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IN THE SUPREME COURT OF THE STATE OF UTAH

BRASWELL MOTOR FREIGHT LINES, INC., a corporation,
Plaintiff-Appellant,

-vs-

BANK OF SALT LAKE, a corporation,
Defendant-Respondent.

Case No. 12784

BRIEF OF RESPONDENT

APPEAL FROM THE JUDGMENT OF THE THIRD JUDICIAL DISTRICT COURT FOR SALT LAKE COUNTY, THE HONORABLE STEWART M. HANSON, JUDGE

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IN THE SUPREME COURT OF THE STATE OF UTAH

BRASWELL MOTOR FREIGHT LINES, INC., a corporation, *Plaintiff-Appellant,* -vs- BANK OF SALT LAKE, a corporation, *Defendant-Respondent.*	Case No. 12784

BRIEF OF RESPONDENT

NATURE OF THE CASE

The Plaintiff and Appellant Braswell Motor Freight Lines, Inc., hereinafter referred to as Braswell, initiated this action against Defendant and Respondent Bank of Salt Lake, hereinafter referred to as Bank, seeking to recover the sum of $574,031.32 which was deposited in an account at the Bank together with $1,000,000.00 in additional damages.

The account at the Bank was opened by one William M. Kendall who had no connection whatever with Braswell. In its complaint Braswell alleges that the account belonged to it and that the Bank is liable for withdrawals from the same which were made by Kendall.

DISPOSITION IN LOWER COURT

Motions for Summary Judgment were made by the Bank and Braswell and were both heard by the Court on December 13, 1971.

The Motion for Summary Judgment filed by the Bank was made for the following reasons:

> ". . . that there are no legitimate issues of fact and that plaintiff's claim is barred by the following provisions of Utah Code Annotated, 1953, as amended: Sections 22-1-1, 22-1-9 and 70A-3-405, and the holding of Sugarhouse Finance Company v. Zions First National Bank, 21 Utah 2d 68, 440 P.2d 809." (R. 93).

The Motion for Summary Judgment filed by Braswell was directed to the issue of liability on the grounds that:

> ". . . the pleadings, depositions, interrogatories and answers thereto show that there is no genuine issue as to any material fact, and that the plaintiff, Braswell Motor Freight Lines, Inc., is entitled as a matter of law to a judgment in its favor on the issue of liability." (R. 98).

The Motion for Summary Judgment of the Bank was granted and the Motion for Summary Judgment of Braswell was denied by the District Court. (R. 101, 102).

Thereafter a Motion was made by Braswell to modify the Summary Judgment by imposing a constructive trust in its favor on the sum of $24,523.90 remaining in the account at the Bank. (R. 103, 105). This Motion was not resisted by the Bank for the reasons that Braswell had shown that the funds in the account at the Bank had been embezzled from it

and that a constructive trust should be imposed upon the same for the benefit of Braswell. An Amended Judgment was entered awarding Braswell the remaining balance in the account at the Bank in the sum of $24,523.90 (R. 106, 107) and this amount has been paid by the Bank to Braswell. (The Satisfaction of Judgment was not included in the record on appeal.)

RELIEF SOUGHT ON APPEAL

The Bank seeks to have the ruling of the District Court in granting its Motion for Summary Judgment and in denying the Motion for Summary Judgment filed by Braswell affirmed.

STATEMENT OF FACTS

On or about the 7th day of July, 1969 a person representing himself to be William M. Kendall opened an account at the Bank in the name of "Braswell Motor Freight Lines" and completed an account card showing William M. Kendall as the authorized signatory on the account. (R. 32 & 41).

