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Chapter 6: Commercial Law

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CHAPTER 6

Commercial Law

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§6.1. General. Commercial law has been the subject of only a moderate amount of activity during the 1960 SURVEY year. In the area of general legislation, Rhode Island has become the sixth state to adopt the Uniform Commercial Code, which will become effective on January 2, 1962.[1] In this Commonwealth, in addition to some random banking legislation discussed in Sections 6.6-6.9 *supra,* civil rights have been expanded to some extent through banking legislation. Discrimination in the granting of mortgage loans by one in the business of making these loans has been added to the list of "unlawful practices" provided by Section 4 of Chapter 151B of the General Laws.[2]

§6.2. Consumer credit. On May 25, 1960, the Judicial Council was requested to investigate consumer protection in instalment purchases of goods other than motor vehicles, to report with its recommendations, and to submit drafts of any legislation to be proposed.[1] Last year, the Commonwealth adopted a comprehensive scheme of regulation of instalment purchases of motor vehicles by consumers. It would seem that the probability of further legislation in the near future covering other consumer goods is quite high.

In the meantime, legislation concerning consumer credit has continued on a piecemeal basis, through the adoption of two statutes. The first concerns the liability of the maker of a note for a deficiency after the sale of a repossessed motor vehicle. The Uniform Commercial Code article on secured transactions requires that a creditor must sell repossessed collateral if he expects to claim a deficiency.[2] Although the creditor has wide discretion in the manner of selling, the disposition must be in a "commercially reasonable" manner; the penalty for failure to comply is that the debtor may recover damages which, in the case of consumer goods, will be at least equal to the credit service charge plus 10 percent of the principal amount of the

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§6.1. [1] R.I. Laws 1960, S.B. No. 546.
[2] Acts of 1960, c. 163.

§6.2. [1] Resolves of 1960, c. 66.
[2] G.L., c. 106, §9-505.

debt.[3] The comprehensive regulation of retail instalment sales of motor vehicles adopted in 1959 has now been amended to bar any deficiency unless the holder of the note files an affidavit signed by the purchaser of the vehicle, stating the price paid and the date and place of sale.[4] Presumably, this will discourage attempts to sue for a deficiency unless the disposition of the collateral was in the required "commercially reasonable" manner.

In the second statute affecting consumer credit, the right to save unusual interest charges by prepayment has been extended. Loans up to $1500, secured by a mortgage on property having an assessed value of not over $10,000, may carry interest as high as 1½ percent per month. The borrower under such a loan now has a statutory right to prepay in whole or in part at any time without penalty.[5] Since interest must be computed monthly on the unpaid balance, unearned interest can be eliminated entirely by prepayment.

§6.3. Commercial paper: Interest. The proposition that the primary obligor on a demand instrument — other than a certificate of deposit — is liable at once, subject to suit at any time even though no demand has been made, was well settled by case law before the enactment of the Uniform Commercial Code. (Since a certificate of deposit is more like a contract for the safekeeping of money than a loan that the debtor is obligated to repay, it was commonly held that suit on such an obligation could not be brought until demand had been made.) The Code, in specifying the time of accrual of the cause of action against the various parties to an instrument, has accepted this proposition. In addition, the Code specifies the time that interest begins to run when the instrument is silent about interest; the general rule is that interest at the judgment rate runs from the date of the accrual of the cause of action.[1]

Although there may be good reasons to allow interest on non-interest-bearing time instruments after they are overdue, a similar rule for demand instruments — in view of the accrual of the cause of action without demand — would not seem to be justified, at least before demand has been made. The Code does, therefore, require a demand to start the running of interest against the maker of a demand note, although demand is not a prerequisite to suit. The legislature has now extended this exception to the general rule to the liability of acceptors and other primary obligors of demand instruments.[2] Thus, the bank that certifies a check or the purchaser of goods who accepts a non-interest-bearing demand trade acceptance will have no obligation to pay interest as long as no demand for payment is made. This is certainly in accord with common commercial practice.

[3] Id. §9-504.
[4] Acts of 1960, c. 173; statute also noted in §9.4 *infra*.
[5] Acts of 1960, c. 446, amending G.L., c. 140, §90A; statute also noted in §9.4 *infra*.

§6.3. [1] G.L., c. 106, §3-122.
[2] Acts of 1960, c. 273.

