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## Commercial Transactions

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## COMMERCIAL TRANSACTIONS

ROBERT W. FOSTER\*

[As stated in the 1963 Survey Issue, "Commercial Transactions" will cover the legal developments relating to the process of the distribution of personal property. This broad area is divided into sales, chattel security, and commercial paper as the principal facets of a commercial transaction.]

*Sales*

In *American Cast Iron Pipe Co. v. McKoy-Helgerson Co.*<sup>1</sup> the federal court had before it the construction and application of a clause appearing on the reverse side of the seller's price quotation letter stating that liability for defective material is limited to the contract price. Subsequently the buyer's purchase order form was accepted by the seller. In reading all of the documents together, the court concluded as a matter of law that the limitation of damage clause was an effective part of the contract and thus precluded the buyer from recovering consequential damages resulting from the breach.

As a general rule, a buyer may recover consequential damages arising out of breach of a sales contract provided the damages were foreseeable.<sup>2</sup> As an application of the principle of freedom of contract, it is clear that the seller may expressly disclaim or limit normal contract liabilities,<sup>3</sup> provided it is not done by unexpected and unbargained for language.<sup>4</sup> To prevent an unconscionable imposition of limitation of liability, under some circumstances, the court may require that the limiting clause be brought to the attention of the buyer in order to be effective.<sup>5</sup> Where both

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1. 226 F. Supp. 842 (W.D.S.C. 1963), *aff'd*, 329 F.2d 152 (4th Cir. 1964).

2. *E.g.*, *Georgetown Towing Co. v. National Supply*, 204 S.C. 445, 29 S.E.2d 765 (1944); *Liquid Carbonic Co. v. Conklin*, 166 S.C. 400, 164 S.E. 895 (1932). See UNIFORM COMMERCIAL CODE § 2-715.

3. *Sanders v. Allis-Chalmers Mfg. Co.*, 237 S.C. 133, 115 S.E.2d 793 (1960); *R.C.A. Photophone Co. v. Carroll*, 174 S.C. 183, 177 S.E. 23 (1934); *Deiter v. Frick Co.*, 169 S.C. 480, 169 S.E. 297 (1933); *Westinghouse Elec. & Mfg. Co. v. Glencoe Cotton Mills*, 105 S.C. 133, 90 S.E. 526 (1916). See UNIFORM COMMERCIAL CODE § 2-719(1)(a), approving contractual modification or limitation of remedies except that limitation of consequential damages for injury to person in the case of consumer goods is "*prima facie* unconscionable."

4. *Durent v. Palmetto Chevrolet Co.*, 241 S.C. 508, 129 S.E.2d 323 (1963).

5. *Ibid.* See also *Reliance Varnish Co. v. Mullins Lumber Co.*, 213 S.C. 84, 48 S.E.2d 653 (1948); *Stevenson v. Kirkland Seed Co.*, 175 S.C. 345, 180 S.E. 197 (1935).

parties to the sales contract are businessmen, as in the *American Cast Iron Pipe Co.* case, there is less need and less likelihood that the court will encroach on the principle of freedom of contract in order to prevent unconscionable terms.

*Lynch v. United States Branch, Gen. Acc. Fire & Life Assur. Corp.*,<sup>6</sup> an action in the federal court to determine liability between two insurance companies, one a liability insurer of an automobile dealer and the other a liability insurer of the buyer of a car, is discussed in the survey of insurance. The outcome in this case turned on the construction of the term "owned" used in the buyer's policy as prescribing his insurer's liability. As an indirect precedent of commercial transactions law relating to the time of effective transfer of ownership in a car, it is significant that the court concluded that the buyer became the owner when he took possession of the car after executing a conditional sales contract to secure the balance of the purchase price, even though a certificate of title had not been issued to him. The reserved legal title in the seller was only a security interest while the equitable title and ownership passed upon delivery of the car to the buyer. The South Carolina Motor Vehicle Title Act,<sup>7</sup> providing that a transfer by an owner is not effective until its provisions have been complied with, did not apply to this case under the proviso in the act, "except—as between the parties."

### *Chattel Security*

The foreclosure procedure after default under a conditional sales contract covering a truck was challenged in *Castell v. Stephenson Fin. Co.*<sup>8</sup> The mortgagor claimed conversion of the truck by the secured party in offering it at public sale without proper notice and by bidding it in at an unconscionably low price. After concluding that the debtor was in default when the secured party took possession and that the statutory requirements of a public sale were complied with,<sup>9</sup> the court held that the mere fact that a sale by the mortgagee results in the property bringing less than its value would not constitute a conversion.<sup>10</sup>

6. 327 F.2d 328 (4th Cir. 1964).

