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## Judgements: The Cognovit Clause and Due Process

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JUDGMENTS: THE COGNOVIT CLAUSE AND DUE PROCESS\*

*D.H. Overmyer Co. v. Frick Co.*, 405 U.S. 174 (1972)

Appellant corporation defaulted on payments for equipment being installed, but respondent company satisfactorily completed the work after appellant issued an installment note for the balance. When appellant was unable to make payments on this note attorneys for both parties negotiated the replacement of the first note with a note containing a cognovit<sup>1</sup> clause, acceptable under Ohio law,<sup>2</sup> in which appellant consented to a judgment obtained by respondent without notice or hearing at the time of default. In consideration for this provision and for second mortgages on appellant's property, respondent reduced interest rates and monthly payments, extended the time for payment, and released mechanic's liens on the property. Claiming breach of the original contract, appellant stopped making payments. Pursuant to the cognovit clause in the second note, respondent had an attorney unknown to appellant confess judgment on behalf of appellant, who had not been served or otherwise notified of the action. Ohio courts overruled appellant's motion to vacate the judgment and appellant appealed, contending that the entry of judgment pursuant to the cognovit clause violated due process. The United States Supreme Court HELD, that due process was not violated by the cognovit procedure, since the corporate appellant waived its rights to notice and hearing by approving the cognovit provision with full knowledge of the legal consequences.<sup>3</sup>

Courts have traditionally held that by signing a contract containing a cognovit clause, a debtor has voluntarily assented to the jurisdiction of the court without service of process.<sup>4</sup> In the summary proceeding authorized by a cognovit clause, a creditor may obtain judgment without having to disprove any defense that the debtor may assert.<sup>5</sup> Such judgment has the same legal effect as a judgment entered by a jury after a full trial,<sup>6</sup> but it is not irre-

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\*EDITOR'S NOTE: This case comment was awarded the *George W. Milam Award* as the outstanding case comment submitted by a Junior Candidate in the summer 1972 quarter.

1. A cognovit note "authorizes an attorney to confess judgment against the person or persons signing it. It is written authority of a debtor and a direction by him for the entry of a judgment against him if the obligation set forth in the note is not paid when due." *Jones v. John Hancock Mut. Life Ins. Co.*, 289 F. Supp. 930, 935 (W.D. Mich. 1968), *aff'd*, 416 F.2d 829 (6th Cir. 1969).

2. OHIO REV. CODE ANN. §2323.13 (Baldwin 1968).

3. 405 U.S. 174 (1972).

4. *E.g.*, *Dayton Morris Plan Bank v. Graham*, 47 Ohio App. 310, 191 N.E. 817 (1934); *Horner Sales Corp. v. Motor Sport, Inc.*, 377 Pa. 392, 105 A.2d 285 (1954).

5. *E.g.*, *Hadden v. Rumsey Products, Inc.*, 195 F.2d 92, 96 (2d Cir. 1952); *Jones v. John Hancock Mut. Life Ins. Co.*, 289 F. Supp. 930, 935 (W.D. Mich. 1968), *aff'd*, 416 F.2d 829 (6th Cir. 1969).

6. *George W. McAlpin Co. v. Finsterwald*, 57 Ohio St. 524, 49 N.E. 784, 789 (1898); *O'Hara v. Manley*, 140 Pa. Super. 39, 12 A.2d 820 (1940).

vocable. The debtor may obtain relief from a cognovit judgment either by a motion to vacate or a petition to reopen the judgment.<sup>7</sup>

Although of ancient origin,<sup>8</sup> the cognovit clause is still used in a few American jurisdictions.<sup>9</sup> In most jurisdictions it is void or severely limited by statute,<sup>10</sup> but some states either specifically provide for such provisions<sup>11</sup> or have no pertinent statutes.<sup>12</sup> Opponents of the confession of judgment<sup>13</sup> generally base their objections on the fact that it denies the debtor the right to his day in court.<sup>14</sup> Critics also object to the cognovit's potential for abuse, especially in the hands of high pressure salesmen and small loan companies<sup>15</sup> dealing with consumers likely to be unaware of the legal consequences of signing a contract containing such a provision. As a result, cognovit clauses have been closely scrutinized<sup>16</sup> and strictly construed<sup>17</sup> by the courts. These clauses have also been held unconscionable or not indicative of the desires of the debtor<sup>18</sup> when the authority to confess judgment was not explicitly granted.<sup>19</sup>