§6.4. Commercial paper: Notice of dishonor. *Durkin v. Siegel*[1] was an action against the indorser of a note. The question involved was whether notice of dishonor sent by certified mail but never actually received by the indorser was sufficient to establish the indorser's liability. The Supreme Judicial Court held that it was.

There are, of course, many legal situations in which required notice must be received. Thus, a statute requiring notice of the cancellation of compulsory motor vehicle liability insurance has been held to have been designed to protect the general public, so that even the contract of insurance itself could provide for nothing less than receipt of notice prior to cancellation.[2] The statutory requirement of notice within thirty days after injury from snow or ice has been held not to be satisfied without receipt of the notice, the Court stating: "Deposit in the mail is evidence of notice, but is not of itself notice."[3] The requirement that notice of dishonor be given to parties secondarily liable on commercial paper, however, is not of this nature. Although the requirement is an exacting one, and is a condition to the liability of an indorser on his contract, it may be waived voluntarily or entirely excused when impracticable.

The factual difficulty in the *Durkin* case was that the notice would have been received if it had been sent by ordinary mail. Since it was sent by certified mail, and since the indorser was out of the country at the time and had not designated an agent to receive such mail, it was returned to the sender. The Court decided that the plaintiff would not be penalized for having used what is generally regarded as a preferred method of ensuring delivery.

Although this decision was based upon an analysis of the statutes in force prior to the Uniform Commercial Code, it indicates that the Court considers certified mail to be a reasonable manner of giving notice, which is all that the Code requires.[4]

§6.5. Secured transactions: Filing. The Uniform Commercial Code article on secured transactions has been amended to provide for the details of recording and indexing, and for appropriate fees therefor, when filing is to be with the registry of deeds because the chattel becomes a fixture. If a single mortgage includes both fixtures and realty, the filing of a single instrument with the registry of deeds is now sufficient.[1]

The effectiveness of a security interest when the financing statement contains minor errors was involved in *Sales Finance Corp. v. McDermott Appliance Co.*[2] The corporate debtor used the abbreviation "Co." in its signature and description on the financing statement. The

§6.4. [1] 340 Mass. 445, 165 N.E.2d 81 (1960).
[2] Taxeira v. Arter, 292 Mass. 537, 198 N.E. 900 (1935).
[3] Regan v. Atlantic Refining Co., 304 Mass. 353, 354, 23 N.E.2d 869, 870 (1939).
[4] G.L., c. 106, §3-508.

§6.5. [1] Acts of 1960, c. 379, amending G.L., c. 106, §9-403, and adding §9-409.
[2] 340 Mass. 493, 165 N.E.2d 119 (1960).

Court held this to be sufficient compliance with the statute that required a signature and designation of the trustee. Accordingly, the entruster's interest was superior to that of the assignee of the trustee for the benefit of creditors. As the Court mentioned, the Uniform Commercial Code (although not involved because the transaction occurred in 1957) expressly provides that minor discrepancies will not invalidate a security interest unless "seriously misleading." [3] This was certainly not such a discrepancy.

§6.6. Banking: General. In the business world, self-regulations that are affected by changing price levels are often related to indices of some type. Escalator clauses in contracts may provide for automatic increases in dollar amounts if certain costs should rise; labor agreements providing for wage scales that vary with price indices are not uncommon. Statutory regulations, however, more often depend upon piecemeal attempts to deal with problems caused by continued inflation. During the 1960 SURVEY year, there has been a fairly large amount of such legislation concerning banking.

Banking legislation generally contains many restrictions on investments and loans expressed in terms of dollar amounts. Limits that might have been quite adequate in an earlier day hamper banking practices as price levels change; in the absence of flexible formulas geared to price indices, badly needed changes are made by the legislature on an ad hoc basis from time to time. The current legislation of this type will be summarized in the following subsections. However, in view of the highly specialized interest in this type of legislation, no attempt will be made to analyze the changes in detail or to present the entire scheme of banking regulation through these isolated changes.

§6.7. Banking: Loans and investments. The maximum amount of personal, unsecured loans that credit unions may make to their own members on unindorsed notes has been increased from $300 to $500; the permissible amount on a note indorsed by a responsible person has been increased from $500 to $750.[1] Personal loans made by savings banks on the notes of the borrowers may now range to $1500, with thirty-six months permissible for repayment.[2] The prior maximum was $1000, with thirty months for repayment.

