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Secured Transactions

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CURRENT LEGISLATION

Means in opposition to the expense account provisions dealt with their adverse effects upon the restaurant and theater business.²¹ But it can be effectively argued that these concerns are not entitled to the fruits of present expense account abuses. It was also urged at the Hearings that the existing laws are adequate and that the Internal Revenue Service should widen its audit coverage to detect possible violations.²² These views were not held by the Secretary of the Treasury, C. Douglas Dillon.

CHARLES B. ABBOTT

SECURED TRANSACTIONS

In the area of secured transactions, legislation has been quite limited since its last treatment¹ in the *Boston College Industrial and Commercial Law Review*. Perhaps increased attention given by various states to the Uniform Commercial Code² is the reason. This article will not include any legislation dealing directly with the UCC.

Louisiana has enacted the Direct Vehicle Loan Company Act,³ the purpose of which is to regulate the lending of money secured by liens on motor vehicles. Loans may not be made until sixty days or more after the borrower is vested with title to the motor vehicle. The legislature later by resolution⁴ suspended certain portions of the act affecting loans made primarily for industrial and commercial purposes or loans made by licensed sales finance companies or companies licensed under the Small Loan Law of Louisiana. The Direct Vehicle Loan Company Act was approved in conjunction with Louisiana's Motor Vehicle Sales Finance Act⁵ which regulates the financing of motor vehicles by retail instalment agreements, the latter act also being amended.⁶

Several states have dealt with the question of whether the buyer should be entitled to a refund or credit on the finance and service charges when he pays in full before maturity the amount of the credit extended for the purchase. The Arizona legislature has amended its law⁷ by now allowing any borrower to prepay a loan at any time during the loan period. The Rule of 78⁸ is the prescribed method of computing the refund. Banks or trust com-

²¹ See particularly the statements of Vincent Sardi, Jr., Hearings on the President's 1961 Tax Recommendations before the House Committee on Ways and Means, 87th Cong., 1st Sess. 1616-24 (1961).

²² Hearings, *supra* note 21, at 1634; Frank V. Olds, Federal Tax Committee of the Controllers Institute of America.

¹ Legislation, 3 B.C. Ind. & Com. L. Rev. 248 (1962).

² Legislation and annotations dealing with the Uniform Commercial Code will be found elsewhere in this Review.

³ Acts 1962, Act No. 138, approved July 6, 1962, effective January 1, 1963.

⁴ House Current Resolution No. 126, adopted July 12, 1962.

⁵ La. Rev. Stat. § 6:951 (1950).

⁶ Acts 1962, Act No. 139, approved July 6, 1962, effective January 1, 1963.

⁷ Ariz. Rev. Stat. Ann. § 6-254 as amended by Laws 1962, ch. 210, approved March 13, 1962, effective June 21, 1962.

⁸ This method, sometimes referred to as the "sum of the digits" method, is based on the notion that the greater part of the finance charge is earned in the early period of the

panies in Kentucky have been authorized⁹ to receive advanced interest on secured and unsecured instalment loans for the entire period of the loan. Repayment of the loan entitles the borrower to a rebate of the advanced interest paid. Massachusetts¹⁰ now permits a debtor to receive credit of the finance charge for services rendered or to be rendered upon payment of a debt for retail consumer goods¹¹ before maturity.

Alaska¹² and Kentucky¹³ have each passed a retail instalment sales act directed at consumer goods, excluding commercial, industrial and agricultural goods. Alaska includes motor vehicles, while Kentucky regulates retail instalment sales of motor vehicles by a separate statute. New York has made revisions and additions to its Retail Instalment Sales Act.¹⁴

An interesting statute regulating add-ons¹⁵ was added to the Michigan laws entitled "Subsequent Conditional Sales of Consumer Goods."¹⁶ The statute makes provision for the consolidation of conditional sales contracts of previous and present purchases of consumer goods. If consolidation is carried out, the seller must prepare and present a memorandum of the transaction to the buyer. The memorandum must include a description of the additional purchases, the consolidated total indebtedness of the buyer, the finance charges and the revised instalment payments.¹⁷

In case of default by the buyer, the seller must take certain steps previous to repossession of the goods. The seller must first retroactively allocate all payments made under the consolidated contracts to the various purchases

debt. As loans are usually based on a yearly period, the months of the year are designated by the digits one through twelve, the sum of which gives seventy-eight. This figure is used as the denominator of the fraction to determine the rebate. The sum of the digits of the number of months anticipated is the numerator, the first month designated as twelve because most of the charge is earned in the early months of the debt period. For a more complete discussion, see Hogan, *A Survey of State Retail Instalment Sales Legislation*, 44 *Cornell L.Q.* 38, 57-58 (1958).

⁹ Ky. Rev. Stat. § 287.215, as amended by Laws 1962, S.B. No. 100, approved March 9, 1962, effective June 15, 1962.

