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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION FIVE

ZENGEN, INC., Plaintiff and Appellant, v. COMERICA BANK, Defendant and Respondent.	B179022 (Los Angeles County Super. Ct. No. BC290637)

APPEAL from a judgment of the Superior Court of Los Angeles County. Teresa Sanchez-Gordon, Judge. Affirmed.

Burton V. McCullough for Plaintiff and Appellant.

Buchalter, Nemer, Fields & Younger and Michael L. Wachtell, Jeffrey S. Wruble, and Robert S. Addison, Jr., for Defendant and Respondent.

Plaintiff Zengen, Inc. ("Zengen") appeals the judgment entered in favor of Comerica Bank (the "Bank") following the latter's successful demurrer and motion for summary judgment in Zengen's lawsuit to recover unauthorized funds transfers totaling $4.6 million. In this opinion, we conclude that Zengen's common law claims for breach of contract, negligence, return of deposit and money had and received are displaced by the provisions of the UCC. We also consider the content of the notice required to be given to a receiving bank under Uniform Commercial Code section 11505 in order to preserve a customer's right to maintain an action for a refund under section 11204. We conclude that the purpose of the notice requirement is to put the receiving bank on notice that the customer considers the bank liable for the unauthorized funds transfer, and that the customer's notification to the bank that the subject payment orders were "unauthorized" and "fraudulent," standing alone, does not satisfy this requirement. Consequently, we affirm the trial court's grant of summary judgment.

FACTUAL AND PROCEDURAL HISTORY

Zengen is a biopharmaceutical company formed in May 1999. Shortly after its incorporation, Zengen opened several bank accounts, including money market account number 88-012-298 (the "298 Account") at Imperial Bank, which has since been acquired by Comerica Bank (the "Bank"). In connection with the opening of its accounts, including the 298 Account, a Business Signature Card and a Funds Transfer Authorization agreement were executed by Zengen's Chief Executive Officer, Johnson Liu, and its Chief Financial Officer, Fung Yen, the company's authorized signatories.[1] While Liu had unlimited check signing authority, Yen's authority was limited to checks not exceeding $10,000.

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[1]Given Mr. Liu's acknowledgement in deposition that he intended the Funds Transfer Authorization to apply to the 298 Account and authorized funds transfers out of that account, it is immaterial that the Authorization itself did not list the 298 Account by number.

From mid-2000 to early 2001, Yen embezzled $4.6 million from Zengen by directing four funds transfers from the 298 Account to an account Yen opened in the name of Zengen at Chinatrust Bank. To accomplish this feat, Yen formed a British Virgin Islands corporation which he named Zengen, Inc. He then opened an account at Chinatrust Bank in the name of this new corporation with an initial deposit of $1,000, with himself as the sole authorized signatory. Between July 11, 2000 and February 5, 2001, the Bank processed four payment orders, which facially appeared to be signed and authorized by Johnson Liu (as was customary, they were faxed to the Bank for processing and payment), and which are the subject of this lawsuit. These four payment orders requested the Bank to draw funds out of the 298 Account and to wire them to Zengen's account at Chinatrust Bank in the amounts and on the dates as follows: $185,000 on July 11, 2000; $550,000 on September 11, 2000; $1,500,000 on November 22, 2000; and $1,700,000 on February 5, 2001 (collectively, the "Payment Orders"). These transactions appeared on Zengen's monthly bank statements, which Zengen acknowledges it received.

Presumably because Zengen's account statements and transaction notices were addressed to Yen as the company's Chief Financial Officer, the latter's defalcation was not discovered immediately. Zengen first learned that something was amiss on June 13, 2001. Zengen's Office Manager, Regina Samuel-Ramcharitar, worked with Tony Galvez of the Bank to uncover the unauthorized activity concerning the 298 Account. According to Zengen, "By July 12, 2001, Samuel-Ramcharitar had specifically told Galvez that Zengen did not authorize the four wire transfers [at issue] and that it appeared that Yen had fraudulently transferred the money." By no later than August of 2001, when Zengen filed a report with the Los Angeles District Attorney's office which included details of the four Payment Orders, Zengen had concluded that Yen had stolen money from the company via the wire transfers from the 298 Account to Chinatrust Bank. By that time, Yen had disappeared with all of the company's financial records, and could not be located.

On February 20, 2003, Zengen filed its complaint against the Bank for breach of contract, negligence, refund of payment pursuant to Uniform Commercial Code

Section 11204, return of deposit, and money had and received.[2] The Bank filed demurrers to the various causes of action alleged in the complaint. The trial court sustained without leave to amend the demurrer to the negligence cause of action on the ground that the Uniform Commercial Code had displaced a negligence claim, sustained with leave to amend the demurrers to the breach of contract and common count causes of action on the basis that the contract was not attached to the complaint, and overruled the demurrer to the claim for refund.

Zengen filed its first amended complaint, realleging the breach of contract claim (and attaching contracts as Exhibits A and B), the claim for refund of payment pursuant to section 11204, and the common counts of return of deposit and money had and received. The Bank demurred to the breach of contract and common counts on the ground that Division 11 of the California Uniform Commercial Code, section 11101 et seq. ("UCC") displaced those claims. The trial court overruled the demurrers.

The Bank filed a motion for summary judgment, arguing that (1) the UCC "preempts"[3] Zengen's non-UCC causes of action that are based on the same underlying circumstances and the same injury; and (2) Zengen's failure to timely notify the Bank of its objection to the debit of the 298 Account defeated the section 11204 claim for refund. The trial court granted the Bank's motion, ruling that the breach of contract and common count causes of action were preempted by the UCC. The court further concluded that Zengen could not prevail on its claim for refund because it failed to notify the Bank of its objection to the payments within the time prescribed by section 11505, and was thus precluded from asserting that the Bank was not entitled to retain the payments.