Cooperative banks are now allowed to make mortgage loans exceeding $20,000 each until the aggregate of such loans equals 20 percent of the deposits of the corporation.[3] Formerly, the aggregate amount of these loans could not exceed 5 percent of deposits. These increases in dollar limitations all recognize the inadequacies of the prior limits during a long period of climbing prices.

A greater freedom has been given to savings banks to enter into par-

[3] G.L., c. 106, §9-402(5).

§6.7. [1] Acts of 1960, c. 151, amending G.L., c. 171, §24(A).
[2] Acts of 1960, c. 272, amending G.L., c. 168, §37.
[3] Acts of 1960, c. 54, amending G.L., c. 170, §24.

ticipation loans with other banks,[4] and to trust companies, savings banks, and cooperative banks to participate in loans insured by the Federal Housing Administration.[5] Geographical boundaries have been extended for a limited number of credit unions, as they may now make mortgage loans on realty outside of the Commonwealth, provided that it is within a radius of fifteen miles of the office of the credit union.[6] Finally, a liberalization of the portfolio of cooperative banks has been provided by raising the percentage of assets that may be invested in stock and obligations of the Federal Home Loan Bank from 3 to 5 percent, divided into 3 percent for stock and 2 percent for obligations.[7]

§6.8. Banking: Borrowings and deposits. The maximum shares or deposits that members of small credit unions may have is $4000, and may reach $5000 with interest and dividends. With large credit unions (those having assets of at least $200,000) the limit for members with joint accounts is $8000, and may rise to $10,000. It is now permissible for fraternal organizations, voluntary associations, partnerships, and corporations to have the higher limit in the larger credit unions without the necessity for joint accounts.[1]

Cooperative banks and credit unions are now authorized to make loans to depositors against deposits to the end of the dividend period, but are restricted to a premium of not over 1 percent.[2] Depositors who wish to make withdrawals when the end of a dividend period is close at hand may thus salvage some of the dividends that would be lost by a premature withdrawal. Credit unions themselves, which normally need approval of the Commissioner of Banks to borrow money, are now authorized to borrow against their own deposits in other banks to the end of the dividend period without special approval.[3]

§6.9. Banking: Miscellaneous. In addition to the changes demanded by the economics of inflation, a number of miscellaneous revisions in banking legislation have been enacted. The minimum reserve requirements for cooperative banks (to meet withdrawals, loans, and payment of taxes received from mortgagors) has been reduced from 12½ to 10 percent of share liabilities.[1] The State Treasurer is now authorized to make deposits in cooperative banks;[2] in the past, only national banks, trust companies, and banking companies have been authorized as depositories of public funds. Persons obligated

4 Acts of 1960, c. 256, amending G.L., c. 168, §35; Acts of 1960, c. 257, amending G.L., c. 168, §38.
5 Acts of 1960, c. 422, amending G.L., c. 167, §51.
6 Acts of 1960, c. 57, amending G.L., c. 171, §24.
7 Acts of 1960, c. 111, amending G.L., c. 170, §26.

§6.8. 1 Acts of 1960, c. 162, amending G.L., c. 171, §10.
2 Acts of 1960, c. 24, adding G.L., c. 170, §25A, and c. 171, §24A, par. 7.
3 Acts of 1960, c. 60, amending G.L., c. 171, §16.

§6.9. 1 Acts of 1960, c. 195, amending G.L., c. 170, §40.
2 Acts of 1960, c. 230, adding G.L., c. 29, §34A.

to make payments to cooperative banks under mortgages are now required to become members of the corporation, whether they are original borrowers or subsequent owners of the mortgaged premises.[3] The effect of this would seem to be that such persons will have to subscribe for at least one share valued at $200.

All types of banking institutions subject to the supervision of the Commissioner of Banking are subject to a penalty of $5 per day for failure to file required reports or to make required amendments. This penalty has now been removed if the failure is "due to justifiable cause and not to wilful neglect."[4] The time for filing of annual reports by credit unions has been extended from twenty to thirty days after the last business day in June.[5] At the same time, the time for filing of such reports by savings banks has been contracted from thirty to fifteen days after the last business day in October.[6]

Finally, credit unions have received statutory approval for investment of funds for alteration, improvements or additions to buildings, whether owned or leased.[7] In the past, investment of funds had been specifically allowed only for the purchase or erection of buildings.