The Supreme Court has considered cognovit notes on two previous occasions,<sup>20</sup> but both of these cases concerned the obligation of a state to grant full faith and credit to a confessed judgment. Although these decisions

7. *De Rose v. Lombardi*, 413 Pa. 258, 196 A.2d 336 (1964). For a discussion of the similar Ohio procedure applicable in the instant case, see Hunter, *The Warrant of Attorney To Confess Judgment*, 8 OHIO ST. L.J. 1, 12 (1941).

8. *First Nat'l Bank v. White*, 220 Mo. 717, 120 S.W. 36 (1909).

9. The overwhelming bulk of cognovit judgments taken in the United States are produced in Illinois, Pennsylvania, and Ohio. Hopson, *Cognovit Judgments: An Ignored Problem of Due Process and Full Faith and Credit*, 29 U. CHI. L. REV. 111, 115 (1961).

10. *E.g.*, ALA. CODE, tit. 20, §16 and tit. 62, §248 (1958); FLA. STAT. §55.05 (1971); MASS. GEN. LAWS ch. 231, §13A (1959). For a full listing of all applicable statutes, see Note, *A Clash in Ohio?: Cognovit Notes and the Business Ethic of the UCC*, 35 U. CIN. L. REV. 470, 490-91 (1966).

11. *E.g.*, ILL. ANN. STAT. ch. 110, §50 (Smith-Hurd 1968); MO. REV. STAT. §511.100 (1949); OHIO REV. CODE ANN. §2323.13 (Baldwin 1968).

12. Maine, New Hampshire, and Rhode Island. The weight of authority is that cognovit clauses were valid at common law. *E.g.*, *First Nat'l Bank v. White*, 220 Mo. 717 120 S.W. 36 (1909). *But see* *General Contract Purchase Corp. v. Max Keil Real Estate Co.*, 35 Del. 531, 170 A. 797 (Super. Ct. 1933) (denies common law authority).

13. The terms "confession of judgment" and "cognovit" are commonly used interchangeably.

14. *See, e.g.*, Hopson, *Cognovit Judgments: An Ignored Problem of Due Process and Full Faith and Credit*, 29 U. CHI. L. REV. 111 (1961); Leary, *Random Reflections on Remedies and Collections in the Consumer Credit Field*, 19 AM. U.L. REV. 189 (1970); Note, *Resort to Legal Process in Collecting Debts from High Risk Credit Buyers in Los Angeles—Alternative Methods of Allocating Present Costs*, 14 U.C.L.A.L. REV. 879 (1967).

15. Some states prohibit the use of cognovit clauses by small loan companies. *E.g.*, CAL. FIN. CODE §24.468 (1958); FLA. STAT. §516.16 (1971); NEV. REV. STAT. §675.350 (1968).

16. *E.g.*, *Park Hotel Co. v. Eckstein-Miller Auto Co.*, 181 Wis. 72, 193 N.W. 998 (1923).

17. *E.g.*, *Spence v. Emerine*, 46 Ohio St. 433, 21 N.E. 866 (1889).

18. *E.g.*, *Cutler Corp. v. Latshaw*, 374 Pa. 1, 97 A.2d 234 (1953).

19. *Solazo v. Boyle*, 365 Pa. 586, 76 A.2d 179 (1950).

20. *National Exch. Bank v. Wiley*, 195 U.S. 257 (1904); *Grover & Baker Sewing Mach. Co. v. Radcliffe*, 137 U.S. 287 (1890).

indicate a distaste for cognovit judgments<sup>21</sup> the validity of the procedure was impliedly recognized. In the instant case the Court stated that the judgment could not be invalidated on the basis of contract law, since a valuable consideration was given for the insertion of the cognovit clause.<sup>22</sup> Therefore, the appellant could succeed only if the cognovit procedure violated due process.