Zengen timely appealed.

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[2] The complaint also named as defendants Chinatrust Bank, Yen, and the corporations controlled by Yen. These additional defendants are not parties to this appeal.

[3] We adopt the terminology used by the parties and the trial court, and use the terms "preempted" and "displaced" interchangeably.

CONTENTIONS

Zengen contends on appeal that the trial court erred in the following particulars: (1) by granting the Bank's motion for summary judgment on Zengen's non-UCC causes of action after it had previously overruled a demurrer based on those same grounds; (2) in ruling that the UCC preempts the non-UCC causes of action; and (3) in concluding that section 11505 bars Zengen's recovery. We discuss each contention in turn.

DISCUSSION

1. *The Bank's motion for summary judgment*

The Bank demurred to the first amended complaint's causes of action for breach of contract, return of deposit, and money had and received, arguing that they were preempted by the UCC. The trial court overruled the demurrers, and the Bank filed its answer. The Bank later filed a motion for summary judgment, arguing that there were no triable issues of fact and, as a matter of law, Zengen could not prevail on its breach of contract, return of deposit and money had and received causes of action since those claims were preempted by the UCC. The trial court agreed, and granted the motion.

Zengen maintains on appeal that "where a general demurrer to the complaint has been overruled and a motion for summary judgment is subsequently brought contesting again the sufficiency of the complaint to state a cause of action, the motion is treated as a motion for judgment on the pleadings." Zengen then argues that Code of Civil Procedure section 438 prohibits a defendant whose demurrer to the complaint has been overruled from bringing a motion for judgment on the pleadings unless "there has been a material change in applicable case law or statute since the ruling on the demurrer." (Code Civ. Proc., § 438, subd. (g)(1).)

The argument lacks merit. The trial court heard and ruled on the Bank's motion for summary judgment. If that ruling was correct – that is to say, the challenged causes of action are indeed preempted by the UCC – then Zengen suffers no prejudice from being spared a trial, and possibly an appeal, it will necessarily lose. If the ruling was

incorrect, as Zengen argues on appeal, it suffers no prejudice, as this court will reverse the ruling. We turn, then, to the merits Zengen's appeal.

2. *The Bank's liability for the Payment Orders*

We begin with an explication of Division 11 of the California Commercial Code,[4] California's adoption of Article 4A of the Uniform Commercial Code, which applies to all funds transfers except transfers subject to the Electronic Funds Transfer Act of 1978, 15 U.S.C. § 1693 et seq.[5] (§§ 11102, 11108.)

A "payment order" is the "instruction of a sender to a receiving bank . . . to pay, or to cause another bank to pay, a fixed or determinable amount of money to a beneficiary . . . ." (§ 11103, subd. (a)(1).) Section 11202, subdivision (a) provides that a payment order "received by the receiving bank is the authorized order of the person identified as sender if that person authorized the order or is otherwise bound by it under the law of agency." Zengen alleges, and we accept as true for purposes of our review, that the Payment Orders were not authorized as provided in this section.

Section 11202, subdivision (b) provides in pertinent part: "If a bank and its customer have agreed that the authenticity of payment orders issued to the bank in the name of the customer as sender will be verified pursuant to a security procedure, a payment order received by the receiving bank is effective as the order of the customer, whether or not authorized, if (i) the security procedure is a commercially reasonable method of providing security against unauthorized payment orders, and (ii) the bank proves that it accepted the payment order in good faith and in compliance with the security procedure and any written agreement or instruction of the customer restricting acceptance of payment orders issued in the name of the customer. . . ." Section 11203

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[4] Further statutory references are to this Code unless otherwise indicated.

[5] The Electronic Funds Transfer Act, which covers bank accounts opened for personal, family or household purposes, is not relevant to this discussion.

provides: "(a) If an accepted payment order is not, under subdivision (a) of Section 11202, an authorized order of a customer identified as sender, but is effective as an order of the customer pursuant to subdivision (b) of 11202, the following rules apply: [¶] (1) By express written agreement, the receiving bank may limit the extent to which it is entitled to enforce or retain payment of the payment order. [¶] (2) The receiving bank is not entitled to enforce or retain payment of the payment order if the customer proves that the order was not caused, directly or indirectly, by a person (i) entrusted at any time with duties to act for the customer with respect to payment orders or the security procedure, or (ii) who obtained access to transmitting facilities of the customer or who obtained, from a source controlled by the customer and without authority of the receiving bank, information facilitating breach of the security procedure, regardless of how the information was obtained or whether the customer was at fault. Information includes any access device, computer software, or the like." (§ 11202, subd. (a).)

Section 11204, subdivision (a) provides in pertinent part: "If a receiving bank accepts a payment order issued in the name of its customer as sender which is (i) not authorized and not effective as the order of the customer under Section 11202, or (ii) not enforceable, in whole or in part, against the customer under Section 11203, the bank shall refund any payment of the payment order received from the customer to the extent the bank is not entitled to enforce payment and shall pay interest on the refundable amount calculated from the date the bank received payment to the date of the refund." The facts alleged by Zengen, and not disputed on summary judgment, establish that the Payment Orders were unauthorized; they do not speak, however, to whether the orders were unverified and therefore not effective as the orders of Zengen pursuant to § 11202, subdivision (b), or to whether the Bank was not entitled to retain payment pursuant to § 11203.

a. *Zengen's negligence, breach of contract and common count causes of action*

Zengen brought causes of action against the Bank for negligence, breach of contract, return of deposit, and money had and received.[6] The Bank argued that these claims were preempted by the UCC, and the trial court so ruled. We agree.