§6.10. Sales warranties: Allergic reactions. The quality of goods which a peculiarly sensitive purchaser has a right to expect, analyzed exhaustively in the 1958 ANNUAL SURVEY,[1] has again come before the scrutiny of the Supreme Judicial Court. The plaintiff in *Casagrande v. F. W. Woolworth Co.*,[2] who had used Mum deodorant for about twenty years without ill effect, finally developed dermatitis after the use of a jar of Mum purchased from the defendant. The Court recognized the existence of a warranty of merchantability but held that the fact that the purchaser was injured by use of the product was not enough to show that the warranty had been breached. A purchaser has no right to expect that a product will not be harmful to him unless it would harm a significant number of people. This, the Court held, the plaintiff had not proven.

The quality that a purchaser may expect — that the product would not harm a significant number of persons — follows the same test developed in several recent tort cases.[3] The difficulty in the *Casagrande* case was not one of a proper test but of sufficient proof. In the tort case of *Taylor v. Newcomb Baking Co.*,[4] testimony by an injured plaintiff's physician that "quite a percentage of people" would be irritated by a certain soap powder that was furnished by an employer

[3] Acts of 1960, c. 122, adding G.L., c. 170, §24.
[4] Acts of 1960, c. 58, amending G.L., c. 167, §7.
[5] Acts of 1960, c. 53, amending G.L., c. 171, §27.
[6] Acts of 1960, c. 58, amending G.L., c. 168, §65.
[7] Acts of 1960, c. 25, amending G.L., c. 171, §21.

§6.10. [1] Section 7.3.
[2] 340 Mass. 552, 165 N.E.2d 109 (1960); case also noted in §21.3 *infra*.
[3] Carter v. Yardley & Co., 319 Mass. 92, 64 N.E.2d 693 (1946); Taylor v. Newcomb Baking Co., 317 Mass. 609, 59 N.E.2d 293 (1945).
[4] 317 Mass. 609, 59 N.E.2d 293 (1945).

without also furnishing rubber gloves was enough to warrant submission of the facts to the jury. In the *Casagrande* case, the plaintiff's dermatologist testified that he could not tell whether anyone else in the United States would have the adverse effects. Furthermore, if the plaintiff was aided by any presumptions, the Court held that "they disappeared in the light of the defendant's evidence which tended to show that the deodorant and its components were not significant irritants." [5]

§6.11. Sales warranties: Damages. In the leading tort case of *Spade v. Lynn & Boston R.R.*,[1] decided in 1897, the Court held that there can be no recovery for physical injuries caused solely by mental disturbance, in the absence of injury from without. By 1939, this doctrine was introduced into sales warranties in *Wheeler v. Balestri*,[2] in which the Court held that although a loaf of bread containing a cockroach was unmerchantable, only nominal damages for breach of warranty could be recovered despite the fact that physical injury was sustained. Unfortunately for the plaintiff, her upset stomach came from the emotional shock of seeing the cockroach, not from eating it.

In 1956, in a case involving an ear of corn containing a worm, the plaintiff testified that she actually swallowed half of the worm.[3] Whether she had done so, however, was disputed, and the Court did not have to decide whether this would have been enough to raise an exception to the rule in the *Spade* case.

During the 1960 SURVEY year, the Court did have the occasion to consider the effect of an actual ingestion of a foreign substance which caused a physical reaction through emotional shock rather than through chemical or physical reaction. *Sullivan v. H. P. Hood & Sons, Inc.*,[4] involved the purchaser of a container of milk, who discovered, after drinking some of the milk, that the carton contained a dead mouse and that she had swallowed some of the mouse's fecal matter. The plaintiff's physical injuries included a rash, sores, itching, and nausea. The case was presented through the findings of an auditor, and the Court concluded that since these findings would require a conclusion that the plaintiff's injuries were caused by the severe emotional shock of realizing what she had swallowed rather than from any deleterious effect of the fecal matter itself, the *Spade* case requirement of injury from without had not been met. The Court refused to find that the ingestion constituted a battery, sufficient to distinguish it from the *Spade* case.

The result of this was twofold: first, the dairy was not liable in tort; second, the dealer, who was liable for breach of warranty of merchantability, was liable only for nominal damages. Since damages are an

[5] 1960 Mass. Adv. Sh. 413, 416, 165 N.E.2d 109, 112.

