CHAPTER

10

ASSIGNMENT AND DELEGATION

I. TERMINOLOGY

In a bilateral executory contract each party is owed a performance obligation — a contract *right* — and each owes or will owe a performance obligation — a contract *duty*. Let us assume that Betty's Food Mart has promised to buy 4,000 boxcars of bananas for $400,000 and Sammy's Produce has promised to sell the bananas to Betty. Betty has a right to Sammy's performance — delivery of the bananas — and Sammy has a right to Betty's performance — purchase of the bananas. Betty owes a duty to pay for the bananas upon proper delivery and Sammy owes a duty to deliver the bananas. These rights and duties are transferable to others, and this chapter concerns such an *assignment of rights* and a *delegation of duties.*

We begin with the proper terminology. Contract *rights* are *assigned*, and contract *duties* are *delegated.* These are words of art and must not be used interchangeably. In an assignment, the person making the assignment (who will be one of the original contracting parties) is called the *assignor.* The person to whom the assignment is made (who will be a stranger to the original contract) is called the *assignee.* The original contracting party whose obligation is assigned is the *obligor.*

In a delegation of duties, the same parties are known as the *delegator*, the *delegatee*, and the *obligee.*

Problem 181

Joseph Armstrong went down to Wonder Spa and signed a contract agreeing to pay the spa $1,000 in return for the use of its facilities for a two-year period. A week later the Nightflyer Finance Company sent him a payment booklet, stating that the contract he had signed with the spa had been purchased by Nightflyer. Label the three parties to this transaction using the above terminology.

Problem 182

After Armstrong had worked out at the spa for six months, it changed ownership. The new owners agreed with the old owners to honor all existing contracts with the spa's customers. Label the parties to this transaction.

II. VALIDITY OF THE ASSIGNMENT/DELEGATION

A. *Performance Obligations*

MACKE CO. v. PIZZA OF GAITHERSBURG, INC.
Court of Appeals of Maryland, 1970
259 Md. 479, 270 A.2d 645

SINGLEY, J. The appellees and defendants below, Pizza of Gaithersburg, Inc.; Pizzeria, Inc.; The Pizza Pie Corp., Inc. and Pizza Oven, Inc., four corporations under the common ownership of Sidney Ansell, Thomas S. Sherwood and Eugene Early and the same individuals as partners or proprietors (the Pizza Shops) operated at six locations in Montgomery and Prince George's Counties. The appellees had arranged to have installed in each of their locations cold drink vending machines owned by Virginia Coffee Service, Inc., and on 30 December 1966, this arrangement was formalized at five of the locations, by contracts for terms of one year, automatically renewable for a like term in the absence of 30 days' written notice. A similar contract for the sixth location, operated by Pizza of Gaithersburg, Inc., was entered into on 25 July 1967.

On 30 December 1967, Virginia's assets were purchased by The Macke Company (Macke) and the six contracts were assigned to Macke by Virginia. In January, 1968, the Pizza Shops attempted to terminate the five contracts having the December anniversary date, and in February, the contract which had the July anniversary date.

Macke brought suit in the Circuit Court for Montgomery County against each of the Pizza Shops for damages for breach of contract. From judgments for the defendants, Macke has appealed.

The lower court based the result which it reached on two grounds: first, that the Pizza Shops, when they contracted with Virginia, relied on its skill, judgment and reputation, which made impossible a delegation of Virginia's duties to Macke; and second, that the damages claimed could not be shown with reasonable certainty. These conclusions are challenged by Macke.

In the absence of a contrary provision — and there was none here — rights and duties under an executory bilateral contract may be assigned and delegated, subject to the exception that duties under a contract to provide personal services may never be delegated, nor rights be assigned under a contract where delectus personae was an ingredient of the bargain. 4 Corbin on Contracts §865 (1951) at 434; 6 Am. Jur. 2d, Assignments §11 (1963) at 196. Crane Ice Cream Co. v. Terminal Freezing & Heating Co., 147 Md. 588, 128 A. 280 (1925) held that the right of an individual to purchase ice under a contract which by its terms reflected a knowledge of the individual's needs and reliance on his credit and responsibility could not be assigned to the corporation which purchased his business. In Eastern Advertising Co. v. McGaw & Co., 89 Md. 72, 42 A. 923 (1899), our predecessors held that an advertising agency could not delegate its duties under a contract which had been entered into by an advertiser who had relied on the agency's skill, judgment and taste.