¹⁰ Laws 1962, ch. 309, approved April 12, 1962, effective July 1, 1962.

¹¹ Mass. Gen. Laws Ann., ch. 255, § 12B allows the buyer to receive credit for anticipation of payments on any credit sale of consumer goods.

¹² Laws 1962, S.B. No. 233, approved April 18, 1962, effective January 1, 1963.

¹³ Laws 1962, S.B. No. 97, approved March 20, 1962, effective January 1, 1963.

¹⁴ The more significant features are as follows: (1) a provision entitling a buyer to receive full credit and a service charge credit for returning any unused merchandise certificates. Laws 1962, ch. 299, approved April 4, 1962, effective October 1, 1962; (2) a provision that no seller is to induce a buyer to become obligated under more than one retail instalment obligation for the purpose of obtaining a higher credit service charge. Laws 1962, ch. 328, approved April 4, 1962, effective October 1, 1962; (3) a provision that the credit service charge must be computed on the principal balance payable in successive monthly instalments equal in amount for a one-year period. Where the obligation is for a period less than or greater than a year, the credit service charge is to be proportional. Laws 1962, ch. 328, approved April 4, 1962, effective October 1, 1962.

¹⁵ The add-on occurs when a buyer enters into a second contract with the same seller for the purchase of other goods before the first purchase is paid for, and the two transactions are consolidated into one contract. The first purchase is usually held as security for the subsequent purchases.

¹⁶ Acts 1962, P.A. No. 167, approved May 14, 1962, effective 90 days after adjournment of Legislature.

¹⁷ Acts 1962, P.A. No. 167, § 1.

CURRENT LEGISLATION

in the same ratio as the original cash prices bear to each other. Down payments must be allocated to their respective purchases. The seller must notify the buyer of the allocations and the buyer has the right to complete payment on any of the purchases within fifteen days. Those purchases which are then paid in full are exempt from repossession.¹⁸ These provisions do not apply to accessions.¹⁹

The Michigan act makes an initial step in regulating the subsequent purchases of consumer goods under conditional sales contracts. The act, however, makes no provision for other types of secured transactions. Michigan, several days later, adopted the Uniform Commercial Code,²⁰ which consolidates conditional sales agreements, chattel mortgages and other security devices under the one heading of "security agreements."²¹ In legislation similar to that of Michigan, New York²² and Illinois²³ have amended their statutes so they will be consistent with the terminology of the UCC. As the situation now exists, the Michigan act possibly can be circumvented by the seller by avoiding the use of a conditional sales contract.

A common provision in instalment sales statutes of other states is the limitation of purchases to consumer goods. Most regulatory legislation, in the form of retail instalment sales acts, already covers the motor vehicle purchase. As opposed to the inconsistent terminology used in describing the form of transaction covered by the act and the terminology of the UCC, the definition of consumer goods as found in the Michigan act²⁴ is consistent with the UCC. By confining the type of purchase to consumer goods, no protection is given to the small business buyer. This is not unusual in this type of regulatory legislation.²⁵ Many such statutes base the exclusions of commercial groups upon the basis that commercial buyers do not need protection.²⁶ An authority in this field writes:

It is easy to become concerned about the unwary and the eager consumer who deals with the professional seller and indirectly with the skilled financing agency. The intensity of concern diminishes when the adversaries are two professionals: the commercial buyer and seller or financing firm.²⁷

The drafters of the Model Retail Instalment Sales Act point out in their comment to Section 1:

¹⁸ Acts 1962, P.A. No. 167, § 2.

¹⁹ *Ibid.*

²⁰ Acts 1962, P.A. No. 174, approved May 17, 1962, effective January 1, 1964.

²¹ Uniform Commercial Code § 9-102(2) (1958).

²² N.Y. Pers. Prop. Law §§ 410(2), 410(3).

²³ Ill. Ann. Stat. ch. 121½, § 250 (Smith-Hurd 1960).

²⁴ *Supra* note 17, at § 4.

²⁵ A Model Retail Instalment Sales Act was proposed in the Boston College Industrial and Commercial Law Review, which includes within the term "goods," chattels purchased for commercial use by a small business buyer. A small business buyer is defined as an instalment buyer whose net income from his business has averaged \$5000 or less per year over the previous three-year period. 3 B.C. Ind. & Com. L. Rev. 437 (1962).

²⁶ See generally Hogan, *supra* note 8.

²⁷ *Supra* note 8, at 72.

The "small business buyer" who purchases on time for commercial purposes should be given the same protection as the luxury cabin cruiser devotee. The student earning his tuition by driving his own taxi, the small independent contractor, the corner grocer, are, to name a few, usually unprovided for in retail instalment sales acts.²⁸

The Model Act uses a "net profits" test combined with the idea of giving certain groups protection rather than using the group or dollar-limit method alone in determining the individuals covered by the act.

