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## Why states should adopt Article 4A of the UCC

**N**ew Article 4A of the Uniform Commercial Code concerns a type of payment made through the banking system called a "funds transfer." (A popular term for the bulk of these kinds of transfers is "wholesale wire transfer." This term is not used in Article 4A because all "funds transfers" are not "wholesale" and not "wire" transfers.) A "funds transfer" is, generally, a large, rapid money transfer between commercial entities. In the average "funds transfer" \$5,000,000.00 changes hands. In most instances, such transfers will occur between banks using computers and electronic communications. (Consumer transfers through credit cards and ATM machines are not governed by Article 4A, but are governed by federal law.) Article 4A provides a body of law on the rights and obligations connected with "funds transfers."

There is currently no comprehensive body of law that defines the rights and obligations that arise from "funds transfers." Some aspects of "funds transfers" are governed by rules of the principal transfer systems. Transfers made by the Federal Reserve network (Fedwire) are governed by Federal Reserve Regulation J and transfers over the Clearing House Interbank Payment System (CHIPS) are governed by CHIPS rules. But these rules apply to only limited aspects of "funds transfer" transactions.

Article 4A will provide:

### CERTAINTY

Currently, no participant in a "funds transfer" can know with certainty what the rights and obligations of parties are. Enactment of Article 4A solves the problem.

### BALANCE

Article 4A carefully addresses the interests of banks, commercial users of this payment method and the public. It seeks a fair balance between interests involved in "funds transfers."

### REMEDIES

What law exists does not provide clear remedies for "funds transfers" when something goes wrong. UCC-4A establishes who takes the risk of loss, who will be liable and what will be the damages.

## EFFICIENCY

Article 4A is designed to facilitate a speedy and inexpensive system to transmit huge sums that are substantially cash equivalent, benefiting both the national and international economies.

## FREEDOM OF CONTRACT

Users and banks are free to vary many provisions of UCC-4A by individual contract. They are not locked into invariable rules that might impede transactions between them.

## UNIFORMITY

"Funds transfers" are an important part of business and are interstate in character. Uniformity is as important to the conduct of "funds transfers" as it is to other current payment methods.

## CONCLUSION

The growing role that "funds transfers" have in the business world today makes it clear that modern law on this subject is needed. Users of "funds transfers" now depend mainly on court cases, or their own rules, to resolve disputes. This creates great uncertainty. UCC-4A answers these immediate needs.

## Important Information on Article 4A of the UCC

In 1989, as Article 4A of the UCC is proposed for enactment by the states, over \$1 trillion is transferred daily by "funds transfers." Five years ago the daily average was \$300 million and two years ago it rose to \$500 million. Some peak days now exceed \$2 trillion, while utilization continues to grow. "Funds transfers" exceed the total amounts transferred in all other payment systems — credit and debit cards and checks combined. The average "fund transfer" exceeds \$5 million.

Yet there is no comprehensive law governing commercial "funds transfers." Regulation J covers the interbank part of any commercial "funds transfer" by the Federal Reserve network (Fedwire). The Clearing House Interbank Payment System (CHIPS) rules cover the bank participants in that system. The Electronic Funds Transfer Act of 1978 covers consumer transactions. In spite of all of that, when a commercial customer initiates a "funds transfer" through a bank for payment to a designated beneficiary, no comprehensive rules and no readily ascertainable law pertains. As a result, most commercial "funds transfers" are made with no provision for the significant liabilities that will accrue if something goes wrong.

**Article 4A fills the void.** It comprehensively provides coverage of commercial "funds transfers" from the order of the originator to the originator's bank, through intermediary banks, to the beneficiary's bank. No other country has such a comprehensive law, proposed or in being.

Article 4A sets forth safety net rules absent agreement of the parties, covering liabilities and obligations arising from: unauthorized payment orders; proper and improper (wrongful and erroneous) execution of payment orders; fraud; and, insolvency of participating banks. What constitutes payment for the discharge of an underlying obligation is, also, governed by Article 4A.

The major objectives of Article 4A are to preserve a fast, efficient, reliable system for the transfer of large volumes of funds rapidly at a low cost; to provide certainty as to the obligations and liabilities; to safeguard the integrity of the "funds transfer" system; and to establish the basic rights and responsibilities of the participants, except as varied by agreement of the parties.

### **Benefits to Corporate Users**

Most senders of payment orders in a "funds transfer" are banks and corporations. Senders under Article 4A enjoy the following benefits:

1. *Finality of payment* — Funds transferred are essentially equivalent to cash with a more certain degree of finality than is currently the case.
2. *Moneyback guarantee* — If the "funds transfer" is not completed, the originator's bank must return the originator's money.
3. *Discharge of underlying obligation* — A statutory discharge of the underlying obligation generally occurs upon acceptance by the beneficiary's bank.
4. *Commercially reasonable security procedures* — Substantial incentives for banks to provide reasonable security procedures are fostered or the bank may absorb the loss for an unauthorized order.
5. *Error reporting* — While users have a duty to report errors, failure to do so within a reasonable time results only in possible interest losses. No other damages are imposed.

6. *Loss apportionment* — If a loss results from an unauthorized order, when there is an agreed security procedure, the receiving bank suffers the loss unless the bank can prove:

- the security procedure was commercially reasonable;
- the bank followed the procedure;
- the bank acted in good faith; and
- the bank complied with the customer's written agreement or instructions restricting acceptance of payment orders.

Even if the bank proves the above, should the customer prove that it's without fault, pure interloper losses fall on the bank.

7. *Damages for dishonor* — If the beneficiary's bank has accepted the order and the beneficiary demands payment, the bank, for failure to pay, may be liable for damages, including consequential damages, if the beneficiary gave notice of the particular circumstances that would give rise to such damages and indication of the magnitude of them.

### Benefits to Banks

The banking community will benefit as follows from Article 4A:

1. *Certainty* — There is no statutory or case law that adequately governs these transactions. Frequently, contracts between customers and banks are absent or inadequate. Perhaps no contract could be adequate to govern the risks, given the paucity of applicable law. Therefore, all parties to "funds transfers" operate in an uncertain legal environment. Article 4A removes the uncertainty. Certainty as to liability and responsibility promotes sound credit policy and financial management. Since Article 4A largely embraces current operating practices, the efficiency of the present system is preserved.
2. *Banks as users* — As the principal users of the "funds transfer" system, banks will enjoy all of the benefits of Article 4A listed above for users.
3. *Limitation of liability* — Article 4A limits liability to loss of interest and principal, or in certain cases other incidental costs and reasonable attorney's fees. Only in the event of intentional dishonor and with specific notice of the particular circumstances and contemplated magnitude, are consequential damages recoverable.
4. *Statute of limitations* — Article 4A precludes objection to payment of an order executed by a bank unless made within one year from the time the customer receives notice the order was sent.
5. *Creditor processes* — Under Section 4A-502, banks are protected from creditor processes during the fast electronic batch processing of payment orders.
6. *Choice of law* — Section 4A-507 contains rules as to choice of applicable law that will promote certainty.
7. *Netting of obligations* — If banks owe other banks and are owed by those same banks on payment orders sent and received, Section 4A-403

gives statutory authorization for bilateral and unilateral netting of payment obligations among banks to reduce insolvency risk.

8. *Number and name of account* — If a bank discloses to its customer that it may rely upon numbers to identify a beneficiary in a payment order, Section 4A-305(3) authorizes it to rely upon the number used by the customer to identify the beneficiary. Because processing is electronic and rapid, reliance on numbers facilitates "funds transfers."

9. *Rely on tested message* — Banks can rely upon the message that tests against the security procedure, unless the customer proves that the payment order is unauthorized and the breach of the confidential security information did not result from a source controlled by the customer. The bank, however, must have offered a commercially reasonable security procedure to the customer and have followed that procedure and any customer written agreement or instruction, all in good faith.

# UNIFORM COMMERCIAL CODE

## ARTICLE 4A — FUNDS TRANSFERS

— A Summary —

**T**he payment of obligations is of vital importance to almost all commercial transactions. Occasionally problems arise when payment is not made, or is made improperly. It is neither convenient nor prudent to pay large or even modest obligations in actual cash. So, individuals and corporations, big account holders and small, have turned to bank accounts and bank credit, and have paid obligations by written instruments that accomplish a transfer of bank credit - check, money order, bank draft, etc. For the past twenty years, in every state, the rights and obligations of parties to payment by check have been governed by Articles 3 and 4 of the Uniform Commercial Code (UCC). Checks will remain the method by which many obligations are paid for the foreseeable future. However, electronic technology is now a fact of life and new methods for transferring bank credit for the purposes of payment are a result. Article 4A is a reflection of this fact.

How has technology affected systems of payment? Most people are aware of automated teller machines for their personal use. Indeed, these machines have become very popular. But such technology is widely used to make large transfers of funds that satisfy obligations arising from commercial transactions as well. The technology is simply too convenient and too fast not to be used for the transfer of large sums around the world.

The amounts which move through the large value automated systems are truly staggering. In 1989 as Article 4A is promulgated, one trillion dollars are transferred on an average day. In 1989, a record day of three trillion dollars was recorded. This is roughly the 1989 gross national product of the United States. Undoubtedly, this record will be surpassed in due course

and probably frequently in the future. Such figures indicate the impact of the technology. They also indicate the need for some governing law.

In 1989, as the new Article 4A is proposed to the states for adoption, there is no backstop statutory law to govern funds transfers. The rules for checks in Articles 3 and 4, which utilize the signatures and endorsements on the check as the basis for determining liability, do not apply to electronic funds transfers. Nor are the rules governing the liability of banks to customers under Article 4 helpful. Many transfers in the United States are effected through electronic transfer networks; one is owned and operated by the Federal Reserve and is known as FedWire and the other is owned and operated by the New York Clearing House and is known as CHIPS (Clearing House Interbank Payments Systems). Each of these systems has rules to govern transactions between participating banks, but they do not affect bank customers. Outside FedWire and CHIPS, common-law contract rules are the basis for determining liability. However, serviceable, negotiated contracts are rare. Bank customers usually need a funds transfer immediately and do not take the time to negotiate a contract. Transfers are frequently made in a legal void.

Article 4A is the remedy for this void. Because the total volume of funds transfers is very great and because many individual transactions are very large, the cost of uncertainty in the law could be very high. Article 4A is necessary to the continued usage of existing funds transfers and for the anticipated future expansion in this usage.

Some terminology is necessary to follow a funds transfer under Article 4A. A "sender" is any person or entity who sends a "payment order." The first sender

is the originator, and subsequent senders are banks participating in the transfer. A sender communicates a "payment order" to a "receiving bank." Receiving banks become senders if they forward "payment orders" to other banks. The last bank in the communications chain is the beneficiary's bank, and it can never be a sender with respect to the specific funds transfer. The "beneficiary" is the entity that the sender intends to pay. A "payment order" is simply the form of communication that the parties to a funds transfer agree to use. The payment order's salient characteristics are that it calls for an unconditional payment of money from the sender to the beneficiary and that it is transmitted to a receiving bank.

Unless the persons or entities involved in a payment of money use the same bank, a funds transfer involves at least four parties: the originator of the payment; the bank to which the originator communicates the first payment order; the beneficiary's bank that receives the final payment order; and last, the beneficiary. Intermediary receiving and sending banks also may be involved. These are banks that act as conduits of payment when there is no capacity to communicate directly between the originator's bank and the beneficiary's bank.

An example illustrates the process of a funds transfer. Suppose Alpha Corporation wants to pay money to Beta Corporation to satisfy a large contractual obligation. Alpha is in New York, and Beta is in California. Alpha has a bank account with a balance sufficient to pay Beta at First Bank in New York. Beta maintains an account at Second Bank in California. The process of payment is simple. Alpha orders First Bank to pay the owed money to Beta through a transfer to Second Bank. Alpha's order is pursuant to an agreement that Alpha has with First Bank. When First Bank receives the payment order from Alpha, it communicates with Second Bank. The communication indicates that a specific amount at First Bank held for Alpha will be transferred to Second Bank with the understanding that it will be passed on to Beta. Second Bank accepts this second payment order and notifies Beta that the money is available to Beta. Value passes

between the two banks through accounting entries in a process known as settlement.

With simple transactions, why do we need a whole new article in the Uniform Commercial Code? New law - or any law - isn't necessary if everything works. But what if something goes wrong? What if First Bank makes a mistake as to the amount to be paid? What happens if Second Bank doesn't notify Beta? What happens if the payment order is fraudulent, and not actually issued by Alpha? What happens if there is a bank failure? These are a few examples of possible errors.

A funds transfer is like a string of Christmas lights: everything is fine until a light burns out. There must be a remedy for the burned out light, and to the extent there are losses they must be paid. What are the remedies if someone takes a loss? Who bears the risk of loss at a given time in the transactional process? No adequate answers to these questions exist without a backstop statutory law that allocates the loss at the appropriate places in the funds transfer. Article 4A provides clear and reliable answers, and thereby keeps the string of lights burning.

To resolve the problem of who is responsible when something in a funds transfer goes wrong, Article 4A divides the actions of the parties to a funds transfer into three essential parts. First, a funds transfer is initiated by the originator and accepted by the originator's bank. Part 2 of Article 4A, entitled "Issue and Acceptance of Payment Order," governs the relationship between the sender of a payment order and the receiving bank that will execute the payment order. What constitutes acceptance and rejection (both rightful and wrongful) of a payment order, and what must be done to amend a payment order, are determined by the rules of Part 2, as these involve the relationship between the sender and receiving bank in a funds transfer.

As between sender and receiving bank, who suffers a loss if there is a mistake? Part 2 of Article 4A resolves this critical issue. Two kinds of mistakes can occur between sender and receiving bank, an un-

authorized payment order and an erroneous payment order. The key to the rules on an unauthorized payment order is the "security procedure" that exists between sender and receiving bank. This is the agreed procedure that verifies the authenticity of a payment order or other relevant communication. In electronic funds transfer systems, the security procedure is an important element, and may involve codes, encryption, callback procedures, and the like. Any procedure that can be devised to protect the transaction is eligible. To be legally effective, it must only be commercially reasonable.

The security procedure determines who takes the risk of loss when there is an unauthorized payment order. If there is a commercially reasonable security procedure that is followed by the receiving bank, the sender must absorb the loss. If the sender proves that the security procedure was not followed or was breached by someone outside the control of the sender, the receiving bank takes the loss. The assumption is that the security procedure, if followed and not breached, will verify the authenticity of payment orders.

The risk of loss for an erroneous payment order also hinges upon compliance with a security procedure for detecting error. If the sender proves that it complied with the security procedure, the receiving bank takes the loss. Otherwise, the sender is responsible for erroneous orders.

The second part of a funds transfer is the passage of funds from receiving bank to receiving bank, until the beneficiary's bank is contacted. This is covered by Part 3 of Article 4A, which is entitled "Execution of Sender's Payment Order by Receiving Bank."