Contending that the state court had no in personam jurisdiction without service of process and that the appearance by an attorney unknown to appellant did not cure this defect,<sup>23</sup> appellant claimed that the state court did not have the power to render a valid judgment. Furthermore, appellant claimed advance waiver of the right to present a defense was an unconstitutional deprivation of fourteenth amendment due process.<sup>24</sup> However, the Court found assent to the inclusion of a cognovit provision in the note with full knowledge of the legal consequences operated as an effectual waiver of appellant's constitutional right to reasonable notice of the pendency of a legal action.<sup>25</sup>

The Court relied on *National Equipment Rental, Ltd. v. Szukhent*<sup>26</sup> for the proposition that notice could be waived in advance. In that case validity of service of process on an agent appointed through an equipment rental contract was upheld, even though the agent was not required by the contract to notify the defaulting debtor. The present case is distinguishable, however, because basic to the *Szukhent* decision was the agent's actual notice to the defendant.<sup>27</sup> In contrast, appellant in the instant case was not entitled to notice under the cognovit clause and no actual notice was received until judgment had been entered.<sup>28</sup>

Although the instant Court noted that appellant had an opportunity to defend on the merits of its claim after judgment had been entered,<sup>29</sup> the Court could not use this post-judgment hearing to justify its decision. In *Sniadach v. Family Finance Corp.*<sup>30</sup> the Court invalidated as violative of due process Wisconsin statutes that authorized garnishment of wages<sup>31</sup> without

21. The Court indicated its distaste for cognovit notes by relying on technicalities and construing the notes very strictly. In *National Exch. Bank v. Wiley*, 195 U.S. 257 (1904), the Court refused to enforce a cognovit judgment entered by an Ohio court because the original payee transferred the note to another bank. The Court construed the word "holder" in the note to preclude enforcement. In *Grover & Baker Sewing Mach. Co. v. Radcliffe*, 137 U.S. 287 (1890), the Court refused to enforce a cognovit judgment because the instrument authorized any attorney to confess judgment and the judgment had been confessed by a prothonotary. The Court further stated "[t]he courts of Maryland were not bound to hold this judgment as obligatory either on the ground of comity or of duty, thereby permitting the law of another State to override their own." *Id.* at 299.

22. 405 U.S. at 183.

23. *Id.* at 186.

24. *Id.* at 184.

25. *Id.*

26. 375 U.S. 311 (1964).

27. *Id.* at 315.

28. 405 U.S. at 182.

29. *Id.* at 188.

30. 395 U.S. 337 (1969).

31. Wis. STAT. §267.04(1) (1967).

prior notice to the debtor,<sup>32</sup> although service on the debtor within ten days after garnishment and a post-garnishment hearing were required.<sup>33</sup> The *Sniadach* Court held that a taking of property without prior opportunity to be heard was repugnant to the fourteenth amendment.<sup>34</sup>

The Court reaffirmed *Sniadach* in *Fuentes v. Shevin*,<sup>35</sup> decided after the instant case, which held that Florida statutes authorizing creditors to obtain *ex parte* writs of replevin enforceable prior to required hearings denied debtors procedural due process. The Court again found that a subsequent hearing would not cure the due process defects inherent in any taking of property without a prior opportunity to be heard.<sup>36</sup> Since the post-judgment proceeding in the present case was on a motion to vacate a judgment entered in appellant's absence, the availability of this proceeding could not save the cognovit judgment from unconstitutionality on due process grounds.

The instant decision rests solely on appellant's waiver of its constitutional rights to prior notice and hearing. While a waiver of constitutional rights will not be presumed, even in civil cases,<sup>37</sup> cases involving such waiver must be decided on a case-by-case basis.<sup>38</sup> Therefore, it is not surprising to find the Court expressly limiting its decision to the facts of the case.

Despite this limitation, the importance of the principal case is twofold. First, it indicates the Court's unwillingness to prohibit categorically the use of cognovit judgments by finding these judgments per se violative of due process. At the same time the Court implied that in certain situations cognovit judgments will be repugnant to due process. For instance, the Court delineated the following factors as likely to cause a due process violation: a contract of adhesion, great disparity of bargaining power, and a lack of consideration for the cognovit provision.<sup>39</sup>

The language used by the Court in outlining these criteria,<sup>40</sup> however, does not convey whether all of these factors must be present or if any one factor will support invalidation of a cognovit clause as violative of due process. The Court noted that the contract in the instant case was not a contract of adhesion or a case of unequal bargaining power, and stressed that valuable consideration was given for the insertion of the cognovit provision.<sup>41</sup> The Court's emphasis on the fact that the present case contained none of the criteria of a due process violation, however, permits the inference that

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32. WIS. STAT. §267.07 (1) (1967).

