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Chapter 7: Commercial Law

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CHAPTER 7

Commercial Law

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§7.1. Consumer credit: Disclosure of interest rate. Interest rates in Massachusetts, with very few exceptions, have no statutory limitations. The exceptions include all loans of under $1000, which have long had a maximum interest rate of 18 percent per year; loans as high as $1500, which are regulated if made by persons in the business of making such loans; and loans by licensed pawnbrokers, which are regulated despite the amount of the loan. In 1959, regulation of still another — and rather curious — type of loan was added to the list of those subject to regulation. This, in general, is a loan of over $1500 secured by a mortgage (other than a first mortgage) of real estate having an assessed value of not over $25,000, if the real estate is used as a home by the borrower. Whatever might have been the evil that prompted this curious conglomeration of requirements, the protection was twofold: limitation of interest to 1½ percent per month and compulsory disclosure of the rate of interest actually charged. The civil penalty for overcharge of interest is simply to reduce the interest to 18 percent per year, but for failure to disclose the rate of interest, the penalty is forfeiture of the right to collect interest.

In Remy v. Sher, the Supreme Judicial Court has practically eliminated the disclosure requirement. The note involved in the case showed that the principal sum was $4500, the rate of interest "or its equivalent in money" was $2356.80, the period of the loan was sixty months, and the monthly payments were $114.28. By the use of complicated formulas or prepared tables it could be established that the rate of interest was actually 1½ percent per month, as permitted by the statute. The borrower maintained, however, that the purpose of the disclosure requirement was to make it unnecessary for him to make computations to determine the rate of interest, and that the disclosure requirement therefore is not met by a statement of the total interest for the entire life of the loan. The statutory limitation of the "rate of interest" is "... an amount equivalent to one and one-half per cent

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§7.1. 1 G.L., c. 140, §90.
2 Id. §96.
3 Id. §72.
5 346 Mass. 471, 194 N.E.2d 106 (1963), also noted in §2.5 supra.
a month computed on unpaid balances."6 Certainly the only rate commonly understood is a rate per month or per year, and it is only when the rate is expressed according to such a standardized period that the borrower has any real basis for comparison. In view of this, the total interest for the life of the loan is somewhat meaningless. Nevertheless, the statute requires disclosure of the rate of interest or its equivalent in money, and the Court held that the total interest for the life of the loan is the equivalent in money of the rate. If there was a purpose to be served by disclosure of the rate of interest, that purpose has been largely denied by this decision.

The Court reached its decision partially because of a statutory right given to the borrower to request a receipt after any payment, showing the application of that payment to principal and interest. "Such a provision," said the Court, "would be wholly unnecessary if . . . such information must be included in the note in the first place."7 Despite this broad statement, it must be recognized that practically all banks that make mortgage loans routinely do provide such receipts, whether or not demanded, even though the rate of interest per month or per year is stated. Far from being "wholly unnecessary," this procedure is often of great interest and value to the borrower.

The ambiguity which made possible the Court's emasculation of the statute was a result of its very inept wording, which defines the "rate of interest" as an "amount equivalent to" a stated percentage of unpaid balances. It would seem almost as if the General Court had been trying to prevent monotony in ignoring all previous examples, found in other portions of the General Laws, which express the rate of interest in the following ways: "six dollars on each hundred for a year";8 eighteen per cent per annum";9 "six dollars upon each one hundred dollars for a year";10 and "eight dollars per one hundred dollars per year."11 With all of these examples expressing the rate of interest as either a percentage per year or a number of dollars for each one hundred dollars per year, it seems peculiar that the newer statute should define the term not as a percentage of the unpaid balance, but rather as an amount equivalent to such percentage of the balance. The words seem to have been taken out of context from General Laws, Chapter 140, Section 100, which limits the total amounts collected for interest and expenses by a licensee under the Small Loans Act, over the life of the loan, to "an amount equivalent to the maximum monthly rate computed on unpaid principal balances."