§6.11. [1] 168 Mass. 285, 47 N.E. 88 (1897).
[2] 304 Mass. 257, 23 N.E.2d 132 (1939).
[3] Kennedy v. Brockelman Brothers, Inc., 334 Mass. 225, 134 N.E.2d 747 (1956).
[4] 1960 Mass. Adv. Sh. 927, 168 N.E.2d 80; case also noted in §3.4 *supra*.

element of the wrong in tort, there may be some justification for holding that without some "damage" through an injury from without, there is no tort to which consequential damage from emotional shock may be added. In simpler language, a person may be as careless as he likes, but he commits no tort without injury to another. The action for breach of warranty, however, sounds in contract, and the plaintiff stands in a very specific relationship to the defendant. The sale of milk included an implied warranty of merchantability. Milk containing a dead mouse and its fecal matter is not merchantable. By allowing nominal damages, the Court, in fact, recognized the existence of a cause of action by the purchaser for breach of warranty. It would seem that the addition of consequential damages might not have been unjustified.

§6.12. Sales warranties: Disclaimers. The sales of many types of consumer goods are accompanied by express warranties by the manufacturer which are widely promoted as inducements to the ultimate consumer. Not so well publicized, however, are the disclaimers which purport to deny the existence of any warranties that may have been implied by law, whether by the manufacturer or dealer. Furthermore, even if a particular purchaser is aware of the effect of the disclaimer, he may be in no position to bargain for any different warranty than that included in the standard contract. The situation becomes particularly difficult with respect to the purchase of new automobiles. Since dealers in automobiles generally must comply with the manufacturer's wishes if they intend to retain their dealership, the manufacturers can make it virtually impossible for anyone to purchase a new automobile without an express warranty and its companion, the disclaimer of any other warranty. This the manufacturers have done, through their association.

The Supreme Court of New Jersey, in a very comprehensive opinion analyzing this practice in great detail, has said: "But the ingenuity of the Automobile Manufacturers Association, by means of its standardized form, has metamorphosed the warranty into a device to limit the maker's liability. To call it an 'equivocal' agreement, as the Minnesota Supreme Court did, is the least that can be said in criticism of it." [1] A thorough examination of the marketing process led the New Jersey court to conclude not only that the attempt of the manufacturer to limit its liability was "so inimical to the public good as to compel an adjudication of its invalidity," [2] but also "that the disclaimer of an implied warranty of merchantability by the dealer, as well as the attempted elimination of all obligations other than replacement of defective parts, are violative of public policy and void." [3]

The plaintiff in *Hall v. Everett Motors, Inc.*,[4] decided in this Com-

§6.12. [1] Henningson v. Bloomfield Motors, Inc., 32 N.J. 358, 375, 161 A.2d 69, 78 (1960).

[2] 32 N.J. at 404, 161 A.2d at 95.

[3] 32 N.J. at 408, 161 A.2d at 97.

[4] 340 Mass. 430, 165 N.E.2d 107 (1960).

monwealth, was not so fortunate as the plaintiff in the New Jersey case. Although he received the sympathy of the Supreme Judicial Court, and might have been comforted by the expressed hope that the Court might be able to decide otherwise in cases arising under the Uniform Commercial Code, the plaintiff was not able to recover from the dealer for the value of his automobile, which was destroyed by fire caused by a wiring defect that the dealer had twice tried to correct.

Although an automobile with wiring so defective as to cause a fire is certainly not merchantable, the Court felt that the purchaser's only recourse, if any, was on the manufacturer's express warranty (which the purchaser testified to having accepted), since that warranty expressly excluded all other warranties made by either the dealer or the manufacturer. The plaintiff apparently did not attempt to recover from the manufacturer directly on the express warranty, although the current trend of opinion seems to be that the manufacturer is a party to the agreement, liable at least on his express statements.[5]

Whether the Uniform Commercial Code will require that the Court decide differently is at least doubtful. The standard express warranty contains limitations that might be considered unreasonable, and therefore inoperative under Section 2-316(1), in so far as they limit recovery to the replacement of defective parts returned, with transportation charges prepaid to the factory.

However, the dealer in the *Hall* case seems to have made no express warranty whatsoever. Furthermore, the Code definitely permits the exclusion of all implied warranties, without regard to reasonableness. There is, however, the possibility that the disclaimer itself may be found to be "unconscionable," especially in view of its commercial setting. If it is so found, the Code gives specific authority for disregarding it.[6] At least, it will not be necessary to decide, as it was for the New Jersey court, that the disclaimer is so inimical to the public good as to be void.

[5] See, e.g., Pelletier v. Brown Brothers Chevrolet, 164 N.Y.S.2d 249 (Sup. Ct. 1956).
[6] G.L., c. 106, §2-302.