As can be seen from the foregoing, sections 11201 through 11204 provide a detailed scheme for analyzing the rights, duties and liabilities of banks and their customers in connection with the authorization and verification of payment orders. Analysis of a funds transfer under these sections results in a determination of whether or not the funds transfer was "authorized," and provides a very specific scheme for allocation of loss. As one court has noted, "[t]his allocation of loss is so integral to the structure of Article 4A that it may not be varied by contract." (*Regatos v. North Fork Bank* (2003) 257 F.Supp.2d 632, 643.)

The express statutory language of Division 11 states that it is the sole governing body of law for the rights, duties and liabilities associated with funds transfers, and expressly preempts all other principles of law or equity regarding funds transfers: "Except as otherwise provided in Section 11108, this division applies to funds transfers defined in Section 11104." (§ 11102.) The comment to section 11102 states in pertinent part:

> "In the drafting of Article 4A, a deliberate decision was made to write on a clean slate and to treat a funds transfer as a unique method of payment to be

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[6] The Bank's alleged negligence consisted of failing to review its records, which review would have revealed that the Funds Transfer Authorization executed by Zengen did not list the 298 Account as an account subject to wire transfers, and "failing to call Zengen, the purported 'sender' of the Payment Orders, to both verify the authority of Yen to issue the Payment Orders and to obtain proper documentation of such authority." As noted above, Mr. Liu testified at deposition that Zengen intended that the 298 Account be subject to the Funds Transfer Agreement, and thus there is no disputed issue of fact concerning the Bank's authority to accept payment orders issued against that account. Additionally, there is no allegation that telephone verification of authority was among the security procedures agreed to by the parties, such that the Bank's failure to verify the Payments Orders by telephone constituted breach of an agreed security procedure.

governed by unique rules that address the particular issues raised by this method of payment. A deliberate decision was also made to use precise and detailed rules to assign responsibility, define behavioral norms, allocate risks and establish limits on liability, rather than to rely on broadly stated, flexible principles. In the drafting of these rules, a critical consideration was that the various parties to funds transfers need to be able to predict risk with certainty, to insure against risk, to adjust operational and security procedures, and to price funds transfers appropriately. This consideration is particularly important given the very large amounts of money that are involved in funds transfers.

"Funds transfers involve competing interests – those of the banks that provide funds transfer services and the commercial and financial organizations that use the services, as well as the public interest. These competing interests were represented in the drafting process and they were thoroughly considered. The rules that emerged represent a careful and delicate balancing of those interests and are intended to be the exclusive means of determining the rights, duties and liability of the affected parties in any situation covered by particular provisions of the Article. Consequently, resort to principles of law or equity outside of Article 4A is not appropriate to create rights, duties and liabilities inconsistent with those stated in this Article."

Thus, in unequivocal language, the legislature has stated its intent to provide an exclusive set of rules, including an exclusive set of remedies, pertaining to funds transfers. Witkin confirms this intent: "The 1990 Legislature enacted Article 4A of the Uniform Commercial Code as Division 11 of the California Uniform Commercial Code (U.C.C. 11101 et seq.), entitled 'Funds Transfers.' The focus of the Article is a type of payment, commonly referred to as a 'wholesale wire transfer,' which is used almost exclusively between business or financial institutions. Payments made by wire transfer, as distinguished from payments made by checks or credit cards, or from electronically based consumer payments, require a separate body of law that addresses the unique operational and policy issues presented by the method. It was therefore the intent of the

drafters of Article 4A to provide a comprehensive body of law to govern the rights and obligations resulting from wire transfers. [Citations.]" (4 Witkin, *Summary of California Law* (10th ed. 2005) Negotiable Instruments, § 132.)

Thus, Division 11 provides that common law causes of action based on allegedly unauthorized funds transfers are preempted in two specific areas: (1) where the common law claims would create rights, duties, or liabilities inconsistent with Division 11; and (2) where the circumstances giving rise to the common law claims are specifically covered by the provisions of Division 11.

Zengen argues that its negligence cause of action is not preempted because the negligent acts which it alleges the Bank engaged in, consisting of its failure to discover that Zengen had not executed a Funds Transfer Authorization with respect to the Zengen 298 Account, occurred outside the scope of Division 11, that is, ". . . outside the series of transactions beginning with the originator's payment order . . . ." Zengen further contends that, even if the negligent conduct alleged in the complaint falls within the scope of Division 11, "the principles of law upon which the claim for negligence is based are not inconsistent with the provisions of Division 11. Division 11 has no provisions that speak to the failure of a bank to check its own documentation to see if the customer has authorized the transfer of funds via wire transfer or whether the customer has authorized a particular person to initiate such a transfer. The Code does not preclude the application of principles of law where the Code does not contain specific provisions covering the situation – its only displaces principles of law that specifically create rights, duties, or liabilities inconsistent with those stated in the Code."

We do not agree. Although the UCC does not catalog all the ways in which a bank may execute an unauthorized wire transfer, it certainly specifies the consequences for doing so. Section 11201 et seq. sets forth the respective rights, duties and liabilities of the parties upon the issuance and acceptance of a payment order under Division 11. Thus, as the trial court stated, "The question is whether the situation in this case falls within the situations covered by the UCC." And even Zengen acknowledges that it does,

since it has brought a refund cause of action against the Bank based on UCC section 11204.