§7.2. Commercial paper: Holder in due course. In order to enforce a negotiable instrument against an obligor who was induced to

6 Emphasis supplied.
8 G.L., c. 107, §3.
9 Id., c. 140, §80.
10 Id., §111.
11 Id., c. 255, §14. This section concerns finance charges in the retail installment sale of motor vehicles. Though this is not "interest," there is a similarity.
sign the instrument by fraud, the holder of the instrument must be a holder in due course. This requires him to have taken the instrument for value, in good faith, and without notice of certain facts. Two cases during this 1964 Survey year involved these requirements, one focusing on “value” and the other on “notice.”

The defendant in *Universal C.I.T. Credit Corp. v. Ingle* had signed a promissory note for the installation of aluminum siding on his house but claimed that there was either fraud or a breach of warranty in the transaction. The note had been purchased by the plaintiff corporation after it had obtained a credit report disclosing that there had been numerous complaints to the Boston Better Business Bureau about the advertising methods of the payee of the note, the firm that sold and installed the siding. The Supreme Judicial Court held that this report had been properly excluded from evidence in the jury trial before the Superior Court, since it could not rebut the prima facie evidence that the plaintiff had taken the note without notice of a defense. (This prima facie evidence consisted of a finding for the plaintiff in a prior trial in a district court.) “[T]he standard of notice contemplated . . .,” said the Court, “is actual notice and not merely reasonable grounds for belief . . . [T]here was nothing in this evidence by which knowledge of any fraud could be imputed to the plaintiff.”

The legislature in 1961 enacted a statute requiring notes given for the purchase of consumer goods to be non-negotiable so that defenses of this type would be available to the consumer regardless of the good faith or lack of notice of the finance company that later purchased the note. Although this statute was not involved because the transaction had occurred before its enactment, it would not have affected notes given in connection with this type of home-improvement contract. “Consumer goods” are defined by the statute as “tangible personal property used or bought for use primarily for personal, family or household purposes.” A contract for the installation of siding, while it involves the passage of title to the siding, ought to be regarded as a contract for “work and labor” rather than for the “sale of tangible personal property.” Therefore, it would not seem to fall within the protection of this statute.

The definition of the value for which a holder must take a negotiable instrument in order to become a holder in due course was changed substantially by the Uniform Commercial Code. “Value” is no longer synonymous with “consideration.” A holder takes for value to the extent that the agreed consideration has been performed. He may, in this way, be a holder in due course for part of the promise on an

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1. G.L., c. 106, §3-302.
3. Id. at 372, 196 N.E.2d at 852.
5. G.L., c. 106, §§3-308(a). Value also consists of several other things not involved in the case under discussion.
instrument while subject to defenses as far as the balance of the obligation is concerned.

The theory behind this change would seem to be that if the holder learns of a defense, or if the instrument is dishonored before the agreed consideration has been performed fully, he does not need the protection afforded a holder in due course since he may simply refuse to perform further himself, and he will have an excuse for non-performance. A striking example of the application of this change is given in the case of *Korzenik v. Supreme Radio, Inc.* The defendant was the obligor on a time instrument that had been obtained by fraud of the payee. The payee negotiated the instrument to the plaintiff, an attorney, as a retainer for legal services. The instrument matured one week after the plaintiff's services had been retained and before any actual services had been performed. The Supreme Judicial Court held that the plaintiff's recovery on the instrument depended upon the purpose of the retainer. If it was for the services that were to be performed, there could be no recovery since no services had been performed prior to the maturity of the instrument. If the retainer was payment for the availability to perform services rather than for the performance itself, there could be recovery to the extent of the value of that availability to the time of maturity of the instrument. Since the burden of proving value is on the holder, and since the plaintiff did not offer any evidence of the value of his availability to perform services for one week, recovery was denied in toto.