Rules governing the relationship between receiving banks are contained in this part. A principal obligation of a receiving bank (other than the beneficiary's bank) is to "execute" a payment order once it has accepted the order - that is, pass it on to the next bank in the string. It executes by issuing a payment order to the next bank. (The beneficiary's bank has a different obligation. It must pay the obligation

to the beneficiary, and that is covered in Part 4 of Article 4A.) Unless agreed otherwise, a bank may use any commercially reasonable method to issue a payment order. A receiving bank is, generally, responsible for any error it commits in issuing a payment order. If a receiving bank overpays the beneficiary of a payment order, the excess is recovered from the beneficiary, not from prior senders. If a receiving bank pays a person or entity that is not the intended beneficiary, recovery is from the person receiving the money, and not from any prior sender. Only if a receiving bank underpays in a payment order, may the bank recover from prior senders, and then only an amount to cover the error and only if it issues a curative order.

Part 3 of Article 4A covers other issues pertaining to receiving banks. For instance, rules on reporting an erroneous payment order and late execution of a payment order are furnished.

The last part of a funds transfer involves actual payment to the beneficiary. It is the subject of Part 4 of Article 4A, "Payment." Each sender, going back to the originator, is obligated to pay. At a given time, the beneficiary is considered to have been paid. There is a two step approach to actual payment, although the steps are accomplished simultaneously if the transfer is made by Fedwire. First, credit is extended by each receiving bank to each sender when the sender's payment order is accepted - basically, a communications function. The second stage involves settling up between participants - the actual passage of value.

Perhaps the most important section in Part 4 is Section 4A-402. It provides that a sender of a payment order is obliged to pay the amount of the order to the receiving bank if the funds transfer is properly completed. It is essential to distinguish, in this regard, a payment order from a check.

A check is a kind of payment order. When a person writes a check on an account, it orders the institution in which the account resides to pay money to a named person (whose technical name is the payee). Although a check suspends the liability of the person

who writes it for an underlying obligation until the instrument is rightfully presented for payment and paid at the institution in which the account resides, it can be passed from person to person as payment for other obligations and accrues and extinguishes liabilities for those persons as it passes between them. If the institution refuses to pay when the check is presented, then the person who initially wrote the check is liable for the underlying obligation as well as for the check. In contrast, acceptance of a payment order for a funds transfer by a receiving bank obligates the sender to pay that bank, and that bank alone. There is no instrument that may be passed from hand to hand as payment between other people. There are no lingering liabilities that result from the negotiability of an instrument. A payment order for a funds transfer is simple and direct.

How does settlement take place? If the sender is a bank, and the funds transfer is through one of the funds transfer systems, payment takes place according to the rules of the system that govern settlement between banks. Typically, payment is a matter of debiting an account of the sender with the receiving bank, and crediting the receiving bank's account. These methods hold whether the sender is an individual or a bank.

The beneficiary's bank, the last bank in the string, is responsible for paying the beneficiary. Payment generally takes place by crediting an account of the beneficiary, although satisfaction of a beneficiary's debt also constitutes payment, and payment in general occurs when the funds are available to the beneficiary for withdrawal. The originator of a payment order, that first link in the string of links, generally is deemed to have paid the beneficiary on the underlying commercial obligation when the beneficiary's bank accepts the payment order. If it seems premature to discharge the originator, it is because at the time of acceptance by the beneficiary's bank, the originator has done all

in its power to see that the beneficiary has obtained a credit balance at the beneficiary's bank in the agreed-upon amount. It is analogous to a situation where the originator has deposited cash to the beneficiary's account at beneficiary's bank. At that point, the originator's obligation to the beneficiary should be considered satisfied.

Finally, there are some other features of Article 4A to be considered. First, any transaction that is subject to the Electronic Funds Transfer Act of 1978 is not subject to Article 4A. This express exclusion places consumer transactions outside Article 4A, and leaves them to federal law. Second, the regulations and operating circulars of the Federal Reserve Board supersede any inconsistent provision of Article 4A. Third, transfer system rules will prevail if inconsistent with any part of Article 4A. Fourth, it is possible to vary the effect of most of the provisions of Article 4A, honoring the general Uniform Commercial Code policy of freedom of contract.

The fifth matter of special interest needs extra emphasis. Funds transfers occur and are useful so long as it is fast, efficient and inexpensive to use current and future electronic methods. A great deal of money can be passed through the current system for very little comparative cost. Therefore, Article 4A limits consequential damages for improper payment orders. Consequential damages might raise costs, reduce transaction speed by requiring the exercise of discretion by management, and increase uncertainty.

Article 4A of the Uniform Commercial Code is essential law. The continuance and viability of funds transfers depends upon its advancement in the states. And uniformity is an absolute requirement in every state, unconditionally and without deviation. Otherwise, there will be impairment of the functioning of funds transfers for the long term.

REPORT OF THE  
AD HOC PAYMENT SYSTEMS LAWS  
TASK FORCE  
TO THE  
BOARD OF DIRECTORS  
OF THE  
AMERICAN BANKERS ASSOCIATION

ON

UNIFORM COMMERCIAL CODE  
ARTICLE 4A  
FUNDS TRANSFERS

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## EXECUTIVE SUMMARY

On August 3, 1989 the National Conference of Commissioners on Uniform State Laws approved Article 4A as an addition to the existing Uniform Commercial Code. Article 4A, when enacted into law by the various states, will govern a class of payment transactions known as wholesale funds transfers. Present law, regulation and private agreements covering funds transfers are considered inadequate and generally incapable of efficiently resolving such issues as liability for mistakes, fraud and insolvency.

The provisions of Article 4A were drafted through the joint efforts of Uniform Law Commissioners, academics, bankers, corporate users of funds transfers and regulators. The final version of 4A represents a compromise which attempts to strike a balance between the interests of the public, those of the providers of funds transfer services and those of the users. While the banking representatives would have resolved several issues differently, it is the general consensus of the bankers that participated in the drafting process, as well as the Ad Hoc Payment Systems Laws Task Force, that Article 4A's benefits to the banking system significantly outweigh its disadvantages.

The task force urges the American Bankers Association Board of Directors to adopt a resolution indicating the Association's support for Article 4A and encouraging State Legislatures to enact 4A into law.

## Project Background

On August 3, 1989 the National Conference of Commissioners on Uniform State Laws (NCCUSL) approved the addition of Article 4A to the Uniform Commercial Code (UCC). This is the first time in over thirty years that the Commission has made any significant changes to the UCC's provisions on payment. Article 4A, when enacted into law by the various states, will provide a comprehensive legal structure for a class of payments known as wholesale funds transfers.

(Throughout this report the term "funds transfer" will be used to denote a discrete method of payment by which a bank customer instructs its bank to credit another bank account. The term "wire transfer", which refers to the method used to transmit the instruction, is a specific sub-class of funds transfer.) Presently, while the greatest dollar value is moved by funds transfers, the existing law governing such transactions is a make shift framework of private agreement, system rules, federal regulation and case law. This patch-work quilt of rules creates uncertainty, litigation and unnecessary expense when problems occur in the course of such transfers.

NCCUSL was organized in 1892 to promote uniformity of law by the voluntary action of state governments. The UCC, which was drafted during the late 1940's and early 1950's, is a fundamental source of statutory commercial law and covers such topics as sales of goods, negotiable instruments, letters of credit, secured lending and securities. Since 1961 a group known as the Permanent Editorial

Board for the UCC (which is composed of NCCUSL members and members of the American Law Institute) has supervised changes to the UCC when, for example, new commercial practices have made additional UCC provisions desirable.

The adoption of Article 4A is the culmination of a project begun in 1977 to revise the payment provisions of the present UCC (i.e., Articles 3 and 4). The initial drafting effort produced a document known as the Uniform New Payments Code which was designed to cover all types of payments (check, credit card, wholesale wire transfer, etc.) under one uniform set of rules. This work was criticized by the banking industry and due to the efforts of the American Bankers Association, among others, the New Payments Code approach was eventually dropped.

In late 1985 a new committee was organized to draft less sweeping changes to present Articles 3 and 4 of the UCC and to develop a new Article to govern wholesale funds transfers. The drafting committee was composed of Uniform Law Commissioners, academics, and advisors from the banking, legal, regulatory and corporate communities. During the past three years numerous meetings on Article 4A were held by the drafting committee as well as other groups such as the American Bankers and American Bar Associations.

Project Review

The American Bankers Association's response to the 4A effort has been coordinated through the work of the Ad Hoc Payment Systems Laws Task Force. This task force is composed of bank operations experts and bank counsel appointed by former Association President Mark Olson in 1987. In addition, W. Robert Moore, Senior Vice President (retired) Chemical Bank of New York and Thomas J. Greco, Associate General Counsel in the ABA's Office of the General Counsel, served as the Association's advisors to the NCCUSL drafting committee and participated in most of that group's meetings.

Bankers and bank counsel had numerous opportunities to review and comment on the various drafts of Article 4A. For example, two meetings were held specifically to generate comments to earlier versions of 4A. On December 3, 1987 the American Bankers Association, along with the Association of Reserve City Bankers, the Bank Administration Institute and the New York Clearing House Association jointly sponsored a one-day forum on 4A. Over two hundred bankers and bank counsel attended the forum, and the comments received were incorporated into the task force's January 29, 1988 report to the NCCUSL drafting committee. On October 18, 1988 the task force met with bankers and counsel who were directly involved in the drafting process in order to achieve an industry consensus on several open issues. In addition to these meetings numerous drafts have been distributed to various ABA committees and to individual bankers throughout the drafting process.

### Provisions of Article 4A

Two major interest groups participated in the drafting of Article 4A, the banking industry and the corporate users of funds transfers. The final version of 4A reflects the compromises which were necessary to achieve the support of both groups and, consequently, neither side is entirely satisfied with each and every provision of the proposed law. The remainder of this section highlights the public benefits of 4A and notes the advantages and disadvantages of 4A from the banking industry's perspective.

### Public Benefits

One of the key public benefits of Article 4A is that it creates a uniform body of law governing the rights and obligations of participants in a funds transfer. The interconnected nature of the funds transfer system requires that the basic rules underlying the system be the same for all participants. Of course, 4A permits a degree of flexibility by allowing many provisions to be varied by agreement in order to accommodate the needs of different users and providers of funds transfer services.

The public also gains from the certainty created by 4A. One by-product of such certainty is the ability to identify which party to a funds transfer is liable when a transfer is mishandled or when payments are not completed due to the insolvency of a participant in the transfer. This, in turn, permits parties to implement procedures to

control risk. This factor is particularly significant given the Federal Reserve Board's concern for reducing risk (i.e., insolvency risk) in the payments system.

Another advantage of Article 4A is that it has been drafted to accommodate such features as speed, low cost and reliability. It is these features which have made wholesale funds transfers such an attractive form of payment. For example, 4A's rules on discrepancies in a payment order between identifying numbers and name promotes the use of automation, which both increases processing speed and keeps costs low. The Article's rules governing liability for erroneous execution encourage operational practices which ensure reliability by penalizing the party responsible for the error.

#### Benefits to the Banking Industry

In addition to the benefits from uniformity and certainty described above, perhaps the single greatest advantage of Article 4A over current law is 4A's treatment of the consequential damages issue. Banks which fail to complete (or to complete in a timely fashion) a funds transfer are typically sued in lawsuits which allege that the banks' actions caused damages far in excess of the amount of the transfers. While no reported decision has ever awarded such damages, one of the leading cases in this area (Evra Corporation v. Swiss Bank Corporation) has been interpreted by some practitioners as permitting consequential damages. Article 4A resolves this issue by prohibiting recovery of consequential damages

for late or improper execution of a funds transfer except where the bank has expressly agreed in writing to undertake such liability.

Another troublesome situation for banks addressed by 4A is the problem of name and account number discrepancies in payment orders. The issue often arises in the context of a fraud committed on a bank which is misled into believing that it is sending funds on the behalf of its customer to the customer's account with another bank. Unfortunately, the account number is for the account of the malefactor, not the customer, but the bank receiving the funds does not recognize any discrepancy because it acts on the payment order solely on the basis of the account number. Article 4A resolves such disputes by providing, generally, that the bank receiving the payment order may pay the person identified by the account number and has no duty to determine whether the name and number refer to the same person.

Finally, 4A establishes a relatively short one-year period in which a customer must notify its bank of unauthorized transfers from its account. Failure to raise objection to a transfer within one-year after the customer receives notice of the transfer bars subsequent assertions that the transfer was not proper.

#### Disadvantages to Banks

While "disadvantages" may be too strong a term, there is no question that Article 4A establishes rules that may be less

favorable than present common law or the agreements that banks have been able to obtain from some of their customers. One of the more controversial issues during the drafting process was the treatment of the "interloper fraud" issue.

This issue arises in the context of Article 4A's provisions on authorized and unauthorized payment orders. As a general rule, a bank's customer is only bound by its authorized payment orders. 4A also states, however, that payment orders verified by a "commercially reasonable security procedure" will be binding on the customer. (4A's provisions on commercially reasonable security measures and verified payment orders are, on the whole, very beneficial to both users and providers of funds transfers.) The "interloper" situation occurs when the security procedure is somehow breached (through no fault of the customer or the bank) and the order is verified. If the customer is able to prove that the unauthorized (but verified) order was not caused by a person the customer entrusted to send its payment order or by a person who obtained, from the customer, the information needed to breach the security procedure, then the bank will ultimately be liable for the loss.

Another aspect of 4A which favors users over providers of funds transfer services is the Article's so called "money-back guarantee" rule. Article 4A provides that the sender of a payment order is not required to pay the order if the order is not accepted by the beneficiary's bank. This could expose a bank to insolvency risk if,

for example, an intermediary bank in a funds transfer fails and the customer must be refunded (because the transfer was not completed) but the customer's bank is unable to get its own funds from the failed institution.

A somewhat related rule applies to payment to the beneficiary and gives rise to similar concerns regarding insolvency risk. As a general rule Article 4A prohibits the beneficiary's bank from recovering funds once they are paid to the beneficiary. Therefore, a bank which permits its customer to use funds from a funds transfer before the bank itself receives payment assumes the risk in the event that the order is not paid. There are two exceptions to this rule. The first, intended to address transfers conducted through the Automated Clearing House system, would permit a funds transfer system rule to provide that funds transfers through the system are provisional until the beneficiary's bank receives payment. The second addresses transfers through a system (such as the one envisioned for CHIPS) which multilaterally nets participants' obligations and has a loss sharing agreement in place to complete settlement if one or more participants fail to settle. If, despite such loss sharing rules, the system is unable to settle, then the beneficiary's bank would be able to recover payments from the beneficiary.

### Conclusion

The task force believes that 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. Article 4A represents a concerted effort by the Uniform Law Commissioners, the providers of funds transfer services and the corporate users of the system to draft uniform rules which equitably balance the interests of the affected parties. The banking community was afforded the opportunity to participate in the drafting of 4A and, while not all of the issues were resolved in the manner that banking might have wished, the proposed Article represents a considerable improvement over the present state of the law.

The task force urges the Board of Directors to consider the points raised in the task force report and vote in favor of the attached resolution.

# THE NATIONAL LAW JOURNAL

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## Big-Buck Transfers A Big Risk

The law tries to catch  
up with technology.

BY MARCA COYLE

National Law Journal Staff Reporter

TAKE A COOL half-billion dollars. Through the miracle of electronic wizardry, zip it from your bank account in Dallas to another account in Zurich — and pray that nothing goes wrong.

If prayers fail, prepare to enter the twilight zone of rights and liabilities, where technology has outpaced law, and law is scrambling to catch up.

The denizens of this uncomfortable twilight zone are big banks, big corpo-

rations, big bucks and big risks.