Braswell disclaims any connection with William M. Kendall whatever. (R. 86 and deposition of J. V. Braswell, p. 26). Mr. Kendall represented to Joann Sullivan, the new accounts secretary of the Bank, at the time the account was opened that he was acting as an agent for Braswell Motor Freight Lines negotiating for the purchase of a dormant trucking authority in the State of Utah. (R. 32). He signed the account card in the name of "Braswell Motor Freight Lines" by designating "William M. Kendall, President," (R. 41). Braswell is a Texas corporation and is not now or has it ever been engaged in business in the State of Utah nor has it ever

done business with the Bank. (Deposition of J. V. Braswell, p. 55). This is significant as the address given by Mr. Kendall for the account in the name of "Braswell Motor Freight Lines" was "P.O. Box 6138, Salt Lake City, Utah 84105." (R. 41).

At all times relevant to these proceedings Braswell employed in its accounting department one D. M. Wertz, as assistant comptroller. (R. 85 and deposition of J. V. Braswell, p. 22). One of the functions of Wertz as assistant comptroller for Braswell was to order checks to be drawn on the account of Braswell with the Oakcliff Bank and Trust Company, Dallas, Texas to be deposited in another account maintained by Braswell for the purpose of paying employees. From June of 1969 through August of 1970 five (5) such orders for checks were prepared by Wertz and approved by his superior C. R. Craig totaling the sum of $573,981.32. The checks were made payable to "Braswell Motor Freight Lines" and were deposited in the account in the name of "Braswell Motor Freight Lines" at the Bank by William M. Kendall and bore the stamped endorsement "For deposit only, Braswell Motor Freight Lines." (R. 76-78).

Subsequent to the opening of the account at the Bank, various checks were written and withdrawals made from the same by William M. Kendall which were presumably misappropriated by him and W. D. Wertz, leaving a balance remaining in the account in the sum of $24,523.90. (R. 28, 29 & 35).

The foregoing was as a result of an embezzlement scheme by William M. Kendall and W. D. Wertz wherein they were successful in embezzling approximately $800,000.00 from Braswell from the time Wertz was employed by them in March of 1969 through September of 1970. (Deposition of J. V. Braswell, p. 43). The embezzlement would no doubt have continued if the employees of the Bank had not undertaken to locate the corporate offices of Braswell in Dallas, Texas and ascertain from them their interest in the account at the Bank and the connection of William M. Kendall with them. (R. 34, deposition of J. V. Braswell, p. 30).

It is significant to note that D. M. Wertz was hired as the assistant comptroller of Braswell in March of 1970 in which position he dealt directly with the management of the funds of the company, however, he was not bonded. (Deposition of J. V. Braswell, p. 22). Nor was an investigation conducted of his background which would have shown that he had been convicted of a felony and discharged from a prior employment because of an embezzlement. (Deposition of J. V. Braswell, p. 23). Also, despite the recommendations of the certified public accounting firm auditing the books of Braswell prior to the time of the embezzlement that better internal controls for the corporation be instituted, these recommendations were apparently not followed. (Deposition of J. V. Braswell, p. 15 & 45, 46). It was also the recommendation of the accountants that an examination of the cancelled checks be made which also was apparently not followed. (Deposition of J. V. Braswell, p. 75). Mr. J. V. Braswell, the President of the corporation, in his deposition also concedes that if someone in the company organization had been following the practice of

reconciling the general account at the Oakcliff Bank and Trust Company, they would have found that the checks drawn by W. H. Wertz payable to the order of "Braswell Motor Freight Lines" did not reach the other company account. (Deposition of J. V. Braswell, p. 80).

After learning of the embezzlement, Braswell hired Burns Detective Agency to investigate the same and in fact obtained sworn statements from W. H. Wertz and William M. Kendall but did not institute proceedings against them to recover the sums embezzled or any property purchased with the same. (Deposition of J. V. Braswell, p. 34). Also no report of the embezzlement was made to any authorities for the purpose of criminal prosecution of the embezzlers until October or November, 1971 which is more than one year after the crime had been discovered. (Deposition of J. V. Braswell, p. 38).