The sole basis for Zengen's lawsuit is its contention that the Bank wrongfully accepted and executed unauthorized payment orders from Yen, and its alleged damages consist solely of a claim for refund of the $4.6 million so transferred. This claim is entirely covered by Division 11 of the Commercial Code.

Although it appears that this court is the first in California to consider the preemptive effect of Division 11, courts in other jurisdictions have reached the same conclusion. (See, e.g., *Fitts v. AmSouth Bank* (Ala. 2005) 917 So.2d 818 [common law claims displaced]; *Corfan Banco Asuncion Paraguay v. Ocean Bank* (1998) 715 So.2d 967, 971 [negligence claim preempted]; *Aleo International, Ltd. v. Citibank, N.A.* (1994) 160 Misc.2d 950, 951 [negligence claim preempted]; *Hedged Investment Partners, L.P. v. Norwest Bank of Minnesota., N.A.* (1998) 578 N.W.2d 765 [contractual duties going beyond the scope of Article 4A not preempted].) Thus, for instance, in *Corfan Banco Asuncion Paraguay v. Ocean Bank*, *supra*, the Florida Court of Appeal held that Article 4A preempted the plaintiff's negligence claim, stating: "The uniformity and certainty sought by the statute for these transactions could not possibly exist if parties could opt to sue by way of pre-Code remedies where the statute has specifically defined the duties, rights and liabilities of the parties." (715 So.2d at p. 971.) We fully concur in this reasoning. Since the UCC provides a remedy for a bank's unauthorized wire transfer, it is necessarily the exclusive remedy. (*Ibid*.; accord *Aleo International, Ltd. v. Citibank*, *supra*, 160 Misc.2d 950 [cause of action for common law negligence barred by UCC wire transfer provisions because conduct of banks involved were directly regulated by the UCC].)

In sum, the facts of this case fall squarely within the provisions of Division 11 of the Commercial Code. This case is about unauthorized wire funds transfers. Zengen's non-UCC causes of action are based solely on the analysis prescribed by Division 11 – that the Bank processed unauthorized payment orders. Because the UCC provides a

remedy to Zengen under these circumstances, it preempts the common law causes of action alleged in the Zengen's complaint.

b. *Zengen's UCC claim*

Zengen also sued the Bank pursuant to Commercial Code section 11204 for a refund of the payments made to the Bank by charging the amounts of the Payment Orders against the 298 Account. The Bank sought summary adjudication of this claim, contending that the undisputed facts established that Zengen failed to notify the Bank of an objection to the debiting of the latter's account within one year of notice of any of the fund transfers as required by section 11505, and thus the action was barred as a matter of law.

Section 11505 provides: "If a receiving bank has received payment from the customer with respect to a payment order issued in the name of the customer as sender and accepted by the bank, and the customer received notification reasonably identifying the order, the customer is precluded from asserting that the bank is not entitled to retain the payment unless the customer notifies the bank of the customer's objection to the payment within one year after the notification was received by the customer."[7] Zengen maintained that it had complied with this statute by timely notifying the Bank that it "had 'accepted' and 'executed' unauthorized Payment Orders," and that "the transfer of funds

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[7] The Comment to this section states: "This section is in the nature of a statute of repose for objecting to debits made to the customer's account. A receiving bank that executes payment orders of a customer may have received payment from the customer by debiting the customer's account with respect to a payment order that the customer was not required to pay. For example, the payment order may not have been authorized or verified pursuant to Section 4A-202 or the funds transfer may not have been completed. In either case the receiving bank is obliged to refund the payment to the customer and this obligation to refund payment cannot be varied by agreement. Section 4A-204 and Section 4A-402. . . . Under 4A-505, however, the obligation to refund may not be asserted by the customer if the customer has not objected to the debiting of the account within one year after the customer received notification of the debit."

was fraudulent." The trial court determined the notice provided did not satisfy the requirements of section 11505, and entered summary judgment for the Bank.

UCC section 11204 in pertinent part provides: "If a receiving bank accepts a payment order issued in the name of its customer as sender which is (i) not authorized and not effective as the order of the customer under Section 11202, or (ii) not enforceable, in whole or in part, against the customer under Section 11203, the bank shall refund any payment of the payment order received from the customer to the extent the bank is not entitled to enforce payment . . . ." As the Official Comment to section 11204 explains, "Section 11204 applies only to cases in which (i) no commercially reasonable security procedure is in effect, (ii) the bank did not comply with a commercially reasonable security procedure that was in effect, (iii) the sender can prove, pursuant to section 11203, subdivision (a)(2), that the culprit did not obtain confidential security information controlled by the customer, or (iv) the bank, pursuant to section 11203, subdivision (a)(1) agreed to take all or part of the loss resulting from an unauthorized payment order. In each of these cases the bank takes the risk of loss with respect to an unauthorized payment order because the bank is not entitled to payment from the customer with respect to the order. The bank normally debits the customer's account or otherwise receives payment from the customer shortly after acceptance of the payment order. Subsection (a) of section 11204 states that the bank must recredit the account or refund payment to the extent the bank is not entitled to enforce payment."

As the foregoing statutory scheme makes clear, the existence and use of security procedures is a key element in allocating liability under the Commercial Code.[8] Official Comment to § 11201 states: "The question of whether loss that may result from the transmission of a spurious or erroneous payment order will be borne by the receiving bank or the sender or purported sender is affected by whether a security procedure was or was not in effect and whether there was or was not compliance with the procedure."

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[8] The dissent relegates this issue to an affirmative defense. We cannot agree with this characterization.