For nearly four years, a committee of the Uniform Law Commissioners, in conjunction with the American Law Institute, has been working feverishly to end the legal ambiguities surrounding so-called wholesale wire transfers, a particular way of making a dollar payment. That effort — expected to produce a new article to the Uniform Commercial Code — has often involved an intense battle between banking and corporate interests.

There is no comprehensive body of law governing wholesale wire transfers, as currently exists for checks and other types of payments, and the financial fallout can be enormous when errors occur. The average transfer — typically between banks and their corporate customers — is \$5 million, and total daily transfers now average more than \$1 trillion.

"When you look at the amount of money moving, it's striking that there are no backstop rules," says one bank lawyer. "People are transferring the net worth of their companies routinely and relying on private agreements with their banks, or no agreements at all."

### Risky Business

The wholesale wire transfer is basically a very simple transaction, says Prof. Robert L. Jordan of the University of California at Los Angeles School of Law, reporter for the ULC drafting committee. If, for example, someone in Los Angeles wants to make a payment to someone in New York, he simply tells his Los Angeles bank to send the money to the other person's bank account in New York, explains the professor. By electronic transfer, the Los Angeles bank sends the payment order to the New York bank, which then credits the amount to the account of the so-called beneficiary — often before the money arrives from L.A.

Small-business users pick up the phone, call their bank and use a code word for authentication to order payment. Large corporate users, such as oil companies that engage in "Star Wars"-like transfers, may be so sophisticated that their computers talk to their banks, adds Thomas Baxter, associate general counsel of the Federal Reserve Bank of New York.

"You really have a spectrum of use," says Mr. Baxter, who, along with the American Bar Association and others, has been advising and monitoring the ULC effort. "In the middle of all this, you have banks debiting accounts of senders and crediting the banks of receivers. We accomplish this by the wonders of technology."

Wholesale wire transfers generally travel over two payment systems — the Fed Wire, operated by the Federal Reserve System, and CHIPS, the Clearing House Interbank Payments System in New York, the largest and only competitor to the Fed Wire. Another system — SWIFT — ties the U.S. systems with other international funds-transfer systems.

Although CHIPS and the Fed Wire have rules and regulations governing certain aspects of interbank transfers among their members, there are no rules governing the entire transaction — beginning with the so-called originator, who initiates a payment order, and ending with the so-called beneficiary, who gets paid.

Some banks and corporate users rely on private agreements to apportion risks if something goes wrong. "But there has been difficulty getting these agreements," says Mr. Baxter. "It also became clear over time that the rights of third parties could be affected by those agreements."

For example, he adds, what if there is a third-party intermediary bank in the transaction and it fails to settle, i.e., pay the balance? "Neither the originator nor the beneficiary may have se-

lected that bank," he explains. "Who bears the loss?"

There never has been a failure on the CHIPS system, says general counsel Norman Nelson, but that does not mean the clearinghouse is ignoring the potential for one. Although working with the ULC to draft a uniform law, CHIPS also has been working independently to ensure so-called settlement finality, he says.

"If a bank is unable to pay the balance, we're looking at having all other participants to the agreement pay pro rata to make sure the system will settle," Mr. Nelson explains.

CHIPS has 140 participants, international banks with offices in New York through which funds are transferred. "Our record day was the day after Memorial Day when we moved \$1.25 trillion," says Mr. Nelson. "On a normal day, we move \$600 billion to \$700 billion."



**DIFFICULT:** Washington attorney Carlyle C. Ring Jr. says it's difficult to work out uniform wire transfer laws.

Established in 1970, CHIPS, he says, has "grown and grown and grown," as has the entire wholesale wire transfer system. "The main thing now is to get a comprehensive body of law."

Commercial lawyers and others close to the wire-transfer field estimate that 90 percent of these transfers are now done without agreements covering rights and obligations.

#### Computer-Age Growth

Wire transfers have existed for many years, says ULC reporter Professor Jordan, but the volume of money moved has grown dramatically in the past two decades. One major reason for the increase in the number of wholesale wire transfers and their amounts is the arrival of computers, he explains.

Before the computer age, transfers were made on a more primitive basis, such as by paper-fed telex machines, recalls Professor Jordan.

"Along with the computer, there has grown up a whole new profession of cash managers who make sure that business is always using its money so it is earning money," he adds. "The ability to move instantly large sums of money from one part of the world to another has increased the volume of transfers.

"And the potential liability of banks has grown also, to the point where they have become very uncomfortable with the lack of any body of law governing what happens when something goes wrong."

The wholesale wire transfer, says Professor Jordan, is a system based on speed and low cost. The liability question for banks is very important, he explains, adding, "If you load up the liabilities, the costs will be greater."

Some of the financial land mines in the wholesale wire transfer are also a product of the new technology.

"There is now great danger that a computer hacker could get on the line, intercept a payment message and

change the beneficiary," says Professor Jordan. "Unauthorized messages also present great potential for fraud."

There also are potential bank insolvency problems, he adds. In many cases, the beneficiary bank pays the beneficiary before it gets the money from the originator bank, he explains. It is customary then for the beneficiary to immediately withdraw the money.

"If the originator bank becomes insolvent, the beneficiary bank has a problem and it's not clear whether the beneficiary bank can get its money back from the beneficiary," he says.

And then there are transfers involving multiple transactions, says Professor Jordan. "What happens if there is a large bank failure? It could set off a chain reaction of other banks failing because of the enormous sums of money they are dealing with."

When errors occur and banks and their corporate users find themselves in litigation, he says, the courts "have to make up the law as they go along."

Court decisions have been unsatisfactory, according to the professor, because courts must fall back on ordinary negligence rules or analogize the situation to problems involving the more traditional check.

"The rules governing payment by check don't always apply," he explains.

Mr. Baxter agrees, noting that in a check transfer, the authentication device is the signature of the drawer. "In the wire transfer world, we don't have any signature. We're getting into an area where the law is not that sophisticated. Payment law is built around the signature. Now we have to think about new alternatives."

#### Growing Pains

For the past four decades, the Uniform Commercial Code has been the "premiere product" of the ULC, a confederation of state commissioners on uniform laws, says Carlyle C. Ring Jr., of counsel to Washington, D.C.'s Ober, Kaler, Grimes & Shriver. But it was getting rapidly out of date, he adds.

Ten years ago, he recalls, the permanent editorial board of the UCC appointed a committee to look at whether the commercial code needed to be revised because of electronic developments. The committee launched an ambitious effort to draft a comprehensive payment code covering checks, wholesale wire transfers and other

payment instruments.

"The committee got into trouble because it was trying to do too much," explains Mr. Ring, a UCC board member. "Consumer groups and banks were not happy at all."

In 1986, the project was scaled down to focus only on wholesale wire transfers. "Uniform laws have been successful where we've been able to get the various interest groups together," says Mr. Ring. "When we step into an area of strong policy disagreement, it's very difficult to achieve uniformity."

If the uniform law effort fails to address the changing technology, he adds, the federal government will preempt the field. Pressures driving the modernization move, he says, include the Federal Reserve System's concern about major bank failures given the uncertainty over rights and liabilities, banks' anxiety over how they fare in the courts when problems occur and corporate users' demands for fair rules.

When the wholesale wire transfer project began three years ago, Mr. Ring, who is co-chairman of the ULC drafting committee, was in private practice. "My role was to be a neutral facilitator, to keep it on track." Today, still co-chairman, he is also general counsel and vice president of Atlantic Research Corp., a corporate user.

After roughly 12 drafts, proposed Article 4A, governing wholesale wire transfers, has the support of the banking and corporate communities and the Federal Reserve System, according to Mr. Ring, who calls the article "basically a safety net." It will not apply to consumer transactions, which continue to be governed by the federal Electronic Fund Transfer Act.

#### A 'Hard Fight'

But bringing those three groups together was neither easy nor pleasant, says Arthur L. Herold of Washington, D.C.'s Webster, Chamberlain & Bean.

Mr. Herold is not a member of the drafting committee, but he does represent the National Corporate Cash Management Association, an organization of corporate treasury officers. The cor-

porate community, he recalls, was not aware of the 4A movement until about a year after the drafting committee began work.

During that year, he and colleagues from Exxon, Shell Oil Co., Kidder Peabody and Sears, Roebuck and Co., attended drafting meetings where, he says, "We were treated as outsiders, shouted down and outvoted."

Throughout 1988, he recalls, his association built a coalition of the oil companies, insurance and railroad industries, and retailers to increase its "voice" at the drafting sessions.

"We felt 4A was being bank-driven," Mr. Herold says. "We don't object to a 4A that equitably distributes risks, but if the rules aren't fair, we'd rather take our chances in the courts."

"We told the committee if they wanted corporate support, they would have



**ACTIVE:** Thomas Baxter is associate general counsel of the Federal Reserve Bank of New York.

to begin to accommodate our concerns, and if they didn't care, we would have to vigorously oppose enactment of 4A in the states. That tended to get their attention."

Mr. Herold called the effort a "hard fight" that became unnecessarily hostile and personal at times. His association has taken a neutral position on Article 4A even though an internal vote showed more members would support it than oppose it. "We felt the members should feel free to express their own feelings," he says.

But whether Article 4A ultimately will be equitable or will impose significant risks on the corporate community, Mr. Herold says, is still unknown.

"The banks are free from a lot of risk," he adds. "Banks don't like having no law and don't like the current common law. If anyone has a worse reputation with juries than big corporations, it's banks. The banks felt it was better to play with rules than without, and they basically wrote the rules."

But Mr. Herold and others involved in the drafting process credit Professor Jordan for pulling the disparate interests together. "He's a special per-

son," says Mr. Herold. "We had great confidence in his fairness. Without him, I don't think this would ever have been done."

Article 4A, says Professor Jordan, tries to provide more certain rules for these transfers and to reduce the possibility of litigation. "It represents compromises and trade-offs," he explains. "We think we've come up with a fairly well-balanced statute for allocating risks and liabilities."

#### Into the States

The proposed Article 4A already has been approved by the American Law Institute. Following ULC approval, the next step will be to win enactment in state legislatures, says Mr. Ring.

"Our goal is to pick up four or five big banking states — New York, California, Texas, Illinois, Georgia and Massachusetts — and then the remaining states, we think, will move quickly," he says. "The rest will want to act rapidly to preserve banking business for themselves and because the courts probably will adopt the rules of 4A even before the legislatures act."

Taking the uniform law route is often time-consuming, notes Mr. Ring, adding there was considerable debate about whether new rules should be enacted instead at the federal level.

"But the federal government and the other parties are willing to give us a chance to use the prestige of the UCC to get these rules adopted," he says.

There has been historical deference to state development of commercial law, he explains. The Federal Reserve, he adds, is reluctant to take on new and substantial regulation. And Congress, he says, has become "such a grab bag" that the banking and corporate communities feared legislation could become enmeshed in extraneous issues.

Most uniform laws, Mr. Ring says, draw on experiments in states or other nations. But Article 4A, he adds, did not fit the pattern. England, Japan and the United Nations are looking to the ULC for guidance on similar projects.

"We're not looking at any models because there are none," he says. "As a matter of fact, we're ahead of the rest of the world."

## *Early Warning*

**O**NE OF THE BEST and worst aspects of the law is the speed with which it changes. A slow, deliberate pace of legislative enactments produces the most error-free laws. And the doctrine of *stare decisis* — by which courts generally adhere to decided cases — helps to guarantee stability in the law.

But none of this is helpful in confronting the megaleaps of today's technology, and nowhere is this more apparent than in computers, banking and high finance.

In an era when trillions of dollars move across state and international borders in electronic blips, the law has failed to keep pace. Eventually mistakes, even big ones that could cause banks to fail, are bound to occur. There is currently no comprehensive body of law that will help lawyers and the courts unscramble the ensuing mess. As one bank lawyer noted, "When you look at the amount of money moving, it's striking that there are no backstop rules. People are transferring the net worth of their companies routinely and relying on private agreements with their banks, or no agreements at all."

For the past 3½ years, one group — the Uniform Law Commissioners — has been drafting a model law that tries to apportion risks and liability fairly when problems arise in these multibillion-dollar wire transfers. The ULC, bringing to the process its unique approach to building consensus, apparently has succeeded in gathering together such disparate interests as the nation's banking community, corporate users and the federal government.

But the ULC's effort is just the first step toward bringing the law into the 21st century of finance. The real challenge rests with the states. If fairness and certainty — the two primary goals of the model law — are to govern, the states must move quickly to enact this model legislation. For the entire legal profession — from bar groups to legislators — the ULC effort should serve as one more lesson on the need for early warning systems to detect and confront changes in the law mandated by rapidly changing technology.

# Business and the Law | Stephen Labaton

## States to Regulate Money Transfers

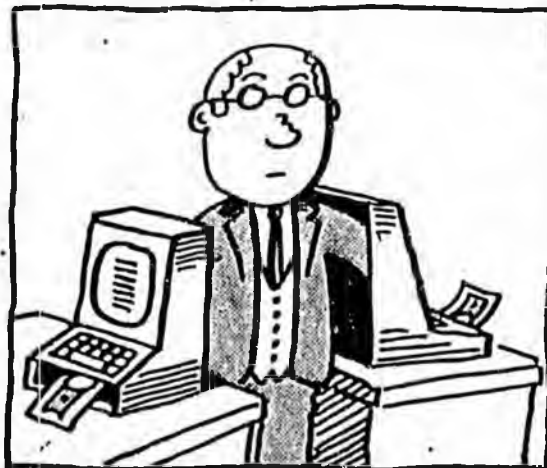
**T**HE sweeping set of regulations for commercial transactions is about to get the most significant addition in decades.

The Uniform Commercial Code is the law in all states except Louisiana and governs everything from checks to the sale of all goods of more than \$500. Despite its broad scope, the Code has failed to keep pace with technology: It does not address the electronic transfer of money among banks, a process that has grown in recent times more than 20 percent a year.

But that is about to change. Within the coming months, a new chapter is expected to be adopted by several large states that will for the first time regulate the computerized transfer of funds between banks. Businesses and banks now move more than \$1 trillion a day electronically without any clear guidelines about what happens if someone goof. The average transfer is \$5 million.

As a practical matter, the courts have tended to define the liabilities and rights of businesses who use the system in terms of contract law. Yet lawyers and banks say only a small percentage of those businesses have signed any contracts with the banks or other businesses on the transfer of funds.

In a typical transfer, the computer of a corporate customer notifies the computer of a bank, which then forwards the information about the transfer to a clearinghouse's computer. It, in turn, notifies the computer of the receiving bank to credit the account of the intended beneficiary of the funds.



Stuart Goldenberg

While the clearinghouses have their own sets of rules, no established laws govern the relationship between the sender and receiver of money. As a result, it is left uncertain who bears the loss for a glitch in the system, a mistake in the transaction, an unauthorized transfer or the meddling of a computer hacker. In many of the dozens of cases that have cropped up, courts have had to draw imprecise analogies to other provisions of the code that do not directly speak to the issue of computer transfers.

A four-year effort to draft the new chapter, known as Article 4A, has recently been completed and legislators say it will soon be introduced in New York, California, Massachusetts, Connecticut, Virginia and West Virginia. With the support of the American Bankers Association and the expected approval soon of the American Bar Association, some legislators in New York and California say the chapter will likely be approved by the summer.

