funds transfer system may also select a particular jurisdiction's law. Both of these features of 4A's choice of law provision have the potential to expand 4A's applicability beyond those states that enact the new article.

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CLYDE D. GRAEBER
REPRESENTATIVE, FORTY-FIRST DISTRICT
LEAVENWORTH
1900 KINGMAN
LEAVENWORTH, KANSAS 66048-4230

STATE OF KANSAS

TOPEKA

HOUSE OF
REPRESENTATIVES

COMMITTEE ASSIGNMENTS
CHAIRMAN: COMMERCIAL AND FINANCIAL INSTITUTIONS
MEMBER: GOVERNMENTAL ORGANIZATION
LOCAL GOVERNMENT

M E M O R A N D U M

TO: Senator Dick Bond, Chairman
Financial Institutions and Insurance

FROM: Representative Clyde D. Graeber

RE: HB 3052

DATE: March 21, 1990

Dick, House Bill 3052 dealing with the Uniform Commercial Code, relating to funds transfers and the adoption of this part of the UCC has been passed by the House. However, the effective date as the bill was drafted apparently does not concur with the recommendation of the National Conference of Commissioners on Uniform State Laws and the bill needs to be amended if it is passed out by your committee to reflect an effective date no earlier than January 1, 1991. A copy of that memorandum from the Commissioners on Uniform State Laws is enclosed and I would appreciate your amending the bill if it is worked by your Committee.

CDG:je
Enclosure

Attachment 3
FI & I
3/23/90

National Conference of Commissioners on Uniform State Laws

676 North St. Clair Street
Suite 1700
Chicago, IL 60611
(312) 915-0195

MEMO TO: State legislative liaisons
FROM: Katie Robinson, Legislative Assistant
DATE: March 8, 1990
RE: UCC Article 4A

I wrote to you earlier about UCC Article 4A, to confirm that the Act which has been introduced in your state is the official and final version of the Act. We also need to make sure that every UCC4A act which has been introduced into the legislatures has an effective date of no earlier than Jan. 1, 1991. The reason for this is to accommodate amendments to existing systems transfer rules in coordination with UCC Article 4A. If UCC4A has already been introduced in your legislature, please make sure of this effective date. If you are considering introducing UCC4A, please keep this in mind. Thanks.