§7.3. Commercial paper: Sum certain. For an instrument to be negotiable, it must contain a promise or order to pay a sum certain. While many courts in the past have confused ambiguity with uncertainty, the Supreme Judicial Court has indicated that when ambiguities have been resolved, uncertainty disappears. The note in question in *Universal C.I.T. Credit Corp. v. Ingel* contained the expression "with interest after maturity at the highest lawful rate." The General Laws, however, expressly refuse to set a "lawful rate" of interest except for specified cases which did not apply to the note before the Court. At the same time, the General Laws provide that the rate of interest will be 6 percent unless some other rate is agreed upon in writing. As an agreement for "the highest lawful rate" cannot be an effective agreement for any specific rate under these circumstances, the statutory provision for interest at the rate of 6 percent must apply; and, since the ambiguity has been resolved by resort to this statute, the promise can be said to be for a sum certain.

The Attorney General and the Massachusetts Commissioners on Uniform State Laws submitted a brief amici curiae containing an

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7 G.L., c. 106, §§-104(1)(b).
10 G.L., c. 107, §§.
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unusually complete analysis of this aspect of the case, in order to try to obtain a decision consistent with a principle of the Uniform Commercial Code that ambiguities should be resolved. The mere presence of ambiguities ought not simply to vitiate obligations.

§7.4. Commercial paper: Proof of signatures. In order to prove that he is a holder in due course, one must prove not only that he took the instrument for value, in good faith, and without notice, but also that he is a "holder." To be a "holder," one must be in possession of the instrument, and the instrument must contain all endorsements that were necessary to its negotiation.¹ Since an unauthorized signature is inoperative as the endorsement of the person whose name is signed, it may be necessary for the person claiming to be a holder to establish² that all signatures necessary to his chain of title are authorized.

The steps in this process are set out rather clearly in the Uniform Commercial Code.³ Signatures not specifically denied in the pleadings are admitted. If the effectiveness of a signature is contested, the burden of establishing it is on the party claiming under it, but he is aided by a presumption that it is authorized, and he need introduce no evidence to meet his burden unless and until opposing evidence that would support a finding of lack of authority is introduced.⁴

The operation of these rules is well illustrated by Watertown Federal Savings & Loan Ass'n v. Spanks.⁵ A note payable to the order of "Greenlaw & Sons Roofing & Siding Co." bore the endorsement "Greenlaw & Sons by George M. Greenlaw." Despite this discrepancy and the fact that the effectiveness of this signature was put in issue, the Supreme Judicial Court held that it was not necessary for the holder of the note to introduce any evidence of genuineness or authority for the endorsement, since the maker of the note had not introduced any evidence to show that Greenlaw & Sons and Greenlaw & Sons Roofing & Siding Co. were not the same company. The presumption of authority therefore required a finding for the holder.

The identity of the person rather than the name used determines the effectiveness of the endorsement. If an instrument is payable to a person under a name other than his own, an endorsement in either that name or his own is effective as an endorsement.⁶ While the Uniform Commercial Code gives a person paying an instrument the right to require signatures in both names, so that he would not be in default for failure to pay if such a demand were refused, the implication of the Spanks decision is that the right does not

¹ C.L., c. 106, §1-201(20).
² Id. §§404. The term "establish" is used rather than "prove."
³ Id. §§3-307.
⁴ Id. §1-201(31).
⁶ G.L., c. 106, §§3-203.
extend to signatures of prior transferors. Thus, although the maker may be able to demand that the last holder sign both in his own name and in the name appearing on the instrument, he must accept prior endorsements as they appear if in fact they have been made by the proper persons. Furthermore, he must introduce evidence that the actual signer and the proper person are not the same before the presumption that they are needs to be supported.

