

IN THE COURT OF APPEALS OF MARYLAND

NO. 103

SEPTEMBER TERM, 1994

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CITIZENS BANK OF MARYLAND

V.

MARYLAND INDUSTRIAL FINISHING CO.,  
INC.

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Murphy, C.J.  
Eldridge  
Chasanow  
Karwacki  
Bell  
Raker  
McAuliffe, John F., (Retired,  
specially assigned),

JJ.

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DISSENTING OPINION BY Bell, J., in  
which Chasanow and Raker, JJ. join.

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FILED: June 8, 1995

I agree that what is important in this case is "whether [the appellee's agent] had authority to indorse the way she did, not whether she had authority to deposit the way she did." Majority Op. at 10. Reasoning that "the validity of an indorsement does not depend on the agent's subjective motivation at the time of the indorsement," Majority Op. at 12, the majority correctly observes:

It defies reason to allow an event that occurs after the indorsement to affect the validity of the indorsement. An indorsement is either valid or invalid at the time it is made; if, at that time, the agent has authority to indorse, the indorsement is authorized. The use to which the agent later puts the check does not affect the agent's authorization to indorse it.

Majority Op. at 10. With this, I do not quarrel.

My quarrel is with what the majority deems to be an unauthorized indorsement in this case. According to the majority, because the appellee's instructions required its agent to use two stamps,<sup>1</sup> a signature stamp and one containing the restrictive indorsement, "For Deposit Only," "[g]iven the importance of restrictive indorsements in the relationship between the depositary bank and its customer ... an unauthorized omission by an agent of

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<sup>1</sup>A more difficult case may be presented when only one stamp is involved and that stamp contains both the principal's signature and the language restricting what the agent may do with the proceeds. In that case, it may be argued that the only authority given is to use the indorsement stamp and that the failure to do so renders the indorsement unauthorized. That is not this case and, I venture no opinion as to the resolution of that scenario.

restrictive language in an indorsement is sufficient to make the indorsement unauthorized." Majority Op. at 15-16. I do not agree. As shall be made clear hereinafter, the agent's "unauthorized omission" to use the authorized and required "For Deposit Only" stamp does not make unauthorized the agent's authorized and required use of the principal's signature stamp.

Section 1-201(43) of the Commercial Law Article, Maryland Code (1975, 1992 Repl. Vol.), defines "unauthorized signature or indorsement" as "one made without actual, implied or apparent authority and includes a forgery." A forgery is "[a] signature of a person that is made without the person's consent and without the person otherwise authorizing it." Blacks Law Dictionary 650 (6th ed. 1990). See also Bank of Glen Burnie v. Loyola Fed. Sav. Bank, 336 Md. 331, 648 A.2d 453 (1994); State v. Reese, 283 Md. 86, 388 A.2d 122 (1978); Reddick v. State, 219 Md. 95, 148 A.2d 384 (1959). Section 1-201(43) thus makes clear that to be unauthorized, a signature or indorsement must have none of the indicia of authority. This does not mean that it must be forged, however. While every forged signature necessarily is unauthorized, the converse is not true, not every unauthorized signature is a forgery.

In a subsequent title, the Commercial Law Article addresses the effect of a signature and how it may be made, § 3-401,<sup>2</sup> by whom

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<sup>2</sup>Section 3-401. Signature

it may be made, § 3-403(1),<sup>3</sup> and the effect of an unauthorized signature.<sup>4</sup>

A similar treatment is accorded the term "indorsement." Title 3, subtitle 2 addresses specific kinds of indorsements. Section 3-204 is concerned with special indorsements and blank indorsements. It provides:

(1) A special indorsement specifies the person

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(1) No person is liable on an instrument unless his signature appears thereon.

(2) A signature is made by use of any name, including any trade or assumed name, upon an instrument, or by any word or mark used in lieu of a written signature.

<sup>3</sup>Section 3-403. Signature by authorized representative.

(1) A signature may be made by an agent or other representative, and his authority to make it may be established as in other cases of representation. No particular form of appointment is necessary to establish such authority.

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<sup>4</sup>Section 3-404. Unauthorized Signatures.

(1) Any unauthorized signature is wholly inoperative as that of the person whose name is signed unless he ratifies it or is precluded from denying it; but it operates as the signature of the unauthorized signer in favor of any person who in good faith pays the instrument or takes it for value.

(2) Any unauthorized signature may be ratified for all purposes of this title. Such ratification does not of itself affect any rights of the person ratifying against the actual signer.

to whom or to whose order it makes the instrument payable. Any instrument specially indorsed becomes payable to the order of the special indorsee and may be further negotiated only by his indorsement.

(2) An indorsement in blank specifies no particular indorsee and may consist of a mere signature. An instrument payable to order and indorsed in blank becomes payable to bearer and may be negotiated by delivery alone until specially indorsed.

(3) The holder may convert a blank indorsement into a special indorsement by writing over the signature of the indorser in blank any contract consistent with the charter of the indorsement.