"Section 4A-203, 4A-204, and 4A-205 contain detailed rules for liability allocation, rules which depend, in part, upon whether a security procedure is in place and used." (Hawkland & Moreno UCC Series § 4A-201:1 (Art 4A).) As one commentator puts it, "In general, section 4A-201, 4A-202, and 4A-203 tell the bank that it can rely [on] orders that are transmitted in accordance with a reasonable security procedure and can charge a customer's account even when those orders have been sent by a thief." (3 White and Summers, Uniform Commercial Code (4th ed. 1995) § 24-5, p. 79.) In order to state a claim for refund under section 11204, Zengen must allege not only that the Payment Orders were "unauthorized" under section 11202, subdivision (a), but that they were "not effective as the order of the customer" under section 11202, subdivision (b), or "not enforceable, in whole or in part, against the customer" under section 11203.

We make this point not to suggest that Zengen's UCC claim was subject to demurrer, but to make clear that Zengen's notification to the Bank that the Payment Orders were unauthorized did not serve to inform the Bank that Zengen was entitled to a refund under section 11204. And it is the untimely notification of the latter information which precludes a customer from "asserting that the bank is not entitled to retain the payment unless the customer notifies the bank of the customer's objection to the payment within one year after the notification was received by the customer." (§ 11505.)

Thus, the question before us is whether Zengen's notification to the Bank that the wire transfers were "unauthorized" satisfied the statute's requirement that the customer "object to the payment." And under our interpretation of section 11505, the critical "fact" which Zengen was required to communicate to the Bank was that the Bank was liable for the fraudulent transfers.

Zengen first contacted the Bank and discussed the Funds Transfers in June 2001, less than one year after the first suspect transfer in July 2000. Specifically, sometime before June 27, 2001, Zengen's office manager, Regina Samuel-Ramcharitar, told Tony Galvez of the Bank that "Zengen had not been aware of the transfer of the funds, that Mr. Liu had not signed the wire transfer request, that Mr. Yen himself had no authority to transfer the funds, that the wire transfer request was fraudulent and had not been

authorized by Zengen, and that Zengen believed that Mr. Yen had stolen the money." On July 10 or 11, 2001, after further investigation, Ms. Samuel-Ramcharitar told Mr. Galvez that Zengen "had received microfilm documents from Chinatrust Bank showing additional wire transfers from Imperial Bank to Chinatrust Bank, gave him the dates and amounts set forth above, and told him that these transfers, like the transfer of the $1,700,000.00 on February 5, 2001, were fraudulent and unauthorized, that it appeared that Mr. Yen had stolen this money as well, and asked him to obtain for us the bank's documentation on those transfers. In this and all my conversations with Mr. Galvez, I continued to keep Mr. Galvez apprised of the facts as we learned them concerning Mr. Yen's fraudulent transfers of funds from the Zengen account at Imperial Bank to the supposed Zengen account at Chinatrust Bank. By July 12, 2001, I had specifically told Mr. Galvez that Zengen did not authorize the four wire transfers identified in this declaration and that it appeared that Mr. Yen had fraudulently transferred the money." In addition to Ms. Samuel-Ramcharitar's conversations with Mr. Galvez, Mr. Liu spoke with Julie Yen (no relation to Fung Yen) of the Bank regarding the wire transfers. During that telephone conversation, Mr. Liu informed Ms. Yen that "I didn't authorize any of those transactions. I suspect that he must have cut and paste my signature if you saw both signatures in there." Zengen relies on Ms. Samuel-Ramcharitar's telephone conversations with Mr. Galvez, and Mr. Liu's telephone conversation with Ms. Yen as Zengen's notification to the Bank of its objection to the debiting of the payment orders from Zengen Account 298.

The Bank argues, and the trial court found, that the foregoing notification did not satisfy the requirements of Commercial Code section 11505. We agree.

Zengen established that it had numerous conversations with the Bank concerning the wire transfers, and made clear to the Bank that these transfers were not authorized by Zengen. The Bank concedes as much. As we have seen, however, liability for an unauthorized payment order can lie with either the customer/sender or with the bank, depending upon the security procedures, if any, in effect. In the absence of an agreed, commercially reasonable security procedure, the bank is liable for the loss. (§ 11202.)

Likewise, if the bank fails to comply with the agreed security procedure, the bank is liable for the loss. (§ 11202.) If, however, the bank complies with the agreed security procedure, then (subject to § 11203 which is not at issue here) the customer bears the loss, notwithstanding that that payment order was unauthorized.

When Zengen notified the Bank of Yen's defalcation, the Bank learned that the Payment Orders were unauthorized. It did not learn, however, that Zengen placed liability for the loss with the Bank, and would look to the Bank to make good the loss. Indeed, while Zengen voiced no objection to the Bank's actions, it hired outside legal counsel to assist it in its attempt to recover its losses; made written demand to ChinaTrust Bank to turn over its account records, close the account and return all money in the account to Zengen; hired a second law firm to file a written criminal report with the Los Angeles District Attorney's Office and to investigate Yen's whereabouts; filed a lawsuit against Yen in Federal District Court seeking recovery of the $4.6 million; and, although Zengen's lawyers corresponded with the Bank requesting copies of its account records, it did not demand that the Bank refund the money wired out of the 298 account by means of the four Payments Orders, or otherwise object to the Bank's actions in accepting the executing the Payment Orders and in debiting the 298 account. That Zengen took the foregoing actions in aggressive pursuit of the recovery of the stolen funds without ever making demand of any kind on the Bank is simply inconsistent with its position in this lawsuit that the Bank was required to refund to it the $4.6 million stolen by Yen, and that it notified the Bank of that fact within one year of its discovery of the theft.[9]