§7.5. Commercial paper: Accommodation parties. The Uniform Commercial Code provides indirectly that an accommodation party will have the benefit of any defense that may exist under the law of suretyship whenever the owner of the instrument is not a holder in due course; and, in addition, he will even have the benefit of suretyship defenses vis-à-vis a holder in due course if the holder in due course has notice of the accommodation.¹ Such a defense might be that the instrument was diverted to a purpose different from that for which the accommodation party agreed to lend his name. It may also be the release of a party against whom the accommodation party has a right of recourse, or the impairment of collateral given by a party against whom the accommodation party has a right of recourse, even though the right of recourse is not disclosed on the face of the instrument. Thus, if one of two co-makers signs an instrument for the accommodation of the other, he will have a right of recourse because of the contract of accommodation, although this is not apparent on the face of the instrument.² The consequence of this is that he will be released despite his signature as a co-maker if collateral given by the other maker is impaired by the holder of the instrument.

In Rose v. Homsey,³ the defendant had signed a note as co-maker with her husband, for his accommodation, and this accommodation was known by the payee. The husband executed a mortgage on real property as security for the note, but the payee, at the husband's request and without the knowledge of the defendant, did not record the mortgage. The husband subsequently became bankrupt, and the mortgaged property went to the trustee in bankruptcy despite the mortgage because of the lack of recording necessary to perfect the security interest. Although the Supreme Judicial Court recognized that the failure of the creditor to record the mortgage was an impairment of collateral that would release a surety under the law of suretyship, it was unable to allow this defense to the defendant wife. The note had been executed before October 1, 1958, the effective date of the Uniform Commercial Code, and under the prior Negotiable Instruments Law, as interpreted by various Massachusetts cases, the obligation of a maker was absolute whether or not he had signed for accommodation. The rules of the Code seem clearly to be superior to those of the prior law. The discharge of

¹ G.L., c. 106, §§4-415(3).
² Id. §§-606(1)(a), (b).
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parties is now governed by underlying relationships rather than by the label of "primary party" or "secondary party."

§7.6. Sales: Consignment as sale or return. Since 1845, entrusting of goods to an agent or factor with even a limited authority to sell has given the agent the power to convey a good title to a bona fide purchaser in any sale even though the limitations on the agent's power may be exceeded. Since 1849 such an agent has had the additional power to pledge his principal's goods for new advances (although not as security for an antecedent debt) even if this violates the agent's agreement with his principal. The Uniform Commercial Code cuts further into the right of a principal to retain control over goods which he entrusts for sale to an agent by providing that if the agent maintains a place of business at which he deals in goods of the kind involved in a name other than that of his principal, then the agent's creditors may have recourse to the goods as if they had been purchased by the agent under a contract of sale or return. The principal's interest in the goods may be protected against these creditors if he complies with any applicable law providing for the posting of a sign (although there is no such law in this Commonwealth); or if the agent is generally known by his creditors to be substantially engaged in selling the goods of others; or if the principal files a financing statement, in accordance with the article on secured transactions.

The Supreme Judicial Court held, in General Electric Co. v. Pettengell Supply Co., that this section of the Commercial Code means what it says. General Electric had delivered substantial quantities of industrial lamps on consignment, as an agent to sell or distribute, to a dealer in various types of electrical merchandise. When the dealer later made an assignment for the benefit of creditors, the assignee's interest in these lamps had priority over the interest of General Electric. While General Electric raised numerous objections to this application of the Commercial Code by attempting to construe various words of the statute in an overly technical manner, the Court disposed of all of the objections by applying the statute as it apparently was intended to be applied. Consignors who want to be protected against creditors of their merchant-agents in the future will simply have to take the trouble of filing financing statements.