"It will bring a substantial amount of certainty to these kinds of transactions," said Carlyle C. Ring Jr., a co-chairman of the committee that wrote the new rules. "No one really knew in the event of a mishap what would happen. And since such a large amount of money is being transmitted, there is a substantial incentive to litigate these issues."

The draft was completed by the National Conference of Commissioners on Uniform State Laws, the organization that drafted the code more than 30 years ago. The nonprofit organization consists of lawyers, judges and academics, many of whom are selected as commissioners by state governors.

Like the other sections of the code, Article 4A will operate as a safety net. It will enable the banks and businesses in most instances to write contracts that differ from the Code. It would generally be applicable in those instances in which there are no contracts or when the contracts are ambiguous.

By adopting Article 4A, the states will enter an area of regulation in which the Treasury Department has also announced its intention to intervene. Earlier this year, the Bush Administration said that to combat the use of the electronic transferring system to launder money to avoid taxes and evade narcotics laws, Treasury regulations would be adopted to make it easier to trace the flow of money through the banking system.

One rule will require that the banks that send and receive transfers keep records, including the name and account of the customer transmitting and receiving the funds. Another rule would require that financial institutions receive more information about the nature of the business of a customer who makes use of international transfers. The Treasury guidelines, which do not appear to pre-empt any move by the states, are expected to go into effect this spring.

# Wholesale Funds Transfers

## *New Article 4A to the UCC*



by Carlyle C. Ring Jr.

**F**ive years ago the National Conference of Commissioners on Uniform State Laws (NCCUSL) and the American Law Institute (ALI) began a project to develop a new Article to the Uniform Commercial Code (UCC) to cover wholesale wire transfers.

The UCC is a legal framework adopted by states to govern the legal aspects of business and financial transactions in the United States. Its purpose is, as the name implies, to provide a single, uniform set of rules for business to follow.

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*The author is vice president and general counsel for Atlantic Research Corporation in Alexandria, Virginia. Mr. Ring also chaired the Article 4A Drafting Committee.*

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In consultation with bankers and the New York Clearing House, it was determined that comprehensive uniform rules for funds transfers were necessary and desirable. Since most payments are covered by state law under UCC Articles 3 and 4, it was deemed appropriate to draft a UCC amendment.

Article 4A has been approved by NCCUSL and the ALI, and has now been endorsed by the American Bar Association.

Article 4A provides the first comprehensive rules for the rapidly growing wholesale funds transfers, which now average more than \$1 trillion daily, with peak days over \$2 trillion. The total funds transfers daily is many times greater than the total for all checks, debit and credit cards together. Yet there is no set of comprehensive rules governing the responsibilities, obligations and liabilities in

the event of error, mistake, fraud, intervention, or insolvency. It is estimated that, in dollar amounts, less than 10 percent of the transactions are governed by contracts between the parties.

While Federal Reserve rules cover the interbank portion of the Fedwire transactions and the CHIPS rules cover the interbank relationships for that system, there is no set of rules covering the funds transfer from the originator through the banking system to the beneficiary. Article 4A fills that void.

A typical funds transfer is illustrated by the following flow chart.

A "payment order" is an instruction of a sender to a receiving bank to pay or cause another bank to pay a beneficiary. In the flow chart shown there are three payment orders: Niagara to Buffalo Bank; Buffalo Bank to Gotham Bank; and Gotham



Execution occurs when the receiving bank issues a payment order intended to carry out the first payment order it received.

A beneficiary's bank accepts a payment order at the earliest of the following times: when it pays the beneficiary; when it notifies the beneficiary of the receipt of the order for the credit to its account (unless this bank states the credit is not available until it receives payment from its sender); when it receives payment by receipt of final settlement; or at the opening of the next funds transfer business day unless the order is rejected within one hour after the opening of business. When the beneficiary bank accepts the payment order, the underlying obligation between the originator and the beneficiary is discharged.

*Unauthorized Payment Orders* — One of the key issues addressed by

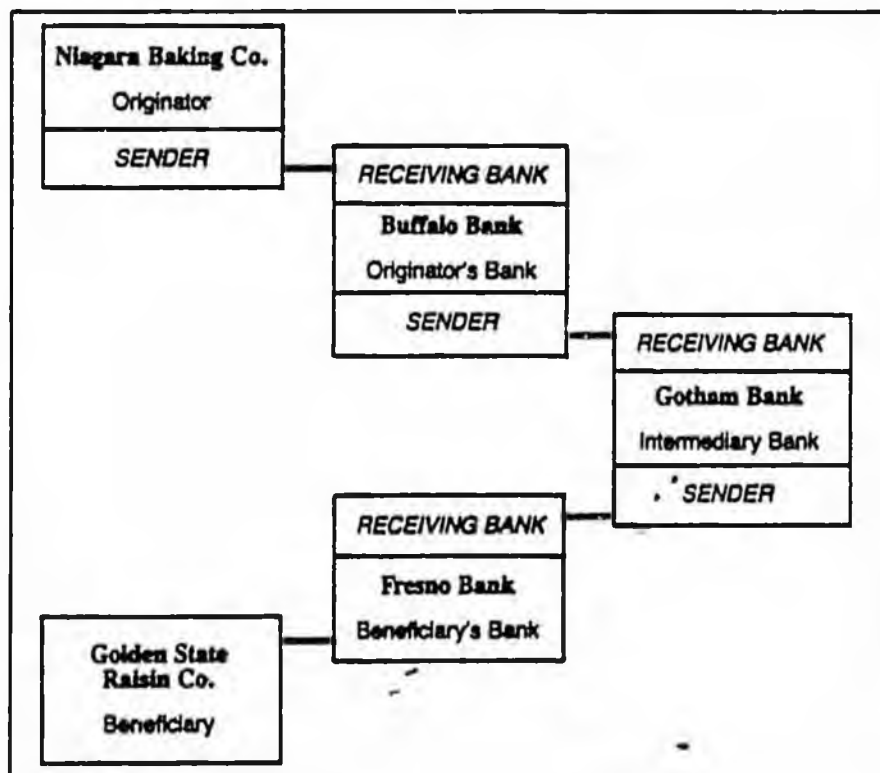
Article 4A is who is responsible for an unauthorized payment order. In effect, Article 4A requires the bank to provide a "commercially reasonable security procedure." "Commercially reasonable" is a question of law (to be decided by the court), taking into account: the wishes of the customer expressed to the bank; the circumstances of the customer known to the bank, including the size, type, and the frequency of the payment orders normally issued by the customer; alternative security procedures issued to the customer; and security procedures in general used by customers in similarly situated receiving banks.

If the bank has complied with the security procedure and written instructions of the customer in good faith, the loss for an unauthorized order falls on the customer, unless the customer proves that his shop was clean. If the customer meets that burden (a pure interloper case), the loss falls on the bank.

Bank to Fresno Bank. A "funds transfer" means a series of transactions, for the purpose of making payment to a beneficiary, beginning with an originator's payment order and ending when the beneficiary bank accepts a payment order.

Article 4A covers wholesale funds transfers, including Fedwires, CHIPS, book transfers, and non-consumer ACH credit transfers. It does not pertain to unconditional payment orders transmitted through the banking system and it excludes consumer transactions (e.g. consumer ACH, credit cards, POS), all debit transfers, conditional orders (e.g. payment against release of documents under letters of credit), and transfers outside the banking system (e.g. Western Union).

A payment order is effected when accepted by the receiving bank, generally through execution of the order.



### **Authorized but Erroneous Orders -**

When a receiving bank accepts an order, it undertakes a duty to properly execute the sender's payment order. That duty is to issue a "payment order complying with the sender's order," which generally covers the amount, beneficiary, and the beneficiary's bank, but may cover the intermediary bank(s), the funds transfer system, the manner of transmission and the time for action. Improper execution may involve errors in amount, wrong beneficiary or wrong beneficiary's bank.

Under Article 4A the bank is obligated to correct such errors and reimburse the originator for expenses in the transfer, incidental expenses and interest losses resulting from the improper execution, but no consequential damages unless there is an "express written contract" covering such damages. Article 4A also imposes a statute of repose of one year.

A more comprehensive summary of Article 4A will be shortly published in the *Business Lawyer* of the ABA.

### **General Benefits**

In summary, Article 4A has the following general benefits to both banks and customers:

- Certainty of result, including ability to assess risks for a cost-benefit analysis in avoidance of litigation;
- Backstop rules filling the gaps in funds transfer agreements and legal framework when agreements cannot be obtained;
- Comprehensive coverage including matters not covered by agreements or system rules, such as discharge of the originator's underlying obligation and limitation of consequential damages;

- Uniformity for the treatment of all funds transfers and standardized terms.

### **Benefits for Banks**

The following are some provisions in 4A that are of particular benefit to banks:

- Banks may rely on an identifying number in the event of names/identifying number inconsistencies;
- Limitation on damages, especially consequential damage recovery;
- Duty of the customer to discover and report unauthorized transfers and erroneous transfers; preclusion to object to debit to account after one year;
- Recognition of multilateral net settlement;
- Right of recovery of CHIPS/ACH payments in the event of settlement failure;
- Right to deduct charges from payment orders.

### **Customer Benefits**

For customers, 4A provides the following benefits:

- Customer is not liable for "interloper fraud";
- Customer has "money-back guarantee" in the event the transfer is not consummated;
- Customer has right to negotiate for increased liability of the banks, although the bank liability generally cannot be reduced;
- Finality of payment;
- Discharge of underlying obligation.

Article 4A has passed in Virginia. It has already been introduced into a number of other state legislatures, but

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If the bank has complied with the security procedure and written instructions of the customer in good faith, the loss for an unauthorized order falls on the customer.

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of particular importance is New York and California.

It is highly probable that Article 4A will be enacted in both states in 1990, and will become effective in 1991. The choice of law provision permits a funds transfer system to select the law of a particular state to govern transactions through its system. It would be anticipated that CHIPS and Fedwire would by rule choose the law of New York and/or California, once New York and/or California enact Article 4A.

While such action by funds transfer systems would not necessarily remove all uncertainty of the choice of law, for all practical purposes the choice of 4A by the principal funds transfer systems would establish substantially uniform rules throughout the country as well as most international payments as well.

Prompt adoption of 4A by all 50 states, however, is essential to assure certainty and uniformity of the law. Such uniformity is an absolute necessity for funds transfers which involve such huge sums of money that move so quickly, and to preserve the speed, reliability and security of this payment system. **T**

## Sending Large Dollars

# U.C.C. Article 4A to Provide Safety Net

Funds transferred by check amount to millions and millions of dollars each year. The legal rules for the check system, although recently somewhat shaken up by federal legislation and regulation CC, basically are well established. Funds transferred by electronic means, including FedWire (operated by the Federal Reserve System) and CHIPS (a funds transfer system operated by the New York Clearing House), often exceed \$2 trillion a day. Yet any resulting problems are resolved only to a limited extent by regulation J for FedWire, a few published cases, the Electronic Funds Transfer Act and regulation E for some consumer aspects, and in some cases by the agreements of the parties. In short, the transfers involving the really large dollars, and the most risk if the transfer goes awry, have the least settled guidelines for conduct and for resolving disputes. Uniform Commercial Code article 4A, the U.C.C.'s newest, will fill this void.

As part of the U.C.C., article 4A is the product of the National Conference of Commissioners on Uniform State Laws ("NCCUSL") and the American Law Institute ("ALI"). The drafting committee also was assisted by two Reporters, whose role was to advise the members of the drafting committee as to the pertinent legal issues and what law exists to resolve those issues, and to embody the decisions of the drafting committee in proper statutory form with comments to elaborate on the meaning of the statute. In addition, a number of advisers from the Federal Reserve System, the banking industry, and the businesses that use funds transfers (including banks) worked with the drafting committee. The American Bar Association also appointed an adviser to the drafting committee from the Business Law Section, and members of the Section's Ad Hoc Committee on Payment Systems and its U.C.C. Committee scrutinized and commented on drafts prepared by the drafting committee.

Preparation of article 4A took almost three years. The new article was approved by the ALI at its annual meeting in May 1989 and by NCCUSL at its annual meeting in July-August 1989. Final approval by the ALI is anticipated in December at the latest.

The Council of the Business Law Sec-

tion has tentatively decided to recommend ABA approval of article 4A when requested by NCCUSL and the ALI. Thus article 4A is ready for enactment by the state legislatures. A number of key commercial states are expected to introduce it soon. Expeditious enactment is contemplated because of the recognized need for greater legal certainty in the governing rules, the general support for article 4A by the interests involved in funds transfers, and the expressed concern of the Federal Reserve System that, unless the states address the significant issues involved in these types of transfers, federal law may become necessary to avoid unacceptable risks to the payment system.

### **Funds transfers under article 4A**

Article 4A creates a series of rules to govern the resolution of legal issues that may arise out of funds transfers. The effect of these rules, like most of those in the U.C.C., may be varied by the agreements of the parties and operating rules of a funds transfer system, with some specific exceptions necessary to protect fundamental policy choices that should not be subject to variance due to fortuitous circumstances of a particular bargain (U.C.C. § 4A-501; *see also* § 4A-107). The ability to vary the effect of the statutory rules allows flexibility and development of new methods, but at the same time, the statutory rules stand as a "safety net" to resolve matters upon which the parties either do not or cannot agree.

Under article 4A, a "funds transfer" (§ 4A-104(1)) is the payment order (§ 4A-103(1)) or series of payment orders by which an originator (§ 4A-104(2)) accomplishes payment to the beneficiary (§ 4A-103(6)) of the originator's order. It can be a very simple transaction in which a corporate originator orders its bank to debit one of its accounts and credit an account of another party at the same bank. In this instance the funds transfer and the payment order are co-extensive. If the originator instructs its bank ("originator's bank"—§ 4A-104(3)) to pay a beneficiary that is a customer of another bank, however, that payment order will require the originator's bank, in turn, to issue at least another payment order, perhaps to the beneficiary's bank directly, perhaps over

a funds transfer system like FedWire or CHIPS (§ 4A-105(1)(e)), or perhaps to an intermediary bank (§ 4A-104)) that will then issue another order to the beneficiary's bank (§ 4A-103(7)).

Payment orders, unlike checks, do not embody independent rights and liabilities for the payment of money. Rather, the rights and liabilities of the parties to a payment order arise out of the contract formed, generally subject to article 4A and any agreement of the parties, when the payment order is accepted by the receiving bank (§ 4A-103(5)). Apart from contract outside article 4A, a bank has no duty under article 4A to accept a payment order (§ 4A-209). A receiving bank other than the beneficiary's bank accepts a payment order if it executes it (§ 4A-209(1)), and need not reject those orders it does not accept, unless otherwise provided by agreement or the receiving bank had sufficient funds of the sender on hand to cover the order (§§ 4A-210(2), 4A-212).

A receiving bank that accepts a payment order and that is not the beneficiary's bank is obliged to issue a payment order complying with the order of the sender (§ 4A-103(4)) that it accepted and generally to follow any instructions as to routing and method (§ 4A-302). If the resulting payment order does not comply, the sender is not responsible for the error and need not pay the bank other than to the extent of proper execution (§ 4A-303) but, upon learning of improper execution, may have a duty to notify the bank of that fact (§ 4A-304). Indeed, if a funds transfer is not completed by acceptance by the beneficiary's bank of a payment order instructing payment to the beneficiary in accordance with the sender's order, the sender is not obligated to pay for its order, or is entitled to its money back (§ 4A-402(3), (4)).