33. WIS. STAT. §267.16 (1) (1967).

34. *Sniadach v. Family Fin. Corp.*, 395 U.S. 337, 339 (1969).

35. 407 U.S. 67 (1972).

36. *Id.* at 85.

37. *Aetna Ins. Co. v. Kennedy*, 301 U.S. 389, 393 (1937); *Ohio Bell Tel. Co. v. Public Util. Comm'n*, 301 U.S. 292, 307 (1937).

38. *Johnson v. Zerbst*, 304 U.S. 458, 464 (1938).

39. 405 U.S. at 188.

40. "For example, where the contract is one of adhesion, where there is great disparity in bargaining power, and where the debtor receives nothing for the cognovit provision, other legal consequences may ensue." *Id.*

41. *Id.* at 182.

the presence of any one of these factors will render a cognovit note unenforceable. Since contracts of adhesion and inequality of bargaining power are the hallmarks of consumer contracts, the dictum of the principal case is a warning that cognovit clauses in consumer contracts will be subject to invalidation in the future.

Although the Court implied a willingness to find cognovit judgments violative of due process in certain situations,<sup>42</sup> the present case indicates no sweeping declaration of unconstitutionality is likely to be forthcoming.<sup>43</sup> Rather, it appears the Court will proceed on a case-by-case basis, determining whether each judgment debtor intelligently waived his rights.<sup>44</sup> However, the present decision should not increase litigation.<sup>45</sup> Since few consumers have the resources necessary to challenge the constitutionality of cognovit judgments entered against them, the instant decision is likely to perpetuate the enforcement of cognovit provisions in consumer contracts where otherwise allowed by local law. In addition, the summary proceeding authorized by cognovit notes precludes litigation<sup>46</sup> so that the total volume of litigation will be less than if the cognovit note had categorically been declared invalid.

While delineating criteria of future import to the waiver of procedural due process the Court protected the rights of a creditor against a debtor, which had for valuable consideration and with full knowledge of the legal consequences accepted the very terms it asked the court to invalidate. Although distinguishable from cases such as *Sniadach* and *Fuentes*, the instant decision demonstrates that the Court is unwilling to invalidate every summary creditor remedy, thus reestablishing a needed equilibrium between creditor and debtor.

LEIGHTON D. YATES, JR.

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42. *Id.* at 188.

43. *In Swarb v. Lennox*, 405 U.S. 191 (1972), decided the same day as the instant case, the Court affirmed the decision of a three-judge court in which plaintiffs brought a class action alleging that the Pennsylvania cognovit procedure was inconsistent with due process. The lower court held that the procedure was not unconstitutional on its face, but declared that no cognovit judgment could be entered against natural persons earning less than \$10,000 annually unless it could be shown that the debtor had understandingly waived his rights. The plaintiffs appealed, seeking a general declaration that cognovit provisions were unconstitutional. The Supreme Court cited the present case and held that under appropriate circumstances an individual debtor was as capable of waiving his rights as a corporate debtor. Since Pennsylvania did not appeal, the Court declined to rule on the validity of the lower court's finding that cognovit judgments could not be entered against low-income groups, holding that the issue was not properly before the Court.

44. Proceeding on a case-by-case basis allows the Court the discretion to weigh the equities of each case. The equities in the instant case, which weighed heavily against the judgment debtor, were instrumental in the Court's decision. 405 U.S. at 188.

45. Jurisdictions not using cognovit notes encounter them only in a full faith and credit context. Since the cognovit clause in the instant case was held valid, however, a sister state would be obliged to enforce it. *But see Atlas Credit Corp. v. Ezrine*, 25 N.Y.2d 219, 250 N.E.2d 474, 303 N.Y.S.2d 382 (1969), where the Court of Appeals of New York refused to enforce a Pennsylvania cognovit judgment, holding it violative of due process.

46. One Ohio study revealed that only 5.2% of the cognovit judgments were challenged. See Hunter, *supra* note 7, at 15.