The six machines were placed on the appellees' premises under a printed "Agreement-Contract" which identified the "customer," gave its place of business, described the vending machine, and then provided:

Terms

1. The Company will install on the Customer's premises the above listed equipment and will maintain the equipment in good operating order and stocked with merchandise.
2. The location of this equipment will be such as to permit accessibility to persons desiring use of same. This equipment shall remain the property of the Company and shall not be moved from the location at which installed, except by the Company.
3. For equipment requiring electricity and water, the Customer is responsible for electrical receptacle and water outlet within ten (10) feet of the equipment location. The Customer is also responsible to supply the Electrical Power and Water needed.
4. The Customer will exercise every effort to protect this equipment from abuse or damage.
5. The Company will be responsible for all licenses and taxes on the equipment and sale of products.
6. This Agreement-Contract is for a term of one (1) year from the date indicated herein and will be automatically renewed for a like period, unless thirty (30) day written notice is given by either party to terminate service.
7. Commission on monthly sales will be paid by the Company to the customer at the following rate:. . .

The rate provided in each of the agreements was "30% of Gross Receipts to $300.00 monthly [,] 35% over [$]300.00," except for the agreement with Pizza of Gaithersburg, Inc., which called for "40% of Gross Receipts."

We cannot regard the agreements as contracts for personal services. They were either a license or concession granted Virginia by the appellees, or a lease of a portion of the appellees' premises, with Virginia agreeing to pay a percentage of gross sales as a license or concession fee or as rent, see Charlotte Coca-Cola Bottling Co. v. Shaw, 232 N.C. 307, 59 S.E.2d 819 (1950) and Herbert's Laurel-Ventura, Inc. v. Laurel Ventura Holding Corp., 58 Cal. App. 2d 684, 138 P.2d 43, 46-47 (1943), and were assignable by Virginia unless they imposed on Virginia duties of a personal or unique character which could not be delegated, S&L Vending Corp. v. 52 Thompkins Ave. Restaurant, Inc., 26 A.D.2d 935, 274 N.Y.S.2d 697 (1966).

The appellees earnestly argue that they had dealt with Macke before and had chosen Virginia because they preferred the way it conducted its business. Specifically, they say that service was more personalized, since the president of Virginia kept the machines in working order, that commissions were paid in cash, and that Virginia permitted them to keep keys to the machines so that minor adjustments could be made when needed. Even if we assume all this to be true, the agreements with Virginia were silent as to the details of the working arrangements and contained only a provision requiring Virginia to "install . . . the above listed equipment and . . . maintain the equipment in good operating order and stocked with merchandise." We think the Supreme Court of California put the problem of personal service in proper focus a century ago when it upheld the assignment of a contract to grade a San Francisco street:

> All painters do not paint portraits like Sir Joshua Reynolds, nor landscapes like Claude Lorraine, nor do all writers write dramas like Shakespeare or fiction like Dickens. Rare genius and extraordinary skill are not transferable, and contracts for their employment are therefore personal, and cannot be assigned. But rare genius and extraordinary skill are not indispensable to the workmanlike digging down of a sand hill or the filling up of a depression to a given level, or the construction of brick sewers with manholes and covers, and contracts for such work are not personal, and may be assigned. Taylor v. Palmer, 31 Cal. 240 at 247-248 (1866).

See also Devlin v. Mayor, Aldermen and Commonalty of the City of New York, 63 N.Y. 8, at 17 (1875). Moreover, the difference between the service the Pizza Shops happened to be getting from Virginia and what they expected to get from Macke did not mount up to such a material change in the performance of obligations under the agreements as would justify the appellees' refusal to recognize the assignment, Crane Ice Cream Co. v. Terminal Freezing & Heating Co., supra, 147 Md. 588, 128 A. 280.