A beneficiary's bank may accept a payment order in a variety of ways, such as by paying or notifying the beneficiary, and acceptance also may occur when the bank receives payment of the sender's order (§ 4A-403) or by the passage of time if the amount of the sender's order is fully covered by a withdrawable credit balance (§ 4A-209(2)). Acceptance of the order entitles the bank to payment by the sender (§ 4A-402(2)) and generally obliges it to pay the amount of the order to the beneficiary (§§ 4A-404, 4A-405). Failure to do so and to give notice of the receipt of the order may subject the bank to liability. If the beneficiary's bank ac-

cepts the order, generally at this point the debt of the originator to the beneficiary for which the order was issued is discharged (§ 4A-406).

#### Scope of article 4A

A payment order can be oral, in writing, or electronic. Like a check, a payment order is an unconditional (except as to timing) instruction to pay a fixed or determinable amount of money to a beneficiary (§ 4A-103(1)). However, a check is not a payment order because a payment order must be transmitted by the sender, not to the payee, but directly to the receiving bank or to an agent, funds transfer system, or communication system for transmittal to the receiving bank

part of which is governed by the Electronic Funds Transfer Act and its implementing regulation E, which protect consumer rights, is excluded from article 4A to avoid conflicting rules (§ 4A-108). However, a consumer purpose transfer over FedWire, for example, outside of the scope of the federal law could be subject to article 4A.

#### Salient aspects of article 4A

Three matters in particular are presently a source of litigation concerning funds transfers. These are: responsibility for unauthorized and erroneous orders, liability for damages caused by orders that are improperly executed, and finality of payment. For discussions of the litigation,

and the bank complied with any instructions of the customer as to a proper account to debit and the like, even an unauthorized order will be effective (§ 4A-202). There is one exception. Even if the order passed an appropriate security procedure, the customer will not bear the loss if the customer proves the order is not attributable to any cause related to the customer's operation (the interloper situation) (§ 4A-203). However, the customer may lose interest owed on any refundable amounts if it does not use ordinary care to detect any unauthorized orders and notify the bank (§ 4A-204).

Payment orders erroneous as to beneficiary, bank, time, amount, or duplicate orders caused by the sender are the sender's responsibility (§ 4A-303). However, such orders only bind the sender as to the intended beneficiary and amount if a security procedure for the detection of error was in effect and the sender complied with it but the bank did not (§ 4A-201). However, again the sender has a duty of ordinary care to discover and report an error (§ 4A-205). A funds transfer or third party communications system to which an order is first transmitted is the agent of the sender; any error made by it is attributed to the sender (§ 4A-206).

Often in fraud schemes or because of mistake, a payment order will identify the beneficiary both by account number and by name, each referring to a different person. Under section 4A-207(2)(a) and (3), the beneficiary's bank is entitled to pay the account if it does not know of the discrepancy and the originator is a bank, or if a nonbank originator received notice that payment might be made by account number even if a name was given. If the bank pays the person identified by name or knows of the discrepancy (§ 4A-402(3)), no person has rights as beneficiary except the person paid by the beneficiary's bank if that person was entitled to payment from the originator. If no person has rights as a beneficiary, acceptance of the order cannot occur (§ 4A-207(2)(b)). If the person paid is not a correct payee, the money back guaranty applies (§ 4A-402(3)). Article 4A also contains provisions resolving situations where the beneficiary's bank or an intermediary bank is misdescribed instead of the beneficiary (§ 4A-208), and governing cancellation (stop payment) and amendment of payment orders (§ 4A-211).

*Continued on next page*

## V I D E O S E M I N A R

Our Section will co-sponsor with the ABA Division for Professional Education "Fundamentals of Asset-Based Financing," to be broadcast via satellite to more than 50 locations nationwide on February 15, 1990, from noon to 4:00 p.m. EST.

Focusing on the basics of asset-based lending, the program will examine the loan from preliminary investigation through closing, including: preparation of loan documents; various types of collateral; guaranties, letters of credit, and debt subordination agreements; relationships between lenders; and usury and regulatory acts.

The program chair is Maury B. Poscover, chair of the Committee on Commercial Financial Services. Other faculty members will include Howard Ruda, Donald Rapson, and E. Carolan Berkley. Registrants at all viewing locations will be able to question the panelists.

The registration fee, which includes study materials, is \$135 (\$85 for government employees, \$65 for law students). To register or to obtain further information, readers should contact Theresa Kittridge, ABA Satellite Seminars, at (800) 621-8986 (outside Illinois) or (312) 988-6200 (within Illinois).

(§ 4A-103(1)(c)). For the same reason, the concept of payment order excludes payment by credit card.

Because payment orders must involve banks (§ 4A-105(1)(b)), funds transfers made by Western Union and the like are excluded; they are sufficiently different from the large, commercial transfers that are the subject of article 4A as to make it inadvisable to employ the same rules. Credit transfers through Automated Clearing Houses ("ACH") are included under article 4A, but ACH debit transfers are excluded, again for the reason they involve sufficiently different considerations (§ 4A-103(1)(b)). Finally, a funds transfer any

tion, see the U.C.C. annual surveys at 35 Bus. Law 1129 (1980); 38 Bus. Law. 1130 (1983); 39 Bus. Law 1333 (1984); 41 Bus. Law. 1412 (1986); and 42 Bus. Law. 1291 (1987). Article 4A addresses each of these problem areas.

An authorized payment order may be properly executed by the receiving bank and binds the person identified as the sender. The order may be expressly or impliedly authorized, or the sender may be bound by apparent authority. If the order is not authorized, the bank will have acted improperly in executing the order. However, if a commercially reasonable security procedure (§ 4A-201) was in place, the payment order cleared

## Sending Large Dollars

*Continued from page 7*

A funds transfer is used instead of a cashier's or similar check because it is fast and cheap. However, because of the large amounts involved, there is considerable risk if something goes awry; if the banks transmitting the orders had to bear the risk of improper or late execution, funds transfers would cease to be either fast or cheap. Accordingly, absent a contrary agreement, section 4A-305 generally relieves a bank from potential liability for consequential damages because of improper or late execution or the failure to execute a payment order, and provides that for delay, noncompletion, or failure to follow instructions (including the order itself), a bank is liable only for interest losses and expenses, as applicable. Reasonable attorney's fees also are recoverable if a justified demand for compensation is made and refused (§ 4A-305(5)).

Acceptance of a payment order by the beneficiary's bank generally obliges it to pay the amount of the order to the beneficiary (§ 4A-404(1)). However, in some cases the bank itself may not receive settlement for the order. In such event,

the obligation of payment and payment are still final as to the beneficiary and any attempt to make it conditional by agreement is ineffective, unless (1) a rule of a funds transfer system used in the funds transfer provides for provisional payment and this rule is accepted by the affected parties after notice before initiation of a transfer, or (2) the order was transmitted over a funds transfer system that has a loss-sharing agreement among participants and nonetheless the system fails to complete settlement under its rules with respect to any payment order in the funds transfer (the "doomsday scenario") (§ 4A-405(3)-(5)).

### Conclusion

Article 4A contains a variety of other provisions governing creditor process served on a receiving bank and set-off by the beneficiary's bank (§ 4A-5032); injunctions prohibiting funds transfers (§ 4A-503); preclusion against a customer contesting a payment order made by its bank (§ 4A-505); and the amount of interest payable (§ 4A-506). In addition, section 4A-507 contains rules on choice of law that seek to maximize the certainty of the law governing funds trans-

1990

- Jan. 17-19 *Midwinter Committee Meetings:*  
Corporate Counsel  
Law & Accounting  
Partnership & Uninc.  
Business Orgs.  
Small Business  
Santa Fe
- Feb. 1-2 Futures Regulation  
Comm.  
Puerto Vallarta,  
Mexico
- Mar. 2-3 National Institute:  
Consumer Fin.  
Services  
in the 90's  
Washington, DC

fers. Indeed, that is the goal of all of article 4A, and its rapid and uniform enactment is necessary to achieve that goal under state law.

Fred H. Miller  
Norman, OK  
William B. Davenport  
Chicago

# THE BUSINESS LAWYER UPDATE

American Bar Association  
Section of Business Law  
750 North Lake Shore Drive  
Chicago, Illinois 60611

Non-Profit Organization  
U.S. Postage  
PAID  
American Bar  
Association

Handwritten cursive letter 'B'.

Printed letter 'H'.

Handwritten cursive letter 'L'.

Handwritten cursive letter 'P'.

Handwritten cursive letter 'Z'.

**FISCAL NOTE**

Revision Date: Draft 4/9/91 Department Affected: DOT&PF  
 Title: An Act relating to operating commercial motor vehicles, BRU:  
 motor vehicles, aircraft, and watercraft; and providing for an  
 effective date  
 Sponsor: Rules Committee Component:  
 Requestor: Governor Component Serial Number:

**EXPENDITURES/REVENUES: (Thousands of Dollars)**

OPERATING	FY92	FY93	FY94	FY95	FY96	FY97
PERSONAL SERVICES	0	0	0	0	0	0
TRAVEL	0	0	0	0	0	0
CONTRACTUAL	0	0	0	0	0	0
SUPPLIES	0	0	0	0	0	0
EQUIPMENT	0	0	0	0	0	0
LAND & STRUCTURES	0	0	0	0	0	0
GRANTS, CLAIMS	0	0	0	0	0	0
MISCELLANEOUS	0	0	0	0	0	0
<b>TOTAL OPERATING:</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>

CAPITAL	0	-12197.1*	-24394.3*	-27361.6*	-34323.9*	Unk*
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REVENUE	0	0	0	0	0	0
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**FUNDING: (Thousands of Dollars)**

GENERAL FUNDS	0	0	0	0	0	0
FEDERAL FUNDS	0	-12197.1*	-24394.3*	-27361.6*	-34323.9*	Unk*
OTHER	0	0	0	0	0	0
<b>TOTAL FUNDING:</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>

**POSITIONS**

FULL-TIME	0	0	0	0	0	0
PART-TIME	0	0	0	0	0	0
TEMPORARY	0	0	0	0	0	0

Estimate of current year impact: None

\* Estimates of future year impacts are based on the Federal Highway Administrations proposed highway program submitted to Congress as H.R. 1351. The proposed highway program is a 5 year program and, therefore, funding impact in FY 96 is unknown.

**ANALYSIS: (Attach a separate page if necessary)**

Failure to enact legislation to bring Alaska into compliance with the Commercial Motor Vehicle Safety Act of 1986 (CMVSA 86) will put our highway dollars in jeopardy. CMVSA provides for 5% sanctions against highway funding for states that do not comply in FY 93 and 10% for each fiscal year thereafter. We believe this draft legislation will bring Alaska into compliance with CMVSA 86. We recommend approval of the legislation.

Prepared by: M. Clyde Stoltzfus

Phone: 465-3900

Division: Commissioners Office

Date: April 10, 1991

Approved by Commissioner: 

Phone: 465-3900

Frank G. Tópicá

Agency: Department of Transportation and Public Facilities

Date: April 10, 1991

Distribution By Preparer: Legislative Finance, Legislative Sponsor, Requestor, OMB, Impacted Agency(ies).

REV 2/7/91

Page 1 of 1

COMMITTEE ON

FISCAL NOTE

№ 2

Version: HB 295

(H) Publish Date: 4/22/91

STATE OF ALASKA  
1991 LEGISLATIVE SESSION

Revision Date: \_\_\_\_\_  
Title: An Act relating to Commercial  
Driver's Licenses  
Sponsor: Rules Committee  
Requestor: Governor

Department Affected: Public Safety  
BRU: Motor Vehicles  
Component: Drivers Services

COMPONENT SERIAL NO. 

	5	0	0
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EXPENDITURES/REVENUES: (Thousands of Dollars) (Inflation not Included)

OPERATING	FY 92	FY 93	FY 94	FY 95	FY 96	FY 97
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
<b>TOTAL OPERATING</b>	-0-	-0-	-0-	-0-	-0-	-0-

CAPITAL	-0-	-0-	-0-	-0-	-0-	-0-
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REVENUE	-0-	-0-	-0-	-0-	-0-	-0-
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FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER/PROG RCPT						
<b>TOTAL</b>	-0-	-0-	-0-	-0-	-0-	-0-

POSITIONS:

FULL-TIME	0	0	0	0	0	0
PART-TIME	0	0	0	0	0	0
TEMPORARY	0	0	0	0	0	0

Estimate of current year impact None

ANALYSIS: (Attach a separate page if necessary)

See attached analysis.

Prepared by: Juanita Hensley Phone: 465-4335  
Division: Drivers Services Date: 4/10/91  
Approved by Commissioner: Richard L. Burton Richard L. Burton  
Agency: Department of Public Safety Date: 4/10/91

Distribution (by preparer): Legislative Finance, Legislative Sponsor, Requestor, OMB, & Impacted Agency(ies).

This bill is the second phase of a two-phase process to revise state law to meet the requirements of the federal Commercial Motor Vehicles Safety Act. Phase one dealt with the licensing of commercial drivers, and passed the Legislature last year (Ch 53, SLA 1990). A fiscal note accompanied that legislation, and was approved. That fiscal note funded a position to handle the workload expected from the commercial driver's license program. At the present time, the position is assigned the duties of determining the eligibility of applicants for a commercial driver's license.

This bill requires the Division of Motor Vehicles to remove an operator's commercial motor vehicle license upon conviction for certain traffic violations. The additional workload resulting from this bill will be absorbed by present staff, hired as a result of Ch 53, SLA 1990.

(7)

HOUSE COMMITTEE REPORT

Date Referred: April 22, 1991

FURTHER REFERRALS:

Labor & Commerce  
Judiciary  
Finance

Date of Committee Action: 5/2/91

The TRANSPORTATION Committee considered:

HB 295

HOUSE BILL NO. 295

OPERATION OF VEHICLES, PLANES, & BOATS

"An Act relating to operating commercial motor vehicles, motor vehicles, aircraft, and watercraft; and providing for an effective date."