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[9] Aside from ascribing to us a "waiver theory" that no where appears in our opinion, the dissent's reliance on *Anheuser-Busch, Inc. v. Starley* (1946) 28 Cal.2d 347 is perplexing. *Anheuser-Busch* applied the collateral source rule – a tortfeasor is not permitted to reduce the amount he is required to pay in damages because of benefits received by the injured person from a collateral source – concluding that the negligent defendant could not defeat the plaintiff's claim simply because the plaintiff had been fully compensated for its loss by a third party wholly independent of the defendant. In other words, double recovery was not an impediment to plaintiff's negligence claim. Here, however, Zengen could recover its $4.6 million loss but once; a recovery from Yen, or

The dissent maintains that the only reasonable inference to be drawn from Zengen's notification to the Bank that the Payment Orders were fraudulent and unauthorized is that the Bank was liable for them. Because an unauthorized transaction does not necessarily result in liability to the bank, we do agree that there is but one inference to be drawn from this fact.[10] The answer to the dissent's rhetorical question – why else would a customer notify a bank that payment orders were unauthorized if it was not to object to the payment of those orders? – seems self-evident to us: to ensure that the Bank does not accept and execute additional payment orders for which Zengen might otherwise be liable under the provisions of the UCC.

In sum, Zengen's notification to the Bank that the Payment Orders were unauthorized, without objecting to the debiting of its account, or demanding that the Bank credit its account in the amount of the executed orders, indeed without any indication that Zengen believed that the Bank had acted inappropriately or was responsible to Zengen for the loss, was not "an objection to the payment" under UCC section 11505. Zengen first notified the Bank of its objection to the payment in February

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ChinaTrust Bank, or any other source, would preclude a second recovery from the Bank. It is unusual, to say the least, for a defrauded party to by-pass a deep-pocket corporate defendant doing business in its domicile which it believes is liable for its loss in favor of a thief who absconded to a far-off foreign jurisdiction, and at least suggests that, at the time that Zengen hired multiple lawyers to pursue all legal avenues available to it, it either did not believe that the Bank was liable for the loss, or did not want to make a demand against the Bank.

[10] We do not believe that this case permits the equitable or liberal interpretation of section 11505 urged by the dissent. The Comment to section 11202 sets forth the intent of the drafters of the Code. Because funds transfers are a unique method of payment, the drafters made a "deliberate decision" to use "precise and detailed rules to assign responsibility, define behavioral norms, allocate risks and establish limits on liability, rather than to rely on broadly stated, flexible principles." These rules are intended to be the exclusive means of determining the rights, duties and liabilities of the parties, and ". . . resort to principles of law and equity outside of Article 4A is not appropriate to create rights, duties and liabilities in connection with those stated in the Article."

2003, when it filed its complaint in this lawsuit. Because this notification occurred more than one year after Zengen learned of Yen's unauthorized transactions, it cannot recover under the Commercial Code.[11]

[11] Zengen also argues that the "cryptic reference in its monthly statements that there were 'outgoing wire' transfers in stated amounts" did not satisfy the Code requirement that the bank must "'reasonably' identify the 'payment order' for the customer." Given our conclusion that Zengen did not object to the payments until the filing of its complaint, the adequacy of the monthly statements is irrelevant, since the Bank identified the payment orders in response to Zengen's inquiries in June and July of 2001. Moreover, as a result of this ruling, we need not consider Zengen's assignment of error concerning the trial court's ruling striking the allegations and prayer for interest on the basis of Zengen's failure to notify the Bank of the unauthorized payment orders within the 90-day period prescribed by Section 11204.

DISPOSITION

The judgment is affirmed.

CERTIFIED FOR PUBLICATION IN THE OFFICIAL REPORTS

ARMSTRONG, Acting P.J.

I concur:

KRIEGLER, J.

CERTIFIED FOR PUBLICATION

MOSK, J., Dissenting and Concurring

I respectfully dissent as to the barring of claims by virtue of a period of repose. As to the issue of displacement covering the other causes of action, with some reservation, I concur in the result.

A. California Commercial Code Section 11505

The trial court held that plaintiff Zengen, Inc.'s (Zengen) claim under California Commercial Code (Commercial Code) section 11204 was barred by the time limitation or period of repose in Commercial Code section 11505 (Uniform Commercial Code (UCC) section 4A-505). The issue is, what constitutes notification to a bank "of the customer's objection to the payment" by the bank of a payment order for purposes of the one-year period of repose under Commercial Code section 11505? Within the required one-year period, Zengen specifically informed Imperial Bank, the predecessor of defendant Comerica Bank (Bank), that the transfers in issue were fraudulent and unauthorized. Having been so informed, the Bank was on notice that the payment orders were fraudulent and the transfers unauthorized. Thus, the Bank had knowledge that it had exceeded its authorization by Zengen.

The trial court concluded that the notification did not satisfy the objection requirement of Commercial Code section 11505 because Zengen did not specifically notify the Bank that the debiting of Zengen's account was improper, unauthorized, or objectionable. It would follow that under Commercial Code section 11505, in order not to be subject to a time limitation, the customer must not only notify a bank within one year that an order was fraudulent and unauthorized, but specify to the bank that the

debiting of the account was improper, unauthorized, or objectionable, which specification constitutes the required "objection to the payment."