The actions of Braswell in conducting its affairs is typified by the fact that its president, J. V. Braswell, did not know of several forgeries on its account at the Texas Bank and Trust Company, Dallas, Texas in February and March of 1970 until they were pointed out to him at the time of his deposition on November 19, 1971. (Deposition of J. V. Braswell, p. 76, 77).

In addition to the instant action against the Bank, Braswell has filed suit against its former accounting firm, Peat, Marwick, Mitchell and Company, in Dallas, Texas for the sum of $1,765,025.93 because of its alleged failure to discover the loss and/or report the same to Braswell. This suit involves the same funds involved in the instant action. (Deposition of J. V. Braswell, p. 40).

ARGUMENT

POINT I

THE RELATIONSHIP BETWEEN THE BANK AND BRASWELL OF BANKER AND DEPOSITOR WAS NEVER ESTABLISHED.

In paragraphs three (3) and four (4) of its Complaint, Braswell alleges that the relationship was created between Braswell and the Bank of depositor and banker and that the Bank is charged with the responsibility of the non-negligent management of its account. (R. 1-3).

The foregoing allegations fly squarely in the face of the denial by the officers of Braswell under oath that William M. Kendall had any connections with Braswell whatever. (R. 86, deposition of J. V. Braswell, p. 26).

It is an elementary principle of law that a corporation, which is a legal entity, can only become bound by the acts of its agent having the authority to act. In this regard 19 *Am. Jur.* 2d, Corporations, Section 1079, provides as follows:

> "All corporations must, from necessity, act and contract through the aid and by means of individuals. Such individuals may be those holding corporate offices or agents properly appointed by such officers; and as a general rule corporations have the power to appoint agents with full authority to do acts or enter into contracts within the power of the corporation. It is said that validity and animation of the corporate principle is animated only through its officers and agents."

The relationship claimed by Braswell with the Bank is the relationship of depositor and banker which clearly is a contractual relationship. If William M. Kendall had no authority to act on behalf of Braswell, any purported contract between Braswell and the Bank made by him is of no force and effect and the acount in the name of "Braswell Motor Freight Lines" opened at the Bank is the account of Kendall and not the account of Braswell. The relationship between a bank and its customers is set forth in 10 *Am. Jur.* 2d Banks, Section 338 as follows:

> ". . . In other words, to create the relation of banker and depositor there must be some contract relation between the proposed depositor and the bank.
>
> * * *
>
> Although money on deposit in a bank is commonly considered to be the property of the depositor, the relationship in fact between him and the bank is that of debtor and creditor; the amount on deposit represents merely an indebtedness by the bank to the deposition. . . ."

See also *Walker Bank & Trust Co. v. First Security Corp.*, 9 Utah 2d 215, 341 P.2d 944 wherein the relationship between a bank and a depositor is determined to be contractual in nature.

Unless Braswell will concede that William M. Kendall who opened the account at the Bank was its agent, it cannot claim that the contractual relationship between the Bank and Braswell of banker and depositor was ever created. It is without question that the funds which were deposited in the account in the name of "Braswell Motor Freight Lines" were embezzled from Braswell by its employee W. H. Wertz and his accomplice William M. Kendall. Based upon this set of facts the only claim of Braswell against the Bank is for the impo-

sition of a constructive trust on the remaining funds in the account. In this regard see *Corporation of Pres. of Ch. of Jesus Christ v. Jolley,* 24 Utah 2d 187, 467 P.2d 984.

POINT II

IF WILLIAM M. KENDALL HAD AUTHORITY OF BRASWELL TO ENTER INTO THE CONTRACTUAL RELATIONSHIP WITH THE BANK OF DEPOSITOR AND BANKER, ITS CLAIM AGAINST THE BANK IS BARRED BY THE PROVISIONS OF THE UNIFORM FIDUCIARIES ACT.

As set forth in Point I, in order for the contractual relationship between Braswell and the Bank of depositor and banker to be created, William M. Kendall must have been an agent of Braswell with the authority to open the account for them with the Bank.