RECOMMENDATIONS:

[ ] the same title

be replaced with \_\_\_\_\_

[ ] a new title

[ ] have attached amendments(s)

[X] do pass

[ ] do not pass

[ ] no recommendations

[ ] individual recommendations

[ ] additional referral to the \_\_\_\_\_ Committee

ADOPTS: \_\_\_\_\_ letter of Intent

ATTACHES NEW FISCAL NOTE(S): (Dept)

APPROVES PREVIOUS: (Dept/Date)

[X] <sup>NEGATIVE</sup> fiscal impact DOT

[ ] fiscal note(s) \_\_\_\_\_

[X] zero fiscal note NPS

[ ] zero fiscal note(s) \_\_\_\_\_

SIGNING DO PASS	DP	OTHER RECOMMENDATIONS	DNP	NR	AM
<i>Robert A. Lemaw</i>	✓	<i>Gene Kubina</i>		X	
<i>Lail Phillips</i>	✓				
<i>Richard [unclear]</i>	*				
<i>[unclear]</i>	X				

*Richard [unclear]*



Please fill in everything

House Transportation ~~Committee~~

DATE: May 2, 91

PLACE: Room 17

SUBJECT OF MEETING:  
 HB 295 State Transportation  
 Overview P.O.T +  
 Uo.T bidding

NAME	REPRESENTING	BUSINESS/PERSONAL MAILING ADDRESS	ZIP	(H) PHONE	(W) PHONE	DO YOU WANT TO TESTIFY?	WHAT SUBJECT/ WHICH BILL?
Juanita Hensley	DPS/dmv	Box N Juneau, AK	99811		4335	<input checked="" type="radio"/> Y <input type="radio"/> N	295
G H ORETSKI	DPS	BOX N, JUNI.				<input type="radio"/> Y <input type="radio"/> N	IF Q'S — HB 295
						<input type="radio"/> Y <input type="radio"/> N	
						<input type="radio"/> Y <input type="radio"/> N	
						<input type="radio"/> Y <input type="radio"/> N	
						<input type="radio"/> Y <input type="radio"/> N	
						<input type="radio"/> Y <input type="radio"/> N	
						<input type="radio"/> Y <input type="radio"/> N	
						<input type="radio"/> Y <input type="radio"/> N	
						<input type="radio"/> Y <input type="radio"/> N	
						<input type="radio"/> Y <input type="radio"/> N	

# ALASKA TRUCKING ASSOCIATION, INC.

3443 Minnesota Drive • Anchorage, Alaska 99503 • Phone (907) 276-1149 • Fax (907) 274-1948

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May 1, 1991

TO: HOUSE TRANSPORTATION COMMITTEE  
ATTN: Representative Foster, Chairman

FROM: Frank J. Dillon, Executive Director

RE: ATA SUPPORT FOR S.B. 261 - " An Act Relating  
To Operating Commercial Motor Vehicles ....."

ATA asks that you support S.B. 261. Enactment of this proposed legislation will help assure improved highway safety by requiring that commercial motor vehicle drivers are sober and drug-free. It mandates severe penalties for those drivers and companies who do not choose to operate in a reasonable, prudent and safety conscious manner. S.B. 261 will only impact a very small number of drivers and companies. The vast majority of commercial drivers do not drive while impaired nor do many companies allow such drivers to drive while impaired. ATA however feels that even a small number of impaired commercial vehicle drivers are too many and S.B. 261 should further help reduce the number of impaired truck drivers on the roads.

Please pass S.B. 261.

HB

297

FISCAL NOTE

BILL NO. HB 297

STATE OF ALASKA  
1992 LEGISLATIVE SESSION

Revision Date: \_\_\_\_\_  
Title: An Act relating to insurance coverage for adopted children

Department Affected: Administration  
BRU: Retirement and Benefits

Sponsor: House Labor and Commerce  
Requestor: House Labor and Commerce

Component: Retirement and Benefits

COMPONENT SERIAL NO. 64

Expenditures/Revenues: (Thousands of Dollars)

OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES	0	0	0	0	0	0
TRAVEL	0	0	0	0	0	0
CONTRACTUAL	0	0	0	0	0	0
SUPPLIES	0	0	0	0	0	0
EQUIPMENT	0	0	0	0	0	0
LAND & STRUCTURES	0	0	0	0	0	0
GRANTS, CLAIMS	0	0	0	0	0	0
MISCELLANEOUS	0	0	0	0	0	0
TOTAL OPERATING	0	0	0	0	0	0

CAPITAL	0	0	0	0	0	0
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REVENUE FUND SOURCE:	0	0	0	0	0	0
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FUNDING: (Thousands of dollars)

GENERAL FUND	0	0	0	0	0	0
FEDERAL FUNDS	0	0	0	0	0	0
OTHER FUND SOURCE	0	0	0	0	0	0
TOTAL	0	0	0	0	0	0

POSITIONS

FULL-TIME:	0	0	0	0	0	0
PART-TIME:	0	0	0	0	0	0
TEMPORARY:	0	0	0	0	0	0

Estimate of current year impact:

ANALYSIS: (attach a separate page if necessary.) The State's insurance plans for retirees and active employees already provide the same level of coverage for adopted children as for natural, foster or step children. This bill will have no fiscal impact on the insurance plans.

Prepared By: Gary Bader *Gary M. Bader*  
Division: Retirement and Benefits

Phone: 465-4470  
Date: 1/28/92

Approved by Commissioner: Nancy Bear Usual  
Agency: Department of Administration *Nancy Bear Usual*

Date: 1/30/92

# FISCAL NOTE

STATE OF ALASKA  
1992 LEGISLATIVE SESSION

BILL NO. HB297

Revision Date April 22, 1991 Dept. Affected Health and Social Services  
 Title: An Act relating to insurance coverage for adopted children and children placed... BRU: Family and Youth Services  
 Component: SCRO, SERO, NRO  
 Sponsor: Rep. Donley  
 Requestor: House Labor and Commerce COMPONENT SERIAL NO. 0254, 0255, 0258

Expenditures/Revenues	(Thousands of Dollars)					
OPERATING	FY93	FY94	FY95	FY96	FY97	FY98
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
<b>TOTAL OPERATING</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

CAPITAL						
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REVENUE						
---------	--	--	--	--	--	--

FUNDING:	(Thousands of Dollars)					
GENERAL FUND						
FEDERAL FUNDS						
OTHER						
<b>TOTAL</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

POSITIONS:						
FULL-TIME						
PART-TIME						
TEMPORARY						

Estimate of current year impact: NONE

**ANALYSIS:** (Attach a separate page if necessary)

The Division of Family and Youth Services supports HB 297, an Act relating to insurance coverage for adopted children and children placed for adoption.

Adoption guarantees a child a permanent family. This bill will ensure that children placed for adoption will receive the same insurance coverage and medical care that a child born to the family would receive. The bill also

Prepared by: Brian Saylor, Deputy Commissioner *BS* Phone: 465-3030  
 Division: Family and Youth Services Date: February 7, 1992

Approved by Commissioner: Theodore A. Mala *TAM* Date: 2/12/92  
 Agency: Department of Health and Social Services

Distribution (by preparer):  
 Legislative Finance            OMB  
 Legislative Sponsor        Impacted Agency(ies)  
 Requestor

**ANALYSIS (cont.):**

requires coverage for pre-existing conditions, just as a birth child is covered at birth.

DFYS places special needs children for adoption. These children frequently have pre-existing medical or psychological needs. Under our subsidy program, we cover the costs of meeting those needs that are not met by the adoptive families insurance coverage. Some of those costs would be transferred to the family's insurance if this bill is enacted. No exact figure can be given as these costs vary per child per year, and are not paid directly by DFYS, but rather through payments to the adoptive family.

However most adoptions in Alaska are done privately or through private agencies. Those children do not have subsidies and they and their adoptive families will benefit considerably from this proposed change.

FISCAL NOTE

STATE OF ALASKA  
1992 LEGISLATIVE SESSION

BILL NO. HB 297

Revision Date: 12/27/91

Department Affected: Commerce & Econ. Dev.

Title: An Act relating to insurance coverage for adopted children and children placed for adoption

BRU: Insurance

Sponsor: House Labor & Commerce

Component: Operations

Requestor: \_\_\_\_\_

COMPONENT SERIAL NO. 

0	3	5	4
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EXPENDITURES/REVENUES: (Thousands of Dollars)

OPERATING	FY 93	FY 94	FY 95	FY 96	FY 97	FY 98
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
<b>TOTAL OPERATING</b>	0	0	0	0	0	0
<b>CAPITAL</b>	0	0	0	0	0	0
<b>REVENUE FUND RESOURCE:</b>	0	0	0	0	0	0

FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER FUND SOURCE:						
<b>TOTAL</b>	0	0	0	0	0	0

POSITIONS:

FULL-TIME	0	0	0	0	0	0
PART-TIME						
TEMPORARY						

Estimate of current year impact: \_\_\_\_\_

ANALYSIS (Attach a separate page if necessary.)

Prepared By: Don Koch, Chief of Market Surveillance Phone: 465-2577

Division: Insurance Date: 1/2/92

Approved by Commissioner: Glenn A. Olds Gov. Council

Agency: Department of Commerce & Economic Development Date: 1-10-92

Distribution (by preparer): Leg. Fin., Legislative Sponsor, Requestor, OMB/DBR, Gov. Legis. Ofc., and Impacted Agency(ies).

# REPRESENTATIVE DAVE DONLEY

ALASKA STATE LEGISLATURE  
DISTRICT ELEVEN  
SEAT A

311 "C" STREET, SUITE 450  
ANCHORAGE, ALASKA 99503  
(907) 561-7629 (FAX) 562-4376

ALASKA LANDINGS • BENTZEN • BIRCHWOOD • CHESTER CREEK • HEATHER MEADOWS • LINCOLN PARK • MIDTOWN • NORTHSTAR  
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CHAIRMAN  
JUDICIARY COMMITTEE

VICE CHAIRMAN  
REGULATION REVIEW COMMITTEE

MEMBER  
RULES COMMITTEE  
LABOR AND COMMERCE COMMITTEE

## HB 297

### Insurance Coverage for Adopted Children

This bill establishes, in law, that insurance companies must cover a new child in the family from the moment that child comes into the family, whether by birth or adoption.

Currently a number of insurance companies require a thirty day waiting period before coverage for an adopted child begins. If the child has any medical problems or even if the child is involved in an accident during that thirty days, the insurance company declines to pay for treatment.

The net effect of this approach is that it is undue and inappropriate discrimination against adopted children. A child is a member of the family, and a dependent from the moment the child enters the family whether that be by birth or adoption.

HB 297 redresses this problem.



P.O. B-

*Sponsor Statement*

3-5661



# HOUSE COMMITTEE REPORT

(7)

Date Referred: April 22, 1991

FURTHER REFERRALS:

Labor & Commerce  
Finance

Date of Committee Action: 5-10-91

The HEALTH, EDUCATION AND SOCIAL SERVICES Committee considered:

HB 297

HOUSE BILL NO. 297

INS. COVERAGE FOR ADOPTED NEWBORN CHILD

"An Act relating to insurance coverage for adopted children and children placed for adoption."

**RECOMMENDATIONS:**

be replaced with \_\_\_\_\_  the same title

\_\_\_\_\_  a new title

have attached amendments(s)

do pass

do not pass

no recommendations

individual recommendations

additional referral to the \_\_\_\_\_ Committee

ADOPTS: \_\_\_\_\_ letter of Intent

ATTACHES NEW FISCAL NOTE(S): \_\_\_\_\_ (Dept)

APPROVES PREVIOUS: \_\_\_\_\_ (Dept/Date)

fiscal impact \_\_\_\_\_

fiscal note(s) \_\_\_\_\_

zero fiscal note DCED

zero fiscal note(s) \_\_\_\_\_

SIGNING <u>DO</u> PASS	DP	OTHER RECOMMENDATIONS	DNP	NR	AM
<i>Cheri Davis</i>	<input checked="" type="checkbox"/>				
<i>Betty Davis</i>	<input checked="" type="checkbox"/>	<i>Mary Miller</i>		<input checked="" type="checkbox"/>	
<i>John E. Souza</i> (GONZALES)	<input checked="" type="checkbox"/>	<i>[Signature]</i> (LINCOLN)		<input checked="" type="checkbox"/>	
		<i>[Signature]</i> (CARNEY)		<input checked="" type="checkbox"/>	

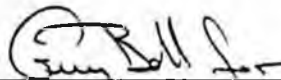
*[Signature]*  
CO-CHAIRMAN'S SIGNATURE (LINCOLN)

HB 297: "An Act relating to insurance coverage for adopted children and children placed for adoption."

The department is in favor of this legislation.

The department has generally been opposed to health insurance mandates. However, AS 21.42.345, passed in 1975, is one "mandate" that the department supported when it was introduced. It represents more of an unfair discrimination issue than it does a coverage mandate. Prior to passage of the section, newborn children were not considered family members until they were 14 days of age. This placed substantial financial stress on the parents of newborn children with medical problems.

Recently, it has been noted that insurers are treating newly adopted children in a similar manner as were newborn children prior to 1975. Insurers are imposing their own definition of "family member" causing in some cases, the same kind of financial stress noted above. Insurers are relying on preexisting conditions restrictions to deny coverage for adopted children, thus, impeding the adoption process. In such cases, immediate medical attention is often preventive and can identify and treat situations that will only become more expensive and potentially life threatening if not treated early. We view this legislation as a clarification of existing statute, not an additional mandate.



Glenn A. Olds, Commissioner

Date: 5-1-91

HB

302

(7)

HOUSE COMMITTEE REPORT

Date Referred: April 26, 1991

FURTHER REFERRALS:

Judiciary  
Finance

Date of Committee Action: 5-11-91

The LABOR AND COMMERCE Committee considered:

HB 302

HOUSE BILL NO. 302

REQUIRE PROFESSIONAL LIABILITY INSURANCE

"An Act relating to malpractice insurance for certain persons who are in a regulated occupation or profession."

RECOMMENDATIONS:

be replaced with \_\_\_\_\_

CSHB 302 (L+C)

the same title  
 a new title

have attached amendments(s)

do pass

do not pass

no recommendations

individual recommendations

additional referral to the \_\_\_\_\_ Committee

ADOPTS: \_\_\_\_\_ letter of Intent

ATTACHES NEW FISCAL NOTE(S): (Dept)

APPROVES PREVIOUS: (Dept/Date)

fiscal impact Commerce

fiscal note(s) \_\_\_\_\_

zero fiscal note \_\_\_\_\_

zero fiscal note(s) \_\_\_\_\_

SIGNING DO PASS	DP	OTHER RECOMMENDATIONS	DNP	NR	AM
<i>[Signature]</i>	✓				
<i>[Signature]</i>	✓				
<i>[Signature]</i>	✓				
<i>[Signature]</i>	✓				

*[Signature]*  
CHAIRMAN'S SIGNATURE

FISCAL NOTE

STATE OF ALASKA  
1991 LEGISLATIVE SESSION

BILL NO. HB 302

Revision Date: \_\_\_\_\_ Department Affected: Commerce & Economic Dev.  
 Title: An Act relating to malpractice insurance for certain persons.... BRU: Occupational Licensing  
 Component: Administration  
 Sponsor: House Judiciary  
 Requestor: House Labor & Commerce COMPONENT SERIAL NO. 

0	3	5	6
---	---	---	---

Expenditures/Revenues: (Thousands of Dollars)

OPERATING	FY 92	FY 93	FY 94	FY 95	FY 96	FY 97
PERSONAL SERVICES	41.2	41.2	41.2	41.2	41.2	41.2
TRAVEL	5.0	5.0	5.0	5.0	5.0	5.0
CONTRACTUAL	5.0	5.0	5.0	5.0	5.0	5.0
SUPPLIES	1.0	1.0	1.0	1.0	1.0	1.0
EQUIPMENT	5.8					
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
<b>TOTAL OPERATING</b>	<b>58.0</b>	<b>52.2</b>	<b>52.2</b>	<b>52.2</b>	<b>52.2</b>	<b>52.2</b>

CAPITAL						
---------	--	--	--	--	--	--

REVENUE	0	0	0	0	0	0
---------	---	---	---	---	---	---

FUNDING: (Thousands of Dollars)

GENERAL FUND	58.0	52.2	52.2	52.2	52.2	52.2
FEDERAL FUNDS						
OTHER						
<b>TOTAL</b>	<b>58.0</b>	<b>52.2</b>	<b>52.2</b>	<b>52.2</b>	<b>52.2</b>	<b>52.2</b>

POSITIONS:

FULL-TIME	1	1	1	1	1	1
PART-TIME	0	0	0	0	0	0
TEMPORARY	0	0	0	0	0	0

Estimate of current year impact: None

ANALYSIS: (Attach a separate page if necessary.)  
 The bill establishes a malpractice insurance requirement for licensees, if judgment has been entered against the licensee for civil damages resulting from an act or omission arising out of the person's occupation or profession. (Continued on attached.)