7. S.C. CODE ANN. § 46-150.15 (1962).

8. 244 S.C. 45, 135 S.E.2d 311 (1964).

9. S.C. CODE ANN. § 45-164 (1962).

10. For a general discussion of policy regarding judicial supervision of collateral liquidation sale, see Foster, *Commercial Transactions*, 16 S.C.L. REV. 29, 34 (1963).

In *Layton v. Flowers*<sup>11</sup> the court was asked to overrule the case of *Tate v. Brazier*<sup>12</sup> holding that the statutory lien on a motor vehicle for damages resulting from its negligent operation is superior to the claim of a subsequent *bona fide* purchaser for value without notice.<sup>13</sup> While the court seems to suggest sympathy for the innocent purchaser, especially since the lien holder waited some six months before asserting his lien, it nevertheless felt that it would "exceed the bounds of proper judicial restraint to overturn a construction which has had implied legislative sanction . . ."<sup>14</sup> by opportunity and failure to amend over a long period of time. The court took some of the sting out of this rule, however, by holding that the lien creditor was estopped from asserting his interest beyond the value of the car immediately following the collision. The increased value resulting from extensive repairs during the six months of inaction by the lienor inured to the benefit of the purchaser. On this latter point, it is not clear whether the court will limit its application to the facts of the instant case where the lienor delayed in asserting his claim thus working an estoppel against him, or whether the statutory lien shall be limited to the value of the car immediately following the collision in all events.

### *Commercial Paper*

*Singletary & Son, Inc. v. Lake City State Bank*<sup>15</sup> involved the factual pattern of the fraudulent employee who, not having authority to draw checks, submits a list of names of fictitious persons to his employer who, believing them to be entitled to payment, makes checks to their order. The fraudulent employee then takes the checks, indorses them in the name of the payee, and the drawee bank, recognizing the drawer's signature, pays them. In the instant case, the employer-depositor was allowed to recover the total amount of 14,879 dollars which the bank had debited against its account on these checks over a period of sev-

11. 243 S.C. 421, 134 S.E.2d 247 (1964).

12. 115 S.C. 283, 104 S.E. 413 (1920).

13. S.C. CODE ANN. §45-551 (1962). See also *Merchants & Planters Bank v. Brigman*, 106 S.C. 362, 91 S.E. 332 (1916), where the court held that the statute creating the "collision lien" was notice to all the world and thus a subsequent chattel mortgagee of a car subject to such lien takes with constructive notice thereof.

14. *Layton v. Flowers*, 243 S.C. 421, 424, 134 S.E.2d 247, 248 (1964). See *Powers v. Powers*, 239 S.C. 423, 123 S.E.2d 646 (1962); *Alexander v. Honeycutt*, 196 S.C. 364, 13 S.E.2d 630 (1941).

15. 243 S.C. 180, 133 S.E.2d 118 (1963).

eral years. The principal basis of the decision upholding the “loan-receipt” device, whereby the plaintiff was paid its losses by its surety company as a “loan” to be repaid if recovery was had against the bank, is discussed in the survey of insurance.

The commercial paper aspects of the case involve the bank’s liability to its depositor under these facts which the court seems to have assumed for the purposes of this appeal. The conventional analysis of this problem turns on the determination of whether the check is bearer or order paper. Under the Negotiable Instruments Law, an instrument is payable to bearer when payable to a “fictitious or non-existing person and such fact was known to the person making it.”<sup>16</sup> The latter phrase is generally construed to mean that the intent of the drawer governs. A check is bearer if the drawer does not intend the named payee to receive the beneficial interest; it is order if the drawer does so intend even though the payee may be fictitious or non-existent.<sup>17</sup> All of the prior South Carolina cases dealing with the application of this principle have involved the factual pattern of the fraudulent employee having authority to sign for his employer: the employee makes checks payable to fictitious persons or other employees, signs their name as an indorsement, and cashes the check at the bank where the employer maintained an account. In those cases it has been held that it was the intention of the drawer—the fraudulent employee—that the named payees not receive the beneficial interest and thus the check was bearer. Since bearer paper is negotiated by physical delivery alone, the forged indorsements are immaterial and the bank may properly debit the drawer’s account.