The State of Utah, along with several other states, has adopted the Uniform Fiduciary Act which is designed to eliminate liability on the part of a bank who deals with a fidicuiary on behalf of his principal unless the bank knows that the fiduciary is breaching his duty or acts in bad faith. If William M. Kendall was an agent of Braswell he would be a fiduciary which is defined by Section 22-1-2, Utah Code Annotated, 1953, as an "agent, officer of a corporation."

The liability of a bank in dealing with an agent or other fiduciary is set forth in Section 22-1-9, Utah Code Annotated, 1953, as follows:

> "Deposits in fiduciary's personal account — If a fiduciary makes a deposit in a bank to his personal credit of checks drawn by him upon an account in his

own name as fiduciary, or of checks payable to him as fiduciary, *or of checks drawn by him upon an account in the name of his principal,* if he is empowered to draw checks thereon, or of checks payable to his principal and endorsed by him, if he is empowered to endorse such checks, or if he otherwise makes a deposit of funds held by him as fiduciary, the bank receiving such deposit is not bound to inquire whether the fiduciary is committing thereby a breach of his obligation as fiduciary; *and the bank is authorized to pay the amount of the deposit or any part thereof upon the personal check of the fiduciary without being liable to the principal, unless the bank receives the deposit or pays the check with actual knowledge that the fiduciary is committing a breach of his obligation as fiduciary in making such deposit or in drawing such check, or with knowledge of such facts that its action in receiving the deposit or paying the check amounts to bad faith."* [Emphasis added.]

The provisions of the Uniform Fiduciaries Act were construed in the case of *Sugarhouse Finance Co. v. Zions First National Bank,* 21 Utah 2d 68, 440 P.2d 869. In the *Sugarhouse* case a Summary Judgment in favor of the defendant Zions First National Bank was reversed as to one cause of action of the Complaint which alleged that Zions *knew* that the fiduciary was committing a breach of his fiduciary obligation. However, in affirming the Summary Judgment as to the balance of plaintiff's Complaint, the Court, in commenting on the Uniform Fiduciaries Act states as follows:

". . . In other words, the statute places a duty upon principal to use only honest fiduciaries, and gives relief to those who deal with fiduciaries except where they know the fiduciary is breaching his duty to his principal or where they have knowledge of such facts that their action in dealing with the fiduciary amounts to bad faith.

* * *

> The statute was intended to cover just such situations. If a principal cannot trust his agent with money, he ought to put the agent under bond."

It is significant to note that the Plaintiff's Complaint fails to allege that the Bank acted in "bad faith" in dealing with the account in question assuming that it was the account of Braswell. In setting forth the principle that allegations of negligence, no matter how many or varied, are not sufficient to amount to bad faith, the Court in the *Sugarhouse Finance Company* case stated as follows:

> "The statute does not define 'bad faith'. However, it defines 'good faith' as being done honestly, whether it is done negligently or not. *'Bad faith' is the antithesis of 'good faith' and has been defined in the cases to be when a thing is done dishonestly and not merely negligently. Davis v. Pennslyvania Co., etc.,* 337 Pa. 456, 12 A.2d 66 (1940). It is also defined as that which imports a dishonest purpose and implies wrongdoing or some motive of self-interest. *National Casualty Co. v. Caswell* & Co., 317 Ill. App. 66, 45 N.E. 2d 698 (1943)." [Emphasis added].

Also, since both Braswell and the Bank made Motions for Summary Judgment simultaneously, all factual matters are deemed to be before the Court. In this case the record is completely void of any facts which would give rise to any claim that the Bank *knew* Kendall was breaching a fiduciary obligation or had acted "dishonestly" in connection with its dealings with the account in question.