Prepared By: Jennifer Strickler, Admin. Officer Phone: 465-2144  
 Division: Occupational Licensing Date: May 6, 1991  
 Approved by Commissioner: Glenn A. Olds  
 Agency: Commerce and Economic Development Date: 5-7-91

Distribution (by preparer): Legislative Finance, Legislative Sponsor, Requestor, OMB, & Impacted Agency(ies).

CONTINUATION OF FISCAL NOTE ANALYSIS - HB 302

HB 302 requires the division to adopt regulations establishing the minimum malpractice insurance requirements for each regulated occupation or profession; and to suspend a license for one year if a licensee fails to comply with the requirement that a copy of the judgment and proof of the malpractice insurance, or a copy of the satisfaction or settlement of the judgement be submitted to the division within 45 days after the judgment is entered.

The division currently licenses 31 occupations and professions in over a hundred separate licensing categories. Since the bill requires the division to establish minimum malpractice requirements for each regulated occupation or profession, the division anticipates that a great amount of staff time and effort will be needed to coordinate with the division of risk management, the insurance companies, and each occupation or profession in establishing minimum malpractice insurance requirements for each licensing category, by regulations. This fiscal note therefore addresses the funding needed to carry out the provisions of the bill.

Personal Services \$ 41.2

1 - Regulations Specialist I, Range 13A, GGU  
12 months

This position will be responsible to coordinate the efforts in establishing the minimum malpractice insurance requirements for each of the 31 occupations and professions, for each licensing category.

Travel 5.0

This funding will provide transportation for the Regulations Specialist to coordinate with insurance companies, licensees, and to hold the necessary public hearings on the proposed regulations throughout the State.

Contractual Services 5.0

This funding will cover printing and advertising of the regulations project, communications expenses, and hearing expenses for suspension of a license in accordance with Section 08.02.040(b).

Supplies 1.0

This funding will provide daily operating supplies for the Regulations Specialist position.

Equipment (one-time costs) 5.8

This funding will provide one-time equipment costs for the Regulations Specialist position.

TOTAL: \$ 58.0

7-LS1254G ✓  
Ford  
5/1/91

CS FOR HOUSE BILL NO. 302 ( )  
IN THE LEGISLATURE OF THE STATE OF ALASKA  
SEVENTEENTH LEGISLATURE - FIRST SESSION

BY

Offered:  
Referred:

Sponsor(s): HOUSE JUDICIARY COMMITTEE

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to malpractice insurance for certain persons who are in a regulated  
2 occupation or profession."

3 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

4 \* Section 1. AS 08.02 is amended by adding a new section to read:

5           Sec. 08.02.040. MALPRACTICE INSURANCE REQUIRED. (a) A person in an  
6 occupation or profession regulated under this title shall obtain malpractice insurance from an  
7 insurer authorized to do business in this state if judgment has been entered against the person for  
8 civil damages and the civil damages resulted from an act or omission arising out of the person's  
9 occupation or profession. Malpractice insurance required under this section must provide  
10 coverage for negligent acts or omissions arising out of the occupation or profession of the insured  
11 and must be maintained in effect until the judgment is satisfied or the parties to the judgment  
12 have entered into a settlement agreement.

13           (b) A person who is required to obtain malpractice insurance under this section shall  
14 provide a copy of the judgment and proof of the required insurance, or a copy of the satisfaction

1 or settlement of the judgment, to the division of occupational licensing within 45 days after  
2 judgment is entered. The license of a person who fails to comply with this section shall be  
3 suspended for a period of one year.

4 (c) The division of occupational licensing shall

5 (1) in coordination with the division of risk management, adopt regulations that  
6 establish minimum malpractice insurance requirements for each regulated occupation or  
7 profession;

8 (2) upon issuance or renewal of a license, notify each person in an occupation or  
9 profession regulated under this title of the requirements of this section.

10 (d) A court that enters a judgment for civil damages resulting from an act or omission  
11 arising out of the liable person's occupation or profession, shall, if that person's occupation or  
12 profession is regulated under this title, forward a copy of the judgment to the division of  
13 occupational licensing.

14 (e) This section does not apply to a person who is required to have insurance or to  
15 provide a bond as a condition of licensing, or to a person who is no longer employed in the  
16 occupation or profession in which an act or omission occurred that resulted in an award of civil  
17 damages, or to an occupation or profession regulated under this title that is unrelated to the  
18 occupation or profession in which an act or omission occurred that resulted in an award of civil  
19 damages.

20 (f) In this section, "malpractice insurance" has the meaning given in AS 21.12.070(a)(10).

# Alaska State Legislature



House of Representatives  
House Judiciary Committee  
Chairman Dave Donley

P. O. Box V  
State Capitol  
Juneau, Alaska 99811  
(907) 465-4990

## SPONSOR STATEMENT

HB 302, "An Act relating to malpractice insurance for certain persons who are in a registered occupation or profession."

HB 302 requires that a person, who engages in a state licensed occupation or profession, must show proof of malpractice insurance when there is an outstanding malpractice judgment against the person, in order for that person to continue practicing the licensed profession.

Major provisions of this bill include requirements that:

\* malpractice insurance be maintained until an outstanding judgment, resulting from the negligent practice of the licensed occupation or profession, has been paid;

\* the licensee provide a copy of the judgment and proof that it has been paid or that required insurance has been obtained within 10 days after the judgment is entered; failure to comply with this requirement can result in a one year license suspension;

\* the Division of Occupational Licensing work with the Division of Risk Management to establish minimum malpractice insurance requirements for each licensed occupation or profession;

\* the court that enters judgment must forward a copy of the judgment to the Division of Occupational Licensing.

The requirements of HB 302 do not apply to a person who:

\* is otherwise required to have insurance or a bond as a condition of licensing;

\* is no longer employed in the occupation or profession the negligent practice of which resulted in an award of civil damages; or

\* is presently engaged in an occupation or profession that is unrelated to the occupation or profession the negligent practice of which resulted in an award of civil damages.

HB 302 serves as an incentive for prompt payment of judgments and for entering into settlement agreements. The measure should also serve to better protect the public by requiring insurance of those professionals who have failed to demonstrate financial responsibility for damages they have caused.

HB

310

# Alaska State Legislature

## COMMITTEES:

MEMBER  
RULES  
INTERNATIONAL TRADES & TOURISM  
LABOR & COMMERCE  
ETHICS  
WESTERN STATES LEGISLATIVE  
FORESTRY TASK FORCE



P.O. BOX 1441  
WRANGELL, ALASKA 99929  
(907) 874-2316

White in Juneau  
P.O. BOX V  
JUNEAU, ALASKA 99811  
(907) 465-4905

## House of Representatives

ROBIN L. TAYLOR  
MINORITY LEADER

### MEMORANDUM

TO: House Transportation Committee  
FROM: Rep. Robin L. Taylor  
DATE: May 7, 1991  
REF: Background on HB 310

In 1986, the Second Session of the 14th Alaska State Legislature passed HB 181, an Act Relating to the Maintenance of Vessels of the Alaska Marine Highway System. The bill passed the House on reconsideration on April 14 by a vote of 30-7. It passed the Senate on June 1, 1986 by a vote of 18-0.

HB 181 had been amended in the House to include a sunset provision. HB 310 will repeal that sunset provision, which would otherwise take effect on August 30, 1992.

The State of Alaska began investigating the feasibility of developing a small ship repair yard in 1976. A special appropriation was approved in 1978, authorizing the DOT/PF to acquire a site for a permanent marine maintenance facility for State ferries.

Between 1983 and 1986, the State spent in excess of \$32 million, building a shipyard at Ketchikan. The yard has never been completed as originally designed or intended. The shipyard is leased to the City of Ketchikan, which in turn sublets the facility to Seley, Inc. Seley, Inc., dba Ketchikan Shipyard, Inc. (KSI) provides full time employment for an average of 50 workers, with an annual payroll of approximately \$2 million. In 1990, KSI provided service to 96 commercial vessels and eight vessels of the Alaska Marine Highway System and the Department of Public Safety.

PAGE TWO - HB 310 BACKGROUND

Since 1987, work on state owned vessels has generated \$10,142,332 in revenue at the Ketchikan yard. All but approximately \$557,000 of that total has been for work on vessels of the Marine Highway. In addition to providing employment, KSI pays property taxes to the City of Ketchikan of about \$180,000 per year.

The intent of the 1986 law was to give Alaska's two shipyards (the other is at Seward) the best advantage possible under law in competing with facilities outside the State. It has not been easy going. The initial operator lost money on the Ketchikan yard and only now is that facility beginning to see a turn around. There is a cooperative effort in the works between the State, City of Ketchikan and KSI to make the yard a viable Alaskan business. Those efforts could be jeopardized by the threat of the sunset provision written in to HB 181 back in 1986.

While the problems at KSI can be blamed in part on poor management by the initial operator, many of the problems stem from an apparent reluctance on the part of the State to use the yard to the fullest extent possible. That attitude is changing with the new Administration and the passage of HB 310 will reemphasize the intent of the Legislature that work on State owned vessels take place in Alaska.

Department of Transportation & Public Facilities



POSITION PAPER

BILL NO: HB 310

APPROVED: J. Granger f. F. Turpi

TITLE: An act relating to instate maintenance of state marine vessels

DATE: 5/6/91

May 6, 1991

AMHS POSITION PAPER HOUSE BILL 310

AS 36.90.050(a) requires that a marine vessel owned by the state be maintained or repaired within Alaska unless the commissioner of Transportation and Public Facilities determines there is no facility in the state able to perform the maintenance at a price that is in the state's best interest. In making the finding the commissioner must consider the following:

- (1) the amount of money the state has granted to, or otherwise invested in, marine vessel maintenance facilities in the state;
(2) the amortization, overhead, and start-up costs of the facilities in the state; and
(3) the direct and indirect benefits to the economy and labor force of the state that may be obtained by contracting with a facility in the state.

AS 39.90.050(b) suspends the competitive bid requirements of AS 36.30 to contracts for the repair or maintenance of state owned marine vessels if the contract is awarded to a facility in the state.

In order to comply with this statute AMHS has developed a policy and procedure which addresses the fact that there are two shipyards in Alaska which can work on some or all of the vessels in the fleet. The procedure gives Alaskan shipyards a 5% Alaska bidder's preference, as well as calculates the cost of moving the vessel either from its designated base port or the port where the vessel's operations are terminated prior to beginning its maintenance.

All vessels serving Southeast Alaska have Ketchikan designated as

the base port. The M/V Tustumena and the M/V Bartlett are based in Seward for the purpose of this calculation. The 5% Alaska bidder's preference is deducted from the resident shipyard's bid, while the vessel transfer costs are added to any shipyard's bid which is either not the vessel's designated base port, or the point at which its service is terminated prior to entering maintenance status.

While this procedure is fairly straightforward and is designed to account for real costs which would be incurred by AMHS in transporting a vessel for maintenance outside of Alaska, AS 36.90.050(a) requires a higher test before the vessel can actually leave the state. The conditions which must be met have no relationship to the need to keep vessel maintenance costs low or maintaining the vessel. These conditions require the consideration of economic factors which are difficult to quantify and cannot be directly related to the primary goal of AMHS.

Perhaps the legislature in renewing this statute should consider deleting AS 36,090.050(a)(1)-(3), allowing the Alaska bidder's preference requirements to serve the public purpose this statute is designed to achieve. In addition consider amending AS 39.090.050(a) to read: "...determines that there is no facility in the state able to perform the required maintenance at (a) the price or quality that is in the state's best interest." This will insure that AMHS receives the best service possible at the fairest price.



## KETCHIKAN SHIPYARD INC.

PO BOX 3380 • 3801 TONGASS AVE. • KETCHIKAN, ALASKA 99901  
PHONE 907-225-0400 FAX 907-225-0517

### PERSONNEL:

General Manager:	Greg Dronkert
Production Manager:	John Thompson
Dockmaster:	Pat Major
Ship Superintendent:	Lance Ridgely
Ship Superintendent:	Chris Cleman
Support Services:	Craig Trettevik

### Foremen:

Steel	Ed Couture
Pipe	Martin Towner
Machinist	Lewis Stamm
Electrical	Janelle Castroni
Paint	Keith Wolfe

See attached resume's



## **KETCHIKAN SHIPYARD INC.**

PO BOX 5180 • 1801 TONGASS AVE. • KETCHIKAN, ALASKA 99901  
PHONE 907-223-0400 FAX 907-223-0517

### **Facility Portfolio**

**December 15, 1990**

#### **Facilities:**

##### **Lift Facilities:**

- Drydock
- DD Gantry Crane
- Grove 50T
- Cascade Shop Crane
- Manlifts
- Forklifts

##### **Paint/Blast Facilities:**

- Grayco King Pump
- Butterworth Hydro Blaster
- Blast Pots

##### **Machine Shop**

- Lathe L&S
- Enco Lathe
- Horizontal Boring Mill
- Vertical Mill
- Radial Drill
- Hydraulic Press
- Drill Presses
- Ironworker
- Pinch Roll

##### **Steel and Pipe**

- Air Compressors
- Miller 8 Pacs - 3
- Miller Big 50 - 1
- Threader/Cutter - 2

##### **Services**

- 2000 Gal Vacuum Truck
- Waste Water Storage Tanks
- Oil Containment Boom
- Mooring Lines
- Shore Power Lines

## KETCHIKAN SHIPYARD, INC.

## DATA SHEET

\*\*\*\*\*

MOORAGE FACILITIES

DOCK FACE	1,000 LINEAR FEET
WATER DEPTH	-35 FT MLLW
DOCK HEIGHT	+25 FT MLLW

VESSEL SUPPORT SYSTEMS

ELECTRICAL	WATER
OILY WASTE DISPOSAL	SEWER
COMPRESSED AIR	STEAM
TELEPHONE	

AVAILABLE SERVICES

HULL PRESERVATION, WATER-BLASTING, SANDBLASTING  
AND COATING SYSTEMS

ENVIRONMENTAL SERVICES, WASTE DISPOSAL, TANK  
CLEANING AND GAS FREEING (NORVAC)

CRANE SERVICES, TO 50 TONS

STEEL/ALUMINUM, FABRICATION AND REPAIR

PIPEFITTING AND FABRICATION

SHIPWRIGHT SERVICES

MACHINE SHOP, HYDRAULICS AND DIESEL REPAIR  
SERVICES, LATHES TO 35 FEET.

KETCHIKAN SHIPYARD, INC.

