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# Sales - Conditional Sales - Whether a Clause Waiving all Defenses, Counterclaims or Cross-Complaints in Favor of an Assignee of a Note Bars the Defense of Failure of Consideration

C. F. Anderson

SALES—CONDITIONAL SALES—WHETHER A CLAUSE WAIVING ALL DEFENSES, COUNTERCLAIMS OR CROSS-COMPLAINTS IN FAVOR OF AN ASSIGNEE OF A NOTE BARS THE DEFENSE OF FAILURE OF CONSIDERATION—The Appellate Court for the First District of Illinois was recently asked, in the case of *Commercial Credit Corporation* v. *Biage*,[1] to determine a hitherto unraised question in Illinois. The defendant therein had signed a note, appurtenant to a conditional sales contract, containing an agreement not to assert any defense against an assignee thereof.[2] The note was assigned to the plaintiff who ultimately confessed judgment thereon. In a motion to open the judgment, the defendant alleged that the consideration for the note had failed. The trial court, however, denied his motion when it concluded that the waiver embodied in the conditional sales contract prevented the assertion of such a defense. On appeal, the reviewing tribunal indicated its agreement with the interpretation of the trial court and held the waiver provision valid on the ground that it was permitted by the Uniform Sales Act.[3] Affirmance followed as a matter of course.[4]

Conditional sellers have long sought a formula for quick negotiability of consumer conditional sales contracts. Since it would seem that such contracts are almost invariably assigned or discounted, any element of negotiability which a seller can embody in the contract will tend to make the paper more appealing to financiers, since then the risk of loss resulting from a breach of contract by the seller will fall on the conditional buyer and not the assignee. In an effort to import to their contracts one of the most important characteristics of negotiability, namely, freedom from defenses possessed by the obligor when the instrument passes to an assignee, the conditional sellers have inserted no-defense clauses like that in the instant case,[5] included negotiable notes evidencing the pur-

[1] 11 Ill. App. (2d) 80, 136 N. E. (2d) 580 (1956).

[2] The clause in the contract read as follows: "This contract may be assigned and/or said note may be negotiated without notice to me and when assigned and/or negotiated shall be free from any defense, counterclaim or cross-complaint by me."

[3] Ill. Rev. Stat. 1955, Vol. 2, Ch. 121½, § 71, which reads as follows: "Where any right, duty or liability would arise under a contract to sell or a sale by implication of law, it may be negatived or varied by express agreement . . ."

[4] The court, in its opinion, made mention of the fact that while there was much discussion in the briefs regarding the laws of negotiable instruments, they felt that reference thereto was unnecessary to achieve the decision in view of the provision in the Uniform Sales Act.

[5] See American Nat. Bank. v. A. G. Sommerville, Inc., 191 Cal. 364, 216 P. 376 (1923).

chase price along with the contract,[6] and have also gone as far as to draft the contract itself as a promissory note.[7]

It is a fundamental axiom of the law of contracts that there must be a good and valuable consideration flowing between the parties thereto or no binding agreement can result. Once a substantial failure of the purported consideration is proved, the contract becomes unenforceable as between the parties[8] and may be rescinded.[9] Thus one would expect that the question to be initially determined would be that of the validity of the original contract of which the waiver clause is a part. It would seem apparent that with the unlimited use of such waiver clauses the aforementioned axiom will become the exception and not the rule since the waiver clause holds the contract up by its own bootstraps and would circumvent any attempt to look to the original agreement for its formal necessities. In determining the validity of the no-defense clauses, however, the courts do not seem to base their decisions on the nature of the particular defense sought to be asserted, to-wit, failure of consideration, fraud, breach of warranty, etc., but rather upon the basic validity of the clause itself as affecting all such defenses. Those courts which have made an effort to give some protection to the consumer buyer, by refusing to uphold such a waiver or cut-off clause, have advanced a number of interrelated reasons for so doing. At least one jurisdiction has held such clauses invalid for violating an existing state statute, insofar as they denied the right to utilize defenses which existed before notice of the assignment.[10] It has also been held that a conditional sales contract which does not on its face meet the elements of negotiability, cannot achieve such a position by the use of a waiver clause providing for negotiable character of the instrument, since only an instrument complying with the requirements of the statute is negotiable.[11] Still a further reason for holding such a clause invalid was advanced in the case of *Bridger* v.

[6] Jones. The Law of Chattel Mortgages and Conditional Sales (The Bobbs Merrill Co., Indianapolis, 1933), 6th Ed., Vol. 3, §§ 940-2, pp. 48-52, and cases cited therein.

[7] See Abingdon Bank & Trust Co. v. Shipplett-Moloney Co., 316 Ill. App. 79, 43 N. E. (2d) 857 (1942).

[8] See 17 C. J. S., Contracts, § 129, p. 476, and cases cited therein.

[9] Ibid., § 420, p. 905, and cases cited therein.

[10] San Francisco Securities Corp. v. Phoenix Motor Co., 25 Ariz. 531, 220 P. 229 (1923). The statute involved was Ariz. Civ. Code 1913, par. 402, and provided that "an action by the assignee shall be without prejudice to any defense existing before notice of the assignment . . ."