Such a strained and hypertechnical reading of Commercial Code section 11505 is unsupported by any authorities. Upon receiving notice that payment orders were unauthorized, the Bank should have known that the debiting of accounts was improper and that it was potentially liable to its customer. Such knowledge satisfies the purposes of Commercial Code section 11505 that a bank be on notice of an objection by the customer within one year of the customer receiving notice. (See *Regatos v. North Fork Bank* (2005) 804 N.Y.S.2d 713, 717 [purpose of period of repose provision to "promote finality of banking operations and to give the bank relief from unknown liabilities of potentially indefinite duration"].)

The notice here satisfies purposes of a period of repose or statute of limitations to guard against the loss of evidence, fading of memories and disappearance of witnesses. (See 3 Witkin, Cal. Procedure (4th ed. 1996) Actions, § 408, p. 513 [purpose of limitation periods].) Based on the notice, the Bank knew there was a serious problem with the payment orders and began jointly investigating the matter with Zengen. Indeed, Zengen went so far as to ask the Bank to accumulate information on the matter. Under these circumstances, it is difficult to discern what more Zengen could have done or what other information the Bank needed to put it on notice of a claim for reimbursement. It should be noted that authorities equate "objection" with "notice" as defined in Commercial Code section 1201, subdivisions 25 to 27. (7 Lawrence's Anderson on the Uniform Commercial Code (3d ed. 2000) § 4A-505:5, p. 713.)

Why else would a customer repeatedly notify a bank that payment orders were unauthorized[1] if it was not to object to the payment of those orders? And what else could a bank infer from such a notification other than that the customer is looking to the bank to rectify the situation? The answers to these rhetorical questions seem self-evident to me.

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[1] Once would be enough to advise the bank not to execute additional unauthorized payment orders.

Authorities do not suggest that more than notification of an unauthorized statement is required. (See *Regatos v. North Fork Bank* (2d Cir. 2005) 396 F.3d 493, 494 ["Immediately upon viewing his statement . . . Regatos informed CBNY that the two transfers at issue were unauthorized"]; *Grabowski v. Bank of Boston* (D.Mass.1997) 997 F.Supp 111, 119 [provision "creates a one year notice requirement"].) One authority has analogized the objection requirement to reporting an error and refers to the period of repose as "more than a year passed before *complaint* . . . ." (3 White and Summers, Uniform Commercial Code (4th ed. 1995) § 24-8, pp. 87-88 (emphasis added) (White and Summers).) Zengen's notification was the equivalent of a complaint.

The Bank argues that merely informing it that the payment order was unauthorized is not sufficient because under Commercial Code section 11202, subdivision (b), an unauthorized payment may not subject a bank to liability if, for example, the bank had complied with agreed-upon security procedures and had accepted the payment orders in good faith. For purposes of the summary judgment, the Bank has not asserted that such conditions existed here. That there is no allegation of agreed-upon security procedures enhances the impact of the notice of unauthorized transfers in this case.

Moreover, that the Bank may have a defense to a claim seems irrelevant as to the notice issue. The issue is whether Zengen's communication constituted sufficient notice to avoid the statutory time limitation. Perhaps it may be possible to convey information about an unauthorized payment without that communication being an "objection." That does not appear to me to be a fair interpretation of the notifications of the payment here. An "objection" is not necessarily an express threat of litigation or a demand for some action. It is reasonable to assume that by notifying the Bank of unauthorized payments of millions of dollars, Zengen was "opposed to," and "disapproved of," the payment. (See Webster's 3d New Internat. Dict. (2005) "objection," p. 1555.)

Zengen's initial claim against the alleged wrongdoer Yen is not, as argued by the Bank, inconsistent with Zengen's position that the Bank was required to refund to Zengen the monies claimed to be stolen by Yen. Pursuing the most culpable wrongdoer first is a rational reaction and not one that should be construed as an acknowledgment of no claim

against others. As this case shows, claims against “a deep-pocket corporate defendant” (maj. opn., fn. 9) often results in vigorous resistance. (Cf. *Anheuser-Busch, Inc. v. Starley* (1946) 28 Cal.2d 347, 349 [“[w]here a person suffers personal injury or property damage by reason of the wrongful act of another, an action against the wrongdoer for the damages suffered is not precluded nor is the amount of damages reduced by the receipt by him of payment for his loss from a source wholly independent of the wrongdoer”].)

The Bank relies on the UCC Comment to what is Commercial Code section 11505, that “the obligation to refund may not be asserted by the customer if the customer has not objected to the debiting of the account within one year . . . .” This statement cannot be taken literally because fund transfers can be made without debiting an account—for example when one customer who does not have an account pays money to the bank when requesting the transfer. (See Cal. U. Com. Code, § 11103(a)(1)(ii) [instruction is “payment order” if “receiving bank is to be reimbursed by debiting an account of, or *otherwise receiving payment from, the sender*”] (italics added); see also 1 Lawrence’s Anderson on the Uniform Commercial Code (3d ed. 2003) § 1-102:34, p. 59 [“although courts give substantial deference to the comments, courts will reject a comment when the comment is in conflict with the court’s view of the meaning of the text of the UCC itself”].) Moreover, neither the UCC nor the comment specifies the form or content of the objection. If, as the Bank suggests, an objection must be in the form of a lawsuit, demand or other formal notice of claim, surely either the UCC or the comment would have alluded to such a rigid procedural requirement.

Based on the undisputed facts, I believe Zengen’s claims are not barred by section 11505. But even if that cannot be established as a matter of law, at the very least, there would be a question of fact as to the nature and meaning of Zengen’s communications to the Bank for the purposes of determining whether the claim is time-barred. (See Cal. U. Com. Code, §§ 1201(25)(C), (26), (27) [regards notice and knowledge].)