Section 3-205 defines restrictive indorsement as one

which either

- (a) Is conditional; or
- (b) Purports to prohibit further transfer of the instrument; or
- (c) Includes the words "for collection," "for deposit," "pay any bank," or like terms signifying a purpose of deposit or collection; or
- (d) Otherwise states that it is for the benefit or use of the indorser or of another person.

The effect of a restrictive indorsement is treated in section 3-206. As relevant to the issue sub judice, it provides that, to be a holder for value, "any transferee under an indorsement which is conditional or includes the words "for collection," "for deposit," "pay any bank," or like terms ... must pay or apply any value given by him for or on the security of the instrument consistently with the indorsement...."

Subtitle 4 of Title 3 is where the liability of the parties to

a commercial transaction is addressed. As the majority accurately points out, the critical provision for our purposes is § 3-419(1)(c), which holds a bank who pays a check on a forged indorsement liable for conversion. Because, for purposes of this section, however, an unauthorized signature is treated the same as a forged one, the critical question when a signature is not a forgery involves the extent of the authority of the agent who signed the check on behalf of the payee. This issue is resolved by reference to § 3-202, which provides:

(1) Negotiation is the transfer of an instrument in such form that the transferee becomes a holder. If the instrument is payable to order it is negotiated by delivery with any necessary indorsement; if payable to bearer it is negotiated by delivery.

A "holder" receives the instrument "drawn, issued or indorsed to him or his order or to bearer or in blank." § 1-201(20). See also § 3-302 (holder in due course).<sup>5</sup> An instrument is payable to order "when by its terms it is payable to the order or assigns of any person therein specified with reasonable certainty, or to him or his order ...." § 3-110(1). To be negotiable, § 3-202(1) makes

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<sup>5</sup>§ 3-302. Holder in due course.

- (1) A holder in due course is a holder who takes the instrument
- (a) For value; and
  - (b) In good faith; and
  - (c) Without notice that it is overdue or has been dishonored or of any defense against or claim to it on the part of any person.

clear, a check paid to order must bear the signature of the person to whose order it is payable. Thus, while "indorsement" is not synonymous with signature, and, indeed, may consist of a signature, a special indorsement and/or restriction on the use of the proceeds, for negotiation purposes, "any necessary indorsement" recognizes and, in fact, contemplates an indorsement in blank, i.e. "a mere signature." See § 3-204(2).

In this case, the checks that Pagani deposited to her own account were made payable to the appellee; they were payable to order. To negotiate those checks so that their proceeds could be deposited in the appellee's account required the appellee's valid signature. Pagani expressly was given authority to place the appellee's signature on those checks and deposit their proceeds in the appellee's account. That authority was expressed by the appellee in terms of requiring Pagani to use two stamps, one of which was a signature stamp. Pagani was, therefore, as the trial court concluded, expressly authorized, by use of the signature stamp to place on the checks the signature necessary for their negotiation. That authority did not dissipate simply because Pagani did not also use the restrictive indorsement stamp. That is particularly the case when, as here, the restrictive indorsement stamp, was not always used when the deposits were made to the proper account. It is no answer, as the majority suggests, that, as to the latter transactions, the appellee ratified the unauthorized signature. See Majority Op. at 16 n.11. If there

were a ratification, logically, from the appellee's perspective, it was of all such "unauthorized signatures." I believe that the appellant bank properly negotiated those checks presented to it stamped with the company's signature.

If, as the majority recognizes, "[t]he use to which the agent later puts the check does not affect the agent's authorization to indorse it," Majority Op. at 10, i.e., the agent's misappropriation of the funds is irrelevant to her authority to negotiate the check, then, surely, the vehicle by means of which the misappropriation is effectuated can have no greater affect on the validity of the indorsement and, thus, the check's negotiability. In this case, being authorized to indorse the appellee's checks with its signature stamp, Pagani simply omitted to follow the instructions of her principal to use the second stamp she was required and authorized to use. While that omission enabled Pagani to misappropriate the funds - it was the means by which Pagani was enabled to deposit the company's funds into her account - it formed no part of the indorsement. Indeed, it was just another event occurring subsequent to the indorsement for purposes of negotiation. As such, it simply could not affect the validity of the appellee's signature.

The culpability of an agent who disobeys his or her principal's instructions and, thereby, misappropriates his or her principal's funds is the same no matter how that disobedience is manifested. Boiled down to its basics, the authority given in this

case was to deposit the appellee's checks in the appellee's account. That the appellee instructed the agent as to the details of how that was to be accomplished, i.e. telling her to use particular stamps to indorse the check, does not change the nature of the instruction. It certainly does not provide a principled basis for differentiating the agent's responsibility.

The cases upon which the majority relies for the proposition that the relevant question is the authority to indorse, rather than where the money is deposited, fully support the result I would reach. As stated in Jones v. Van Norman, 522 A.2d 503 (Pa. 1987):

The signing of the payee-principal's name on the check is either authorized or it is not. That status does not depend upon whether the authorized representative properly applies the checks to the account of the payee or misapplies them to his own use.