In the Brief filed by Braswell, several cases are cited wherein a depository bank was held liable for unauthorized withdrawals made by an agent of the corporate depositor including *American Lumber Sales Co. v. Fidelity Trust Co.,* 127

Me. 32, 141 A. 102 (1928); *Nationwide Homes v. First-Citizens Bank & Trust Co.,* 267 N.C. 528, 148 S.E. 2d 693 (1966); *Barclay Kitchen, Inc. v. California Bank,* 25 Cal. Rptr. 383 (Cal. D.C. of App., 1962) and *Pacific Indemnity Co. v. Security First National Bank,* 56 Cal. Rptr. 142 (Cal. Ct. of App. 1967). In each of these cases the account with the depository bank either existed or was opened by an agent of the depositor as opposed to the fact situation in the instant case where the account in question was opened by William M. Kendall who had no connection whatever with Braswell. Also, the cases are not germane here as they were decided in jurisdictions where the Uniform Fiduciaries Act had not yet been adopted as liability would not have attached to the depository bank because of its dealings with a dishonest agent of the corporate depositor.

POINT III

NO LIABILITY WOULD ATTACH TO THE BANK BECAUSE OF THE DEPOSIT BY IT OF THE CHECKS DRAWN ON THE ACCOUNT OF BRASWELL AT THE OAKCLIFF BANK AND TRUST COMPANY WHICH WERE DEPOSITED IN THE ACCOUNT AT THE BANK.

Section 70A-3-405, Utah Code Annotated, 1953, appears to preclude Braswell from asserting any claim against the Bank for the deposit of the checks drawn upon the account of Braswell at the Oakcliff Bank and Trust Company and provides in part as follows:

> "Imposters — Signature in name of payee — (1) An indorsement by any person in the name of a named payee is effective if

(a) . . .

(b) . . .

(c) an agent or employee of the maker or drawer has supplied him with the name of the payee intending the latter to have no such interest. . . ."

As was noted in the foregoing Statement of Facts, W. D. Wertz, the assistant comptroller of Braswell, supplied the name of the payee on the checks as "Braswell Motor Freight Lines". Mr. Wertz obviously intended that the plaintiff Braswell should not have any interest in the check which was deposited in the account at the Bank in the name of "Braswell Motor Freight Lines" as part of the embezzlement scheme in which he was engaged with his accomplice William M. Kendall. This is further borne out by the fact that the account opened by William M. Kendall at the Bank bore only his name as an authorized signatory and listed the address of "Braswell Motor Freight Lines" as P.O. Box 6138, Salt Lake City, Utah 84105. (R. 41).

A history, analysis and rationale of the "fictitious payee" rule is succinctly set forth in *The Law of Bank Checks,* 4th Ed. Henry J. Bailey (1969) in Section 1524 at p. 523 as follows:

> "The 'fictitious payee' rule; Where agent of drawer supplies name of payee intended to have no interest in checks. — It is clear that, under the Negotiable Instruments Law, where a check is payable to a fictitious or non-existing person and that fact is known to the person who signed the check, the check is deemed to be payable to bearer. Thus, an endorsement in the name of the payee is not regarded as a forgery, and the loss arising from the payment of the check must fall on the drawer who employed the dishonest signing agent.

* * *

> The Uniform Commercial Code continues the expanded 'fictitious payee' rule but does so in a somewhat different manner. The Code provides that, if an agent or employee supplies the drawer with the name of the payee but intends the payee to have no interest in the check, an endorsement by anyone in the payee's name will be effective . . . *cases applying the expanded 'fictitious payee' rule virtually always involve endorsement in the name of the named payee by the embezzler or his confederate, rather than an attempt by the embezzler to circulate bearer paper without endorsement.*
>
> *The Code, like the amended N.I.L. provision, takes the position that the loss in 'padded payroll', fraudulent invoice and other cases where a dishonest employee furnishes the signing officer with the name of the payee (who is to have no interest in the check) should fall upon the employer as a risk of his business rather than on the banking system.* It is reasoned that the employer is in a better position to prevent such acts of dishonesty or to obtain forgery insurance and that the cost of such insurance is a proper business expense of the employer. *The Code provision would cover both cases where the payee is fictitious and cases where there is an actual person named as payee but where the dishonest employee intends the payee to have no interest in the check."* [Emphasis added].