For these reasons, I would reverse the summary adjudication on the claim under Commercial Code section 11204. I also disagree with the conclusion that Commercial Code section 11505 bars any of the causes of action.

B. Displacement[2]

As to the issue of displacement, I am not prepared to conclude that certain common law causes of action are always displaced by Article 11 of the Commercial Code—Article 4A of the UCC. The issue of displacement is difficult. (See *Sheerbonnet, Ltd. v. American Express Bank* (S.D.N.Y. 1995) 951 F.Supp. 403, 407-408; *Regions Bank v. Provident Bank, Inc.* (11th Cir. 2003) 345 F.3d 1267, 1275 ["the only restraint on a plaintiff is that 'resort to principles of law or equity outside of Article 4A is not appropriate to create rights, duties and liabilities *inconsistent* with those stated in this article.' U.C.C. § 4A-102 cmt. (emphasis added)"]; *Dubai Islamic Bank v. Citibank, N.A.* (S.D.N.Y. 2000) 126 F.Supp.2d 659, 666 ["the law concerning Article 4A 'exclusivity' appears to be evolving"]; Cal. U. Com. Code, § 1103, UCC Comment ["this section indicates the continued applicability to commercial contracts of all supplemental bodies of law except insofar as they are explicitly displaced by this Act . . ."].)

White and Summers note the issue and state, "We are uncertain about the proper outcome. On the one hand, we appreciate the argument for liability; on the other, we recognize that a comprehensive statute that allocates liability quite precisely should not be lightly disrupted." (White and Summers, *supra,* § 24-9 at p. 89.) In a thoughtful article, one writer argued "that Article 4A should not displace negligence as a cause of action, because a negligence claim will prevent inequity and promote efficiency without unduly frustrating code policies." (Note, *Allocation of Loss Due to Fraudulent Wholesale Wire Transfers: "Is There A Negligence Action Against a Beneficiary Bank After Article 4A of the Uniform Commercial Code"* (1992) 90 Mich. L.Rev. 2565, 2566.)

A negligence or breach of contract theory in a case such as this one is not necessarily inconsistent with the UCC provisions, other than as to the period of repose.

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[2] The term "preemption" does not apply to conflicts between state laws. (See *Stop Youth Addiction, Inc. v. Lucky Stores, Inc.* (1998) 17 Cal.4th 553, 568.)

In other cases, a negligence or breach of contract theory might provide rights that are foreclosed by the UCC and thus would be inconsistent with its substantive provisions. But, perhaps the period of repose is part of the compromise framework of the UCC so that using common law claims to avoid that period could be viewed as inconsistent with the UCC.

One authority has stated, "[t]he sections are to be interpreted in light of the carefully balanced compromises demonstrated within structure and rules of Article 4A. Unlike the other Articles of the UCC, Article 4A should not be supplemented or expanded by resort to principles of law or rules of equity outside of Article 4A to create rights, duties, or liabilities inconsistent with those stated in the Article itself." (6A Hawkland & Moreno, UCC Series (1999) § 4A-101:1, p. Art. 4A-4, fn. omitted.) Another authority has written, "[w]e said at the outset that Article 4A was not drafted in an hermetically sealed environment. Instead, the draftspersons sought to control carefully the contacts which Article 4A would have with other bodies of law. Many of Article 4A's provisions represent a delicate balancing of the rights and duties of parties to a funds transfer. The unintended importation of a common law doctrine would upset that balance, just like foreign bacteria can adversely affect a healthy organism. The years of work by the Drafting Committee should not be undone in this manner. [¶] We are confident that Courts will continue to interpret carefully drafted U.C.C. remedies to be 'exclusive,' and thereby prevent the frustration of Article 4A's objectives." (Baxter and Bhala, *The Interrelationship of Article 4A with Other Law* (1990) 45 Bus. Law. 1485, 1507, fns. omitted; see Note, *Article 4A of the Uniform Commercial Code: "Dangers of Departing From a Rule of Exclusivity*" (1999) 85 Va. L.Rev. 183, 211-212; *Eduardo Gil v. Bank of America* (2006) 136 Cal.App.4th 848, 856-859 [displacement of negligence claim by Cal. U. Com. Code, § 4406, subd. (f) dealing with duties of customer in asserting forgery against payor bank]; but see 1 Lawrence's Anderson on the Uniform Commercial Code, *supra,* 1-103:3, p. 201 [areas not "covered" by the UCC are governed by common law]; *Grain Traders, Inc. v. Citibank, N.A.* (2d Cir. 1998) 160 F.3d 97, 103 ["we do not reach the issue of whether common law claims that concern matters

expressly addressed by Article 4-A would be precluded as duplicative even if consistent"].)

Generally, an unauthorized or erroneous transfer would be negligent or a breach of the agreement. To allow those causes of action would amount to strict liability. On the other hand, to foreclose all common law rights might result in the preclusion of claims against banks for gross negligence or intentional conduct. Although there may be displacement here, that does not mean there may not be situations in which the common law supplements Article 11 of the Commercial Code—Article 4A of the UCC.

I concur that the non Commercial Code claims can be summarily adjudicated against Zengen. I would reverse the judgment as to the third cause of action for a violation of the Commercial Code. The two issues addressed here have not been covered by California authorities. The nature of an objection under UCC Article 4A-505 has received scant, if any, attention, and the issue of displacement under the Funds Transfer provision of the UCC is a much debated issue. Further consideration of these questions would be desirable.

MOSK, J.