In the *Singletary* case, the employer-drawer intended the named payee to receive the beneficial interest. Under the analysis of the negotiable instruments law which makes the drawer’s intent decisive, the check would therefore be order paper. Since an indorsement is necessary to transfer interest in an order instrument, the forgery of the payee’s name would pass no right to receive payment and thus the payee bank could not debit the drawer’s account in the amount so paid. While there are no South Carolina cases directly in point, this is the usual conclusion

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16. S.C. CODE ANN. § 8-820(3) (1962).

17. *Southern Frozen Foods, Inc. v. Hale*, 241 S.C. 524, 129 S.E.2d 420 (1963); *Bourne v. Maryland Cas. Co.*, 185 S.C. 1, 192 S.E. 605 (1937); *Ellis Weaving Mills v. Citizens & So. Nat’l Bank*, 91 F. Supp. 943 (W.D.S.C. 1950), *aff’d*, 184 F.2d 43 (4th Cir. 1950).

reached in other jurisdictions where the matter has arisen<sup>18</sup> and may have been assumed by the court in the instant case.

Aside from this conceptual analysis, when the problem is viewed simply as a matter of visiting loss on either the drawee-bank or on the employer whose employee caused the loss, the conclusion that the bank may not debit the drawer's account is difficult to defend. Presumably, as a reaction against placing the loss on the drawee bank in either of the fraudulent employee patterns, the 1964 session of the General Assembly of South Carolina adopted the American Bankers Association's recommendation of amending the present statute by adding to the definition of an order instrument in section 8-820(3) of the South Carolina Code, 1962, the clause: "or known to his employee or other agent who supplies the name of such payee."

The proposed Uniform Commercial Code would place the loss on the employer whose faithless employee caused the loss, not through the bearer-order analysis, but by the direct provision that "an endorsement by any person in the name of a named payee is effective if an agent or employee of the maker or drawer has supplied him with the name of the payee intending the latter to have no such interest."<sup>19</sup>

In *Burns v. Prudence Life Ins. Co.*<sup>20</sup> (commented on in the survey of insurance) a subsequently dishonored check given to reinstate a lapsed life insurance policy, was held not to be effective under the usual presumption that a check is payment only on condition that it be paid.<sup>21</sup> The court recognized that the presumption may be rebutted by an expressed or implied agreement between the parties that the check would be absolute payment leaving only an action on the check to collect the debt. Even though the defendant had issued to the insured its receipt, this was not sufficient to establish the intent of unconditional payment in light of the fact that the insurer notified the insured who acknowledged his application for reinstatement that the policy had lapsed after issuance of the receipt.

The giving of an unconditional receipt stating that the premium has been paid is usually treated as at least a factor tending

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18. *E.g.*, *Robertson Banking Co. v. Brasfield*, 202 Ala. 167, 79 So. 651 (1918); *Commonwealth to use of Coleman v. Farmers Deposit Bank*, 264 Ky. 839, 95 S.W.2d 793 (1936).

19. UNIFORM COMMERCIAL CODE § 3-405(c).

20. 243 S.C. 515, 134 S.E.2d 769 (1964).

21. *Atlantic Life Ins. Co. v. Barringer*, 175 S.C. 145, 178 S.E. 505 (1934); *Holladay v. South Carolina Power Co.*, 169 S.C. 241, 168 S.E. 691 (1932).

to show an intent that the check was accepted unconditionally in satisfaction of the premium.<sup>22</sup> The fact in the instant case that the insured acknowledged in the reinstatement application that the policy had lapsed for non-payment of the premium had the effect of eliminating any inference whereby the jury would be justified in finding an intention of unconditional acceptance of the check.

A novel aspect of the tender of payment problem to prevent the lapse of an automobile liability insurance policy appeared in *Surety Indemnity Co. v. Estes*<sup>23</sup> (also commented on in the survey of insurance). A premium check was dishonored for insufficient funds when presented by the insurer prior to the expiration of the grace period within which the premium could be paid to keep the policy in force. Subsequently the insured restored the account to an amount sufficient to cover the check. Since the insurer was in possession of the check which it could have collected from the bank before the expiration of the grace period, this constituted a tender of payments sufficient to prevent forfeiture.

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22. *National Life Co. v. Brennecke*, 195 Ark. 1088, 115 S.W.2d 185 (1938); *Martin v. New York Ins. Co.*, 33 N.M. 617, 273 Pac. 1916 (1928).

23. 243 S.C. 593, 135 S.E.2d 226 (1964).