As can be seen by the foregoing, even assuming that the payee on the checks, "Braswell Motor Freight Lines", was a pseudonym for Braswell, no liability would attach to the Bank for depositing the checks in the account in question or by accepting the endorsement on the check placed there by W. H. Wertz or William M. Kendall because of the obvious fact that by their embezzlement scheme they did not intend that Braswell have any interest in the check.

POINT IV

BRASWELL IS GUILTY OF CONTRIBUTORY NEGLIGENCE AS A MATTER OF LAW.

In its Brief Braswell assumes incorrectly that the account at the Bank was in fact its account and cites certain actions on the part of the Bank which it claims constituted negligent mismanagement of the account. Even if the account were Braswell's it is clear that the actions of Braswell in the management of its funds constitutes contributory negligence on its part and would preclude any recovery by it from the Bank in any event.

As was noted in the Statement of Facts, Braswell failed to follow the recommendations of its accountants on at least two occasions to implement better internal controls as they related to the management of company funds. Also, Braswell, in its Brief, focuses on the transactions surrounding the account at the Bank, however, it omits any reference to the fact that no investigation was made of its assistant comptroller W. H. Wertz at the time he was employed and that such an investigation would have disclosed that he had been convicted of a felony and dismissed from a prior employment because of an embezzlement.

Also it is significant to note that Braswell only became aware of the embezzlement by Wertz and Kendall which approximated some $800,000.00 when the Bank inquired of them concerning their interest in the account in question and their relationship, if any, with William M. Kendall.

The embezzlement by Wertz and Kendall could have been prevented or at least detected at any early stage had the employees of Braswell performed the elementary bookkeeping task of reconciling its general account at the Oakcliff Bank and Trust Company, with its special payroll account at that Bank. This proposition was acknowledged by Mr. J. V. Braswell in his deposition and his testimony is as follows:

> "Q. Mr. Braswell, if somebody had been reconciling the general account and following the checks to the deposit slips in the other account, they would have found these checks didn't reach the other account, wouldn't they?
>
> A. They should have, yes."

The position that Braswell is precluded from asserting any claim against the Bank based upon the checks drawn on its account at the Oakcliff Bank and Trust Company or withdrawals from the account opened by William M. Kendall at the Bank is supported by the provisions of Sections 70A-3-406, Utah Code Annotated, 1953, which provides as follows:

> "Negligence contributing to alteration or unauthorized signature. — Any person who by his negligence substantially contributes to a material alteration of the instrument or to the making of an unauthorized signature is precluded from asserting the alteration or lack of authority against a holder in due course or against a drawee or other payor who pays the instrument in good faith and in accordance with the reasonable commercial standards of the drawee's or payor's business."

In the instant case the actions of Braswell in failing to augment its internal controls allowed checks to be drawn payable to the order of "Braswell Motor Freight Lines" by W. H. Wertz and it may not now complain that the checks were deposited in an account over which it maintained no control.

CONCLUSION

On the basis of the foregoing it is apparent that the account in the name of "Braswell Motor Freight Lines" opened by William M. Kendall was not the account of Braswell. If the account in question was the account of Braswell it is precluded from asserting a claim against the Bank because of the provisions of the Uniform Fiduciaries Act.

The actions of Braswell's employee, W. H. Wertz, in supplying the name of "Braswell Motor Freight Lines" as the payee on the checks drawn on the account at the Oakcliff Bank and Trust Company with the intent that the payee have no interest in the same causes the loss to fall upon Braswell who employed a dishonest employee rather than upon the bank in accordance with the "fictitious payee" rule as codified in the Uniform Commercial Code. Additionally, the actions of Braswell in employing W. H. Wertz and in otherwise managing its financial affairs constitutes contributory negligence on its part.

Respectfully submitted,

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