§7.7. Sales: Warranties. Carlo Bianchi & Co. v. Builders' Equipment & Supplies Co. involved the acquisition by a contractor of a concrete batching plant from an equipment supplier under a "rental contract" running for thirty months, with an option to pur-

§7.6. 1 G.L., c. 104, §1.
2 Id. §§4, 5.
3 Id., c. 106, §§2-326(3).
4 Under Section 9-102(2), a consignment intended as a security is governed by Article 9 of the Code.
chase at any time for the remaining rental payments. While this transaction was in form a lease, its effect was that of a conditional sale, and the Supreme Judicial Court properly treated it as such. In preliminary negotiations between the parties, the seller (or lessor) represented orally to the buyer that the plant would batch one and three-eighths cubic yards of concrete in forty-five seconds. The written rental contract, however, contained no statements about performance of the equipment. Although the parol evidence rule forbids introduction into evidence of prior representations if a contract is reduced to writing, the Court held that the rental contract, which was concerned solely with the method of payment, did not purport to be the complete contract. Accordingly, the buyer was permitted to show by evidence of the oral statements that there was an express warranty of this performance.

Since the transaction involved had occurred before the enactment of the Uniform Commercial Code, the Code rules were not applied. Had the Code been in effect, the result would have been precisely the same since the Code expressly permits evidence of additional terms to a written contract if the contract was not intended to be a complete and exclusive statement of the terms of the agreement.²

In addition to this express warranty, the Court found that the buyer had made known the purpose for which he wanted the equipment and relied upon the seller's skill and judgment in furnishing equipment that would perform continuously for eight-hour periods. Although the equipment had a trade name, and although the Uniform Sales Act stated that there could be no warranty of fitness for a particular purpose in the sale of an article under its trade name,³ the Court nevertheless held that this section did not apply if the buyer relied upon the seller's recommendation rather than on the trade name. The Commercial Code would not only agree with this conclusion, but it would also make it a little easier to reach. The principal element of an implied warranty of fitness for a particular purpose is reliance upon the seller's skill and judgment. The Code makes no mention of trade names, so that the mere existence of a trade name could never result in the denial of this warranty. A determination must be made in every case whether the buyer relied upon the trade name or upon the seller.

Having found the existence of these warranties, and having determined that they were breached, the Court awarded as damages the additional expenses that the buyer had incurred in performing the contracts for which the equipment had been acquired. Although the usual measure of damages for defective goods which have been accepted is the difference in value between the goods as they were and conforming goods,⁴ the Commercial Code expressly provides for consequential damages including "any loss resulting from general

³ Former G.L., c. 106, §17(4).
⁴ G.L., c. 106, §2-714.
or particular requirements and needs of which the seller at the time of contracting had reason to know and which could not reasonably be prevented by cover or otherwise.”11 Thus, this result also would have been reached if the Code had governed the case.

§7.8. Sales: Revocation of acceptance. In Carlo Bianchi & Co. v. Builders’ Equipment & Supplies Co.1 the contractor who had purchased equipment for the performance of two specific jobs used the equipment for those jobs even though the equipment failed to comply with express and implied warranties of performance. During this time he made no payments, and he complained to the seller a number of times. Both the buyer and seller made substantial efforts to get the equipment to perform as warranted, but their efforts were fruitless. After completing the jobs for which he had purchased the equipment, the buyer notified the seller that he would not accept the equipment. The Supreme Judicial Court held that while continued use ordinarily constitutes acceptance, the use in these circumstances signified only that the buyer would accept if the improvements were effective. Nevertheless, since the buyer had recovered his actual additional expenses in his action for breach of warranty, and since the breach by the seller was not intentional, the Court held that the seller was entitled to the reasonable value of the use of the equipment by way of restitution.

If the Uniform Commercial Code had controlled the case, some new concepts would have been introduced. Under the Code rule, a buyer may reject goods if they fail to conform to the contract in any respect.2 Once having accepted the goods, he may still revoke his acceptance if nonconformity is substantial, and if his acceptance was on the reasonable assumption that the nonconformity would be cured.3 Whether it is determined that the buyer never accepted the goods or that, having accepted, he revoked his acceptance after the attempts of the seller to cure the defects proved unavailing, the buyer in either case is entitled to consequential damages. But what of the seller’s right to the reasonable value of the use of the equipment? The remedies provided for a seller depend on a wrongful rejection or revocation of acceptance,4 and it would seem that this, read together with the buyer’s statutory right to recover whatever part of the price had been paid in any case of rightful rejection or justifiable revocation of acceptance,5 would bar any recovery by the seller. Nevertheless, the reasonable value of the use of the equipment ought to affect the determination of the amount of the buyer’s consequential damages. Therefore, it would seem logical that the recovery which was allowed the seller in this case would,