DATA SHEET

=====

DRYDOCK

ABS CLASS +A1

LENGTH, OVERALL	434'0"
LENGTH, OVER PONTOON	384'0"
WIDTH, BETWEEN WINGWALLS	110'0"
WIDTH, BETWEEN FENDERS	107'0"
TOTAL LIFTING CAPACITY	9,600 LONG TONS

PONTOON DECK, APRON, & VEHICLE RAMP LOADING

FORK LIFTS	8,000 LBS
TRUCKS	HS-20-44
MOBILE CRANES	5-10 SHORT TON, SWL

VESSEL SUPPORT SYSTEMS

ELECTRICAL	OILY WASTE
LIGHTING	COMPRESSED AIR
EMERGENCY GENERATOR	TELEPHONE
FIRE PROTECTION	POTABLE WATER
SEWAGE COLLECTION	



# KETCHIKAN SHIPYARD INC.

P.O. BOX 9300 • 3RD TONGAST AVE. • KETCHIKAN, ALASKA 99901  
 PHONE 907-223-0400 FAX 907-223-0517

## Ketchikan Shipyard, Inc. Equipment List

DESCRIPTION	MAKE	MODEL	S/N
AIR COMPRESSOR, 150 HP	SULLAIR	20-150L	003-70388
AIR COMPRESSOR, 350 HP	SULLAIR	25S-350H	003-70385
CRANE, WINCHWALL	MANITEX	M6-2400	8606A
CRANE, GANTRY	CASCADE	15-T	P5778
CRANE, 50 TON	GROVE	RT-75S	39159
FORKLIFT	HYSTER	H-60C	005D22431B
FORKLIFT	CLARK	CFY200LB	25-482-1162
FORKLIFT, 8 TON	HYSTER	P80A	A018D5037A
FORKLIFT, 60 FT	HYSTER	T60A	6122
Manlift 40'	JLG	70/JLG-40H	030901492A
FLATBED TRUCK, 1968, GREEN	FORD	F-752	F75EUC73936
VACUUM TRUCK, 1965, RED	SMC	DS	F7012L
FUEL TRUCK, 1952, GREEN	CHEV	3800	6JSL1035
40 FOOT CONTAINER	TSPT EQUIP		
PICKUP, 1982, WHITE	FORD	F-250	
PICKUP, 1979, RED/WHI	CHEV	C-20	CCL2397215292
PICKUP, 1976, GREEN	SMC	HS-25	T102461523565
PICKUP, 1983, WHITE	CHEV	C-20	16C0C1424JE143755
PICKUP, 1987, WHITE	FORD	F-150	2FTCF15Y6CB66090
PICKUP, 1987, RED	DODGE	D-100	1161789618
PICKUP, BLUE	MAZDA		
RESTROOM TRAILER	BELO SPACE	1-1	9292
TRAILER, HOUSING	SAPRISON		
GEN SET, EMER, DRYDOCK	CATERPILLAR	3406TA	2W000656
WASTEWATER OIL STORAGE TANK	HARDROCK CONST	10,000 GAL	
SLDF TANKS	UNKNOWN	AUCTION?	
BASE 17 1 1/2'	ELLIS		
FRONT END LDR	HOUGH	H-60	28AH1320
FRONT END CRASER	BOBEAT	H371	2001
HYDRAULIC PRESS	JAYE	75H	132627
DRILL PRESS	WALKER-TURNER	113-41	0001359
IRONWORKER	AUBEA	MPS 250	0150635-413-400
PIPE THREADER/CUTTER	RIGID	300	
DRILL PRESS	ORBIT	OR2501F	2-600729
PIPE THREADER/CUTTER	TOLEDO BEAVER	1-2-4	692425
PINCH ROLL	BERTSCH	6742	
LATHE, 1967	L & S	3220/24	46697
HORIZONTAL BORING MILL	GLIDDEN & LEWIS	350-T	
BOILER, NAT STEAM	YORK POWER	5PHC150-W3-965-9822-K-33069	
PAINT STILL (FURNACE), 1986	RENNMANN	6551	M20H
DRAIN CLEANER	RIEID	K1500A	23712
RADIAL DRILL	FOSDICK	X-114-A	
LATHE, 13 X 50, 1989	ENCO	111-3540	4929
VERTICAL MILL, 1989	SUPERMAX	YCM-1-1/2VP	90420136
BANDSAW	DO ALL	C-9V	296-74239
SANDBLASTER, 600 LB	ELENCO	2412	7077
SANDBLASTER, 600 LB	ELENCO	2452	7079
Strip Cleaner	HOISY	5630B	M136620489
PRESS WASH, DIESEL 3500 PSI	KUBOTA	CW3006KDK	117540
PRESS WASH, GAS 3500 PSI	HONDA	300A	N/A
WELDERS, 8 PACK, PORTABLES	MILLER	MARK VIII	KK324903
WELDERS	MILLER	BIG 50	JD15554
WELDERS, 8 PACK	MILLER	MARK VIII	JP495250
WELDERS, 8 PACK	MILLER	MARK VIII	MF370670
SANDBLAST POT, 1978	CAF	6000 LB	15830
PAINT PUMP	BRACO	KING	
2 PAINT PUMPS	SPEE-FLD 35:1	941842	11385/11224
OIL CONTAINMENT BOON	SEASPAR	CITY KTN	
HOOSING LINES	UNKNOWN	CITY KTN	
SPOKEPOWER CABLE	UNKNOWN	CITY KTN	
SERVICE HOSES	UNKNOWN	CITY KTN	

Ketchikan Shipyard Inc.  
State of Alaska Revenue

Customer		Vessel Yr Annual Maint	Vessel Gen Maint	Vessel Esurg Maint	Other	Total Revenue
Dept of Public Safety	1987					
	1988	223,622				223,622
	1989	162,579				162,579
	1990	100,470		69,980		170,450
	1991					
Dept of Public Safety	Subtotal	486,672	0	69,980	0	556,652
-----						
Dept of Fish & Wildlife	1987					
	1988					
	1989				150	150
	1990					
	1991					
Dept of Fish & Wildlife	Subtotal	0	0	0	150	150
-----						
Dept of Transportation Alaska Marine Highway	1987	400,263	172,281	48,738	79,731	701,013
	1988	2,747,070	131,855	68,316	5,825	2,953,065
	1989	2,806,300	6,805	10,538	14,208	2,837,851
	1990	1,649,653	16,975	63,227	30,873	1,760,709
	1991	1,329,283	1,611	2,000		1,332,893
Alaska Marine Highway	Subtotal	8,932,549	329,526	192,819	130,636	9,585,531
-----						
Total State of Alaska	1987	400,263	172,281	48,738	79,731	701,013
	1988	2,970,692	131,855	68,316	5,825	3,176,687
	1989	2,968,880	6,805	10,538	14,358	3,000,581
	1990	1,750,103	16,975	133,208	30,873	1,931,159
	1991	1,329,283	1,611	2,000	0	1,332,893
State of Alaska	Total	9,419,221	329,526	262,799	130,786	10,142,332

STATE OF ALASKA  
THE LEGISLATURE

POUCH Y - STATE CAPITOL  
JUNEAU, ALASKA 99811  
907-465-3800

LEGISLATIVE AFFAIRS AGENCY  
LEGISLATIVE REFERENCE LIBRARY

Copies of minutes listed below were originally included in this file. The minutes are available on the STAIRS database CMPR. In order to save space copies of minutes have not been left in the files.

Mary Van Nimwegen

3/18/86 H Transportation 7:00 am

HB

317

(7)

**HOUSE COMMITTEE REPORT**

Date Referred: May 8, 1991

FURTHER REFERRALS:

Resources  
Judiciary

Date of Committee Action: 4-9-92

The LABOR AND COMMERCE Committee considered:

HB 317

HOUSE BILL NO. 317

GUIDE-OUTFITTER AIRCRAFT INSURANCE

"An Act repealing the aviation passenger insurance or financial bond requirement for aircraft used by certain guide-outfitters, marine mammal guide-outfitters, class-A assistant guide-outfitters, and assistant guide-outfitters."

**RECOMMENDATIONS:**

be replaced with CSHB 317 (L+C)  the same title  a new title

have attached amendments(s)

do pass

do not pass

no recommendations

individual recommendations

additional referral to the \_\_\_\_\_ Committee

ADOPTS: \_\_\_\_\_ letter of Intent

ATTACHES NEW FISCAL NOTE(S): (Dept) \_\_\_\_\_

APPROVES PREVIOUS: (Dept/Date) \_\_\_\_\_

fiscal impact \_\_\_\_\_

fiscal note(s) \_\_\_\_\_

zero fiscal note Commerce + Econ Dev.

zero fiscal note(s) \_\_\_\_\_

SIGNING <u>DO</u> PASS	DP	OTHER RECOMMENDATIONS	DNP	NR	AM
		<i>Christ Taylor</i>	<input checked="" type="checkbox"/>		
		<i>[Signature]</i>	<input checked="" type="checkbox"/>		
		<i>[Signature]</i>	<input checked="" type="checkbox"/>		
		<i>[Signature]</i>	<input checked="" type="checkbox"/>		

*[Signature]*  
CHAIRMAN'S SIGNATURE

*New CS*

7-LS1282D /  
Utermoitte  
4/8/92

CS FOR HOUSE BILL NO. 317 ( )  
IN THE LEGISLATURE OF THE STATE OF ALASKA  
SEVENTEENTH LEGISLATURE - SECOND SESSION

BY

Offered:  
Referred:

Sponsor(s): REPRESENTATIVE SHARP BY REQUEST

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to liability insurance and bond requirements for guide-outfitters or marine  
2 mammal guide-outfitters."

3 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

4 \* Section 1. AS 08.54.395(a) is amended to read:

5 (a) A guide-outfitter or marine mammal guide-outfitter, while engaged in providing big  
6 game commercial hunting services shall carry, as a minimum, comprehensive general liability  
7 insurance of \$300,000 per occurrence or \$500,000 per annual aggregate or post a financial or  
8 cash bond in those amounts.

9 \* Sec. 2. AS 08.54.395(c) is amended to read:

10 (c) During the provision of big game commercial hunting services, an aircraft used by  
11 a guide-outfitter, marine mammal guide-outfitter, class-A assistant guide-outfitter, or assistant  
12 guide-outfitter to transport clients must carry aviation passenger liability insurance of at least  
13 \$100,000 per seat or must be subject to a financial bond in that amount. This subsection does  
14 not apply to an aircraft while that aircraft is being used by a guide-outfitter or marine

- 1 mammal guide-outfitter who
- 2 (1) contracts to guide-outfit three or less hunts a year;
- 3 (2) transports clients by aircraft for less than 20 hours a year; and
- 4 (3) includes in the contract for guide-outfitter services a statement that the
- 5 aircraft used to transport clients is not covered by the minimum aviation passenger liability
- 6 insurance or the bond that is otherwise required under this subsection.

7-LS1282D ✓  
Utermohle  
4/7/92

CS FOR HOUSE BILL NO. 317 ( )  
IN THE LEGISLATURE OF THE STATE OF ALASKA  
SEVENTEENTH LEGISLATURE - SECOND SESSION

BY

Offered:  
Referred:

Sponsor(s): REPRESENTATIVE SHARP BY REQUEST

A BILL

FOR AN ACT ENTITLED

1 "An Act amending the aviation passenger insurance or financial bond requirement for  
2 aircraft used by certain guide-outfitters or marine mammal guide-outfitters."

3 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

4 \* Section 1. AS 08.54.395(c) is amended to read:

5 (c) During the provision of big game commercial hunting services, an aircraft used by  
6 a guide-outfitter, marine mammal guide-outfitter, class-A assistant guide-outfitter, or assistant  
7 guide-outfitter to transport clients must carry aviation passenger liability insurance of at least  
8 \$100,000 per seat or must be subject to a financial bond in that amount. This subsection does  
9 not apply to an aircraft while that aircraft is being used by a guide-outfitter or marine  
10 mammal guide-outfitter who contracts to guide-outfit three or less hunts a year or who  
11 transports clients by aircraft for less than 20 hours a year.

# Alaska State Legislature

REPRESENTATIVE  
**BERT SHARP**

DISTRICT 20

MEMBER  
FINANCE COMMITTEE

FINANCE SUBCOMMITTEES  
GOVERNOR  
FISH AND GAME  
LABOR



FAIRBANKS

119 N CUSHMAN  
FAIRBANKS, ALASKA 99701  
(907) 452-7885/7886

WHILE IN JUNEAU

PO BOX V  
STATE CAPITOL  
JUNEAU, ALASKA 99811  
(907) 465-3004/3018

## House of Representatives

### SPONSOR STATEMENT Representative Bert Sharp HB 317

January 22, 1992

House Bill 317 would delete the requirement for liability insurance for registered guides doing their own flying.

The current insurance requirement is costly for small guide outfitters, particularly those who only conduct a few hunts for one or two individuals a few times a year.

It is inconceivable that an individual using a family airplane to conduct a small scale guide service be expected to carry the same insurance as an air taxi operator. The large guiding operations may be able to absorb these high costs, but the smaller guides are essentially put out of business as a result.

This is an example of a state mandated requirement that imposes extreme costs on family type businesses. It should be eliminated.



REPRESENTING  
GOLDEN HEART  
OF ALASKA

# Chairman's Summary

Alaska State  
Legislature



House  
Labor  
Commerce  
Committee

Date:

4-7-92

Bill Name  
and #:

HB 317 - Guide / Outfitter

Summary  
of Purpose:

To exempt small guides from  
the aviation insurance requirement

Fiscal Notes:

zero - Division of Insurance - (I ED)

Amendments  
Enclosed:

CS which narrows bill is in packet  
Recommendation: the original bill deleted the  
entire section. The CS just  
exempts small  
guides  
Y N DP NR DNP

Interest  
Groups  
Supporting:

Letters in packets from guides

Interest  
Groups  
Opposed:

The bill was originally introduced  
by request by Sharp

Interest  
Groups  
Opposed:

Dept of Commerce Occ Licensing says OK

No one has indicated opposition  
However, the current statute is  
the result of the  
major guide/outfitter overhaul  
last legislature. The ~~Task Force~~  
on ~~Guiding~~

Additional  
Issues:

The argument against the bill is  
that insurance is necessary regardless  
of the number of clients exposed.

Other:

See R.08.54.395 (a) will still cover

(Division of Insurance ready to testify)

## Concerns last meeting:

1. and vs or (3 hunts any no more than 20 hours/year)

→ CS page 2 line 3

2. Bonding requirements - allow cash bonds

→ CS page 1, line 8

3. Notice: Bruckman wanted confirmation of notice

→ CS page 2, lines 4-6

4. Will the flights be covered by general liability insurance

→ Answer "No" no coverage

There was no insurance requirement before the guide outfit bill, so no lower level to return to.

You could choose a lower amount of coverage, but the Division of Insurance doesn't think that will help the cost.

JNU MOD LIOCJAM

T/C NO: 22-04-007  
DATE: APRIL 7, 1992  
SPONSOR: HOUSE LABOR AND COMMERCE COMMITTEE  
SUBJECT: HE 560, HR 530, HR 457, HR 317, HR 294  
MODERATOR: MELBA  
SITE: FAIRBANKS

PARTICIPANT LIST

\*\*\*\*\*  
TESTIFIER

NAME/REPRESENTING	ADDRESS	PHONE	BILL NO.
1. CHUCK GRAY			HR 317
2. BUD HELNERICKS			HR 317
3. DAVE MORRIS			HR 317
4. BOB ELLIOTT			HR 317
5.			

This requirement is extremely onerous for those of us who only conduct one or two high-quality guided hunts each fall. The cost, about \$2500, which mostly goes to London, makes it unprofitable for low-volume guides to operate.

If given the opportunity to testify at a tele-conference, several of us can give your committee more reasons the requirement should be dropped.

Sincerely,

Charles Gray

CG:cga