[11] Motor Contract Co. v. Van Der Volgen, 162 Wash. 449, 298 P. 705 (1931); American Nat. Bank v. A. G. Sommerville, Inc., 191 Cal. 364, 216 P. 376 (1923).

*Goldsmith*[12] where the defense was that of fraud. The court there held that the fraud involved vitiated the entire contract of which the waiver clause was a part. Further approaches used to deny the validity of the clauses are that the assignee under such a contract acquires the rights as well as the liabilities of the seller and thus stands in his shoes as to all defenses which the buyer has against his vendor;[13] or is held to be a party to the agreement;[14] or that he had a duty to see that the merchandise or equipment involved performed adequately.[15]

While all of the foregoing decisions have been achieved by application of existing principles of law, the great compulsion which seems to underlie most of them is that of public policy. It must be admitted that the term public policy is ambiguous and somewhat obscure, but it seems to be the only one available to embrace the many bases which the courts use in denying the validity of the no-defense clauses. It is generally considered that parties may agree to waive contract, statutory, or other rights, unless a question of public policy is involved.[16] Thus while some of the courts have gone to great lengths to justify their decision, the majority of those which hold such clauses invalid, have done so on the basis of public policy.[17] The feeling of these courts seems to be best expressed by the statement of O'Brien, J. in the Bridger case where he said, "it is difficult to conceive that such a clause could ever be suggested by a party to a contract unless there was in his own mind at least a lingering doubt as to the honesty and integrity of his conduct. Public

[12] 143 N. Y. 424, 38 N. E. 458 (1894); see also, First Acceptance Corp. v. Kennedy, 95 F. Supp. 861 (1951) (where a waiver of fraud clause is embodied in a fraudulently obtained contract, the waiver clause is ineffective as to the defense of fraud); and Ebenreiter v. Freeman,—Wis.—, 79 N. W. (2d) 649 (1956) (conditional sales contract invalid, thus the waiver clause therein is of no effect).

[13] Bulldog Concrete Forms Sales Corp. v. Taylor, 195 F. (2d) 417 (1952), affirming 94 F. Supp. 328 (1952); Parker v. Funk, 185 Cal. 347, 197 P. 83 (1921); First Lumberman's Nat. Bank v. Buckholz, 220 Minn. 97, 18 N. E. (2d) 771 (1945); Universal Credit Co. v. National Radio Mfg. Co., 174 Okla. 178, 49 P. (2d) 743 (1935); Mercantile Trust Co. v. Roland, 143 Okla. 190, 288 P. 300 (1930); Gen. Elec. Cont's. Corp. v. Heimstra, 69 S. D. 78, 6 N. W. (2d) 445 (1942); Pearson v. Picco, 181 Wash. 613, 44 P. (2d) 186 (1935).

[14] Commercial Credit Co. v. Childs, 199 Ark. 1073, 137 S. W. (2) 260 (1940).

[15] C. V. Hill & Co. v. Hadden's Grocery, 299 Ky. 419, 185 S. W. (2d) 681 (1941).

[16] 12 Am. Jur., Contracts, § 181, p. 682.

[17] Equipment Acceptance Corp. v. Arwood Can Mfg. Co., 117 F. (2d) 442 (1941); San Joaquin Finance Corp. v. Allen, 102 Cal. App. 400, 283 P. 117 (1929); American Nat. Bank v. A. G. Sommerville, Inc., 191 Cal. 364, 216 P. 376 (1923); Pacific Acceptance Corp. v. Whalen, 43 Idaho 15, 248 P. 444 (1926); Industrial Loan Co. v. Grisham,—Mo. App.—, 115 S. W. (2d) 214 (1938); Progressive Finance & Realty Co. v. Stempel, 321 Mo. App. 721, 95 S. W. (2d) 834 (1933); State Nat. Bank of El Paso, Tex., v. Cantrell, 47 N. M. 389, 143 P. (2d) 592 (1943); Motor Contract Co. v. Van Der Volgen, 162 Wash. 449, 298 P. 705 (1931); Malas v. Lounsbury, 193 Wis. 531, 214 N. W. 332 (1927); D. M. Osborne & Co. v. M'Queen, 67 Wis. 342, 29 N. W. 636 (1886).

policy and morality are both ignored if such an agreement can be given effect in a court of justice."[18] A further element of public policy which urges the judicial repudiation of such clauses is that they are designed to settle in advance the substantive rights of the parties under the contract and oust the courts of their jurisdiction to determine such rights. As was said in *Industrial Loan Co.* v. *Grisham*,[19] "after a right has accrued, a party may waive his rights, but it is not permissible for him to stipulate in advance that in the event of differences arising in the future he will deny himself the right to resort to the courts for their settlement." This is an expression of the idea that the state has an interest in all of its inhabitants which interest demands that the rights of all should be protected and enforced according to the course of jurisprudence which has been provided.