5 Id. §2-715(2)(a).

2 G.L., c. 106, §2-601.
3 Id. §2-608.
4 Id. §2-709.
5 Id. §2-711(1).
if the Code had been applicable, simply have reduced the damage
which the buyer was found to have suffered, and for which he got
a judgment.

§7.9. Secured transactions: Subrogation. The priority of a per­
fected security interest over an interest in the same property perfected
at a later date may be transferred to a new creditor by assignment
of the interest.\(^1\) In \textit{French Lumber Co. v. Commercial Realty &
Finance Co.},\(^2\) the Supreme Judicial Court found a means of allowing
a new lender to succeed to the rights of a prior secured party without
any assignment. The debtor had financed the purchase of an auto­
mobile through a security interest that was perfected by filing. The
debtor then borrowed money from a second creditor who perfected
a security interest in the same property by filing. After the debtor
defaulted on the first agreement, the first creditor threatened to
foreclose, and a third creditor advanced new funds to the debtor
so that he could pay off the first creditor. This third creditor also
perfected a security interest by filing. Although this third creditor’s
rights under its own security interest were subordinate to those of
the second creditor, the Court held that the third creditor succeeded
to the rights of the first by the doctrine of subrogation.

Since this third creditor could have succeeded to the rights of the
security interest of the first by getting an assignment of the interest
when its funds were used to discharge the first debt, the Court
found that the intervening creditor could not be prejudicially affected
by allowing this subrogation. The Court further stated: “No pro­
vision of the Code purports to affect the fundamental equitable
document of subrogation.”\(^8\) Under the circumstances the Code spe­
cifically provides that the principles of law and equity shall supple­
ment its provisions.\(^4\)

The Chicopee Falls Co-operative Bank, a “tiny, pitifully inadequate
bank . . . in danger of closing its doors,”\(^1\) had an opportunity to merge
with a federal savings and loan association in another county. Such
a merger required first the conversion of the bank to a federal
savings and loan association; and such a conversion, though permitted
by statute, first required the approval of the Board of Bank
Incorporation and its finding that the conversion would, promote the
public convenience and advantage. Although the Board of Bank
Incorporation found that the proposed merger would promote the
public convenience and advantage and therefore authorized the
conversion in order to make possible the merger, the decision of

\(^1\) G.L., c. 106, §9-302(2).
\(^2\) 346 Mass. 716, 195 N.E.2d 507 (1963), also noted in §2.2 supra.
\(^3\) Id. at 719, 195 N.E.2d at 510.
\(^4\) G.L., c. 106, §1-103.

\(^1\) Chicopee Co-operative Bank v. Board of Bank Incorporation, 1964
the Board was set aside by the Supreme Judicial Court at the instance of other co-operative banks.

The Court held that the Board's order, though in form an approval of a conversion and within its statutory power, was, in fact, an approval of a merger. There is no statutory authority for mergers of co-operative banks with federal savings and loan associations, although there is express statutory authority for a number of other types of bank mergers. Furthermore, extensive legislative history indicated increasing resistance to true conversions, which led to the conclusion that approval of mergers under the guise of conversion could not be within any implied power of the Board.

The legislative hostility to this type of merger seems to be based on a policy against branch banking across county lines—a policy which cannot be enforced against federal savings and loan associations. It is interesting to note that, by the Acts of 1964,² the privilege of conversion of a co-operative bank into a federal savings and loan association has been suspended completely for two years, except for those banks that may have filed application for conversion before January 1, 1964.

² Acts of 1964, c. 386.