Most instalment credit legislation does not prohibit the add-on, but rather regulates its use. Normally, provisions regulating add-ons require allocation of payments to each purchase, and when a purchase is fully paid, it is no longer held as security by the seller. The Michigan act requires only that before repossession must a seller make allocations of instalment payments of the consolidated contracts. In an analogous situation, New York provides much stronger and clearer requirements. First, New York allows add-ons only when the total unpaid balance of previous contracts does not exceed \$3000. Goods purchased under previous contracts can be used for security only until the purchase price under the previous contract is fully paid or until twenty per cent of the time sale price of the goods under the subsequent contract has been paid.²⁹ Secondly, a provision³⁰ requires that all payments made up to the time of the subsequent purchases be applied to the original purchases. Where the amount of each instalment is not increased, all payments made after that time are immediately allocated to all of the various purchases in the same proportion as the original cash sale price of each purchase bears to each other.

The Alaskan Retail Instalment Sales Act goes one step further.³¹ If the amount of each instalment payment is not increased in connection with the consolidated contracts, the subsequent payments made under the consolidation must first be allocated to the previous purchase. Not until the previous purchases are fully paid will any payment go to the subsequent purchase. If, however, the amount of each instalment is increased in connection with the subsequent purchase, the seller may allocate an amount equal to the original rate to the previous purchase, and an amount equal to the increase to the subsequent purchases.

In comparing the provisions of the Michigan statute with those of New York and Alaska, it becomes apparent that the Michigan statute may be construed to provide less protection to the buyer.³² By construction of the

²⁸ Supra note 25, at 440.

²⁹ Supra note 22, at § 410(2).

³⁰ Supra note 22, at § 410(3).

³¹ Supra note 12.

³² At the time the buyer defaults on payments under the consolidated contract, the terms of the statute indicate that all payments made by the buyer under the contract, both previous to and after consolidation with subsequent purchases, are allocated among all the various purchases under the contract, with the exception of the down payments made on the individual purchases. The language of the statute, which is not ideally drafted, may imply that all payments made on the previous contract are thrown into a pool to be allocated with payments made on the consolidated purchases. The net effect, if such construction is given to the provision, would be that no purchase can be fully paid

statutory language it is possible to get a result similar to that of New York whereby the buyer does not lose out on any payments made on his previous purchases.

The Michigan act provides a criminal sanction³³ for the "wilful" violation of the provisions of the act by the seller. This sanction gives little or no protection to the buyer who is the primary subject of the regulation. To prove that an action by the seller is wilful is not an easy task, and even if the seller is found guilty, the buyer is still left without a civil remedy.³⁴

The Michigan statute leaves much to be desired in the regulation of subsequent purchases of goods. In its compromise to equalize the bargaining position of the seller and the buyer, the buyer needs more and gets very little protection and support. As the statute was passed within days of the adoption of the UCC, there should have been a more consistent relationship, especially where the Michigan statute is not affected by the repealer provisions of the UCC. If the unwary buyer is to receive much needed protection, a statute similar to that of New York would be more desirable.

EDWARD BOGRAD

TRADE REGULATION

The Tariff Classification Act of 1962, which provides for the adoption and implementation of revised tariff schedules, was enacted into law on May 24, 1962.¹ Although creating no rate changes the act attempts to simplify product classifications and to make them more consistent with present trade conditions. Under the act, as soon after the enactment of the legislation as is practicable, the President is authorized to take whatever steps he deems necessary to bring the several trade agreement schedules into line with the new tariff schedules.² This "conforming process will not involve changes in the new tariff schedules; the trade agreement schedules will be changed to conform to the new tariff schedules."³ At the present time, the provisions under which the bulk of the import trade of the United States is classified for tariff purposes are "modified" provisions subject to "concessions made by the United States in foreign trade agreements and proclaimed by the President under authority of trade agreements

until all the instalment payments are completed. The New York statute clearly sets out a method of allocation which gives the buyer protection.

³³ *Supra* note 16, at § 5.

³⁴ The Model Retail Instalment Sales Act, *supra* note 25, provides civil remedies for the buyer as well as criminal penalties against the seller. Generally, a violation by the seller of a particular section will impose a penalty payment to the buyer of an amount equal to the first instalment payment. Sections 2(e), 3(b), 4(c), 5(b), 6(e), & 8(e). Section 16 provides a criminal penalty as well for any wilful violation by the seller of any section of the act.

¹ Pub. L. No. 87-456, 87th Cong., 2d Sess., 76 Stat. 72 (1962).

² The tariff schedules consist of the proposed schedules included in the United States Tariff Commission's report of November 15, 1960, as changed by the First Supplemental Report of January 1962.

³ 9 U.S. Code Cong. & Ad. News 992 (June 20, 1962).