The instant case does, however, find much support in many cases where the courts have given full effect to such waiver clauses.[20] While they recognize that at the time of the sale the parties should have a right to place in their contract any terms or conditions which are not unlawful or against public policy, the dividing point seems to involve a question of just what is against public policy. The general feeling in most of these cases is that this type of clause is not injurious to the public or against the public good and that to deny to men of full age and competent understanding the right to deal as they see fit would prove to be even worse than the results of holding such clauses valid.[21] The decision in the instant case receives its greatest support from the case of *United States* v. *Troy-Parison, Inc.*,[22] where the United States Court of Appeals for the Ninth Circuit said that "the provision does not run counter to the declared policy of Idaho, since the state code allows parties to negative their rights and duties arising under a contract, by express agreement."[23] The court, however, did limit its decision to instances of breach of warranty.

The problem of determining the validity of the no-defense clauses

[18] Bridger v. Goldsmith, 143 N. Y. 424, 38 N. E. 458 (1894).

[19] —Mo. App. —, 115 S. W. (2d) 214 (1938).

[20] See United States v. Troy Parison, Inc., 115 F. (2d) 224 (1940); Refrigeration Discount Corporation v. Haskew, 194 Ark. 549. 108 S. W. (2d) 908 (1937); A. J. Colson & Sons v. Ellis, 50 Ga. App. 768, 151 S. E. 654 (1930); Elzey v. Ajax Heating Co., 10 N. J. Misc. 281, 158 A. 851 (1932); Glens Falls Nat. Bank & Trust Co. v. Sansivere, 136 N. Y. S. (2d) 672 (1955); President and Directors, Etc. v. Monogram Associates, 276 App. Div. 766, 92 N. Y. S. (2d) 579 (1949); National City Bank v. Prospect Syndicate, 170 Misc. 611, 10 N. Y. S. (2d) 759 (1939); Security Holding Co. v. Christensen, 53 S. D. 37, 219 N. W. 949 (1928); Anglo-California Trust Co. v. Hall, 61 Utah 223, 211 P. 991 (1922).

[21] Elzey v. Ajax Heating Co., 10 N. J. Misc. 281, 158 A. 851 (1932).

[22] 115 F. (2d) 224 (1940).

[23] 115 F. (2d) 224 at 226.

seems to be one which demands the attention and voice of the legislature for its ultimate determination. While the holding in the instant case seems at first blush extremely inconsistent with the original attitude in Illinois toward the validity of conditional sales contracts,[24] one must admit that the present status of the law justifies such a holding. Unless the court is willing to realize the position and limited legal understanding of the average buyer under such a contract, thus necessitating the public policy argument, it can come to no other conclusion than that of enforcing the contract in its entirety. The law, as a general proposition, says that courts cannot rewrite contracts into which parties have seen fit to enter and that a man is bound by his contract. When such principles are backed up by clauses such as that in the Illinois Sales Act,[25] the courts are left no alternative other than some aspect of public policy. If the public are to be given adequate protection in their commercial dealings, such protection must come from the law making body. Such a step in the right direction has been taken in the Uniform Commercial Code,[26] which to date has had but limited acceptance.[27] It is not the purpose of this note to decide whether this provision or some other means is the answer to a growing problem but rather to point out the need of some definite determination of the issues involved. In this light, it might well be asked, is there a place in our social order for the seller who, in his dealings with the public, needs an accompanying waiver to carry his luggage?

C. F. ANDERSON

TORTS—INVASION OF PERSONAL SAFETY, COMFORT, OR PRIVACY—WHETHER PUBLIC EXPLOITATION OF A DEBTOR'S PERSONAL AFFAIRS BY A COLLECTION AGENT IS AN INVASION OF THE DEBTOR'S RIGHT OF PRIVACY—A significant problem concerning a debtor's right of privacy came before the Supreme Court of Ohio for the first time in the case of *Housh* v. *Peth*.[1]

[24] See Gilbert v. Nat. Cash Register Co., 176 Ill. 288, 52 N. E. 22 (1898); and Brundage v. Camp, 21 Ill. 329 (1859). Both were overruled in Sherer-Gillett Co. v. Long, 318 Ill. 432, 149 N. E. 225 (1925). The original attitude of the courts in Illinois was that a secret reservation of title to personal property amounted to a constructive fraud and was invalid against a bona fide purchaser or subsequent incumbrancer for value.

[25] Ill. Rev. Stat. 1955, Vol. 2, Ch. 121½, § 71.

[26] Uniform Commercial Code, Part 2, § 9—206, which reads in part as follows: "An agreement by a buyer of consumer goods as part of the contract for sale that he will not assert against an assignee any claim or defense arising out of the sale is not enforceable by any person."

[27] Kohn, "The Present Status of the Uniform Commercial Code," 45 Ill. B. J. 224 (1956). Although the code was immediately referred to legislative committees in a number of states, it has since become law only in Pennsylvania.

[1] 165 Ohio St. 35, 133 N. E. (2d) 340 (1956), affirming—Ohio—, 135 N. E. (2d) 440 (1955), noted in 7 Western Res. L. Rev. 452 and 2 Wayne L. Rev. 240. Hart, J. wrote a dissenting opinion, concurred in by Stewart and Taft, J. J.