Id. at 507. Similarly, in Bank South, N.A. v. Midstates Group, 364 S.E.2d 58 (Ga. Ct. App. 1987), the court wrote:

"[t]he question of what use Williams was ultimately authorized to put an instrument held by Midstates after he had placed the corporate indorsement on it is separate and distinct from the question of whether he was authorized to indorse the instrument in the first instance."

Id. at 61. See also Great Southern Nat. Bank v. Minter, 590 So.2d 129 (Miss. 1991) (indorsement authorized despite misappropriation of funds). And Oswald Machine Equip., Inc. v. Yip, 10 Cal. App. 4th 1238, 13 Cal. Rptr.2d 193 (1992), upon which the majority heavily relies to establish that "an agent who is authorized to do

one [act] is not necessarily authorized to do the other," Majority Op. at 15, is inapposite. There the agent indorsed checks with name stamps of fictitious businesses and then deposited those checks into an account opened under those fictitious names. The agent did not, in other words, use the principal's authorized stamp; unlike in the case sub judice, in that case, the agent's indorsement clearly was unauthorized.

I agree with the majority. There are consequences associated with the failure to comply with a restrictive indorsement. See § 3-206(3) (transferee is holder for value only to extent that payment or value is given consistently with indorsement). Thus, as the majority points out, a transferee is answerable in contract, to its immediate indorser, for damages caused by failing to comply with any restrictions contained in the indorsement and a depository bank<sup>6</sup> is liable in conversion for the same reason. See § 3-419(4) ("An intermediary bank or payor bank which is not a depository bank is not liable in conversion solely by reason of the fact that proceeds of an item indorsed restrictively ... are not paid or applied consistently with the restrictive indorsement of an indorser other than its immediate transferor."). A restrictive indorsement is not, however, any part of the "necessary indorsement" for purposes of negotiation. What is required to negotiate a check is that the check be transferred so that the

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<sup>6</sup>"Depository Bank" is "the first bank to which an item is transferred for collection...." § 4-105(a).

transferee becomes a holder. A transferee is a holder of a check indorsed in blank. An indorsement in blank may "consist of a mere signature." See § 3-204(2). Moreover, the absence of a restrictive indorsement does not render the negotiation ineffective. As § 3-207(1)(d) makes clear, "[n]egotiation is effective to transfer the instrument although the negotiation is ... [m]ade in breach of duty." In short, while consequences flow from the failure of a transferee, in this case the appellant bank, to comply with an actual, disclosed restrictive indorsement, the same consequences do not follow from the failure of the indorser to include the restrictions in the indorsement. In that latter circumstance, the check is appropriately and validly negotiated. To the extent the transferee gives value, acts in good faith, and without notice of defenses,<sup>7</sup> it is a holder in due course. § 3-302(1).

The majority makes much of the fact that, if the omission were not noticed by this Court, "the principal - drawee's ability to recover [would be placed] entirely in the hands of the agent under the circumstances presented in this case." Majority Op. at 16. The argument is curious inasmuch as the method an agent chooses to

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<sup>7</sup>There is no dispute that the appellant gave value. The other two requisites are also established on this record. There is no suggestion, and certainly no evidence that the appellee informed the appellant of the instructions it gave its agent - that it authorized only the use, in tandem, of two stamps and that any indorsement that was not strictly in compliance with those instructions was unauthorized.

breach his or her duty to the principal always impacts the principal's liability or right to recover. Under my approach, however, what approach the agent uses to breach his or her duty is not an issue. I repeat, as I see it, the agent in this case simply breached her duty to her principal. That does not impact the authority she was expressly given to place the appellee's signature on checks paid to the appellee's order. That the instructions specifically addressed the method by which the misappropriation was effected does not change the question from one of misappropriation to one of authority.

It is quite likely, as the majority suggests, that the bank ultimately will prevail in this case, in light of § 3-419(3).<sup>8</sup>

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<sup>8</sup>Who better than the businesses that authorize their agents to indorse checks are in a position to avoid loss? In this case, MIFCO had several mechanisms at its disposal to "police" such losses. It could have given its agent only one stamp; it could have notified the appellant of its indorsement procedures; it could have checked its books internally, periodically, for any losses. MIFCO apparently had no system. Surely then, it is MIFCO that should bear the loss. See § 3-406, which provides:

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.

That, however, does not answer the question this case presents. In my opinion, the bank should not be called upon to establish its entitlement to the benefit of § 3-419(3) unless and until the agent's lack of authority to indorse the check has been shown. Where the evidence is clear, as here, that the appellee authorized the agent to use its signature stamp and the agent did so, express authority has been shown, notwithstanding the agent's failure to use another authorized stamp.

I dissent.

Judges Chasanow and Raker join in the views herein expressed.

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Comment 7 to that section notes that "[t]he most obvious case is that of the drawer who makes use of a signature stamp or other automatic signing device and is negligent in looking after it." That rather clearly describes this case.