In support of the proposition that the agreements were for personal services, and not assignable, the Pizza Shops rely on three Supreme Court cases, Burck v. Taylor, 152 U.S. 634 (1894); Delaware County Commr. v. Diebold Safe & Lock Co., 133 U.S. 473 (1890); and Arkansas Valley Smelting Co. v. Belden Mining Co., 127 U.S. 379 (1888), all of which were cited with approval by our predecessors in Tarr v. Veasey, 125 Md. 199, 207, 93 A. 428 (1915). We find none of these cases persuasive. *Burck* held that the contractor for the state capitol in Texas, who was prohibited by the terms of his contract from assigning it without the state's consent, could not make a valid assignment of his right to receive three-fourths of the proceeds. In *Delaware County*, Diebold Safe and Lock, which was a subcontractor in the construction of a county jail, was barred from recovering from the county commissioners for its work on the theory that there had been a partial assignment of the construction contract by the prime contractor, which had never been assented to by the commissioners. This result must be limited to the facts: i.e., to the subcontractor's right to recover under the assignment, and not to the contractor's right to delegate. See Taylor v. Palmer and Devlin v. Mayor, Aldermen and Commonalty of the City of New York, both supra. *Arkansas Valley*, which held invalid an attempt to assign a contract for the purchase of ore, is clearly distinguishable, because of a contract provision which stipulated that payment for the ore was to be made after delivery, based on an assay to be made by the individual purchaser named in the contract. The court concluded that this was a confidence imposed in the individual purchaser's credit and responsibility and that his rights under the contract could not be transferred to another. Tarr v. Veasey involved a situation where duties were delegated to one person and rights assigned to another and our predecessors held the rights not to be assignable, because of the parties' intention that duties and rights were interdependent.

We find more apposite two cases which were not cited by the parties. In The British Waggon Co. & The Parkgate Waggon Co. v. Lea & Co., 5 Q.B.D. 149 (1880), Parkgate Waggon Company, a lessor of railway cars, who had agreed to keep the cars "in good and substantial repair and working order," made an assignment of the contract to British Waggon Company. When British Waggon Company sued for rent, the lessee contended that the assignment had terminated the lease. The court held that the lessee remained bound under the lease, because there was no provision making performance of the lessor's duty to keep in repair a duty personal to it or its employees.

Except for the fact that the result has been roundly criticized, see Corbin, supra, at 448-449, the Pizza Shops might have found some solace in the facts found in Boston Ice Co. v. Potter, 123 Mass. 28 (1877). There, Potter, who had dealt with the Boston Ice Company, and found its service unsatisfactory, transferred his business to Citizens' Ice Company. Later, Citizens' sold out to Boston, unbeknown to Potter, and Potter was served by Boston for a full year. When Boston attempted to collect its ice bill, the Massachusetts court sustained Potter's demurrer on the ground that there was no privity of contract, since Potter had a right to choose with whom he would deal and could not have another supplier thrust upon him. Modern authorities do not support this result, and hold that, absent provision to the contrary, a duty may be delegated, as distinguished from a right which can be assigned, and that the promisee cannot rescind, if the quality of the performance remains materially the same.

Restatement, Contracts §160(3) (1932) reads, in part:

> Performance or offer of performance by a person delegated has the same legal effect as performance or offer of performance by the person named in the contract, unless,
>
> (a) performance by the person delegated varies or would vary materially from performance by the person named in the contract as the one to perform, and there has been no . . . assent to the delegation. . . .

In cases involving the sale of goods, the Restatement rule respecting delegation of duties has been amplified by Uniform Commercial Code §2-210(5), Maryland Code (1957, 1964 Repl. Vol.) Art. 95B §2-210(5), which permits a promisee to demand assurances from the party to whom duties have been delegated. See also, "The Uniform Commercial Code and Contract Law: Some Selected Problems," 105 U. of Pa. L.R. 837, at 913-916 (1957); Noblett v. General Electric Credit Corp., 400 F.2d 442 (10th Cir. 1968), cert. denied 393 U.S. 935 (1968).

As we see it, the delegation of duty by Virginia to Macke was entirely permissible under the terms of the agreements. In so holding, we do not put ourselves at odds with Eastern Advertising Co. v. McGaw, supra, 89 Md. 72, 42 A. 923, for in that case, the agreement with the agency contained a provision that "the advertising cards were to be 'subject to the approval of Eastern Advertising Company as to style and contents,' " at 82, 42 A. at 923, which the court found to import that reliance was being placed on the agency's skill, judgment and taste, at 88, 42 A. 923. . . .

Judgment reversed as to liability; judgment entered for appellant for costs, on appeal and below; case remanded for a new trial on the question of damages.

QUESTION

Assume Macke had refused to provide the drink machines and the defendant had sued Virginia Coffee Service for breach. Would the delegation by Virginia be a defense to breach? Compare UCC §2-210(1).

The common law limitations of assignments and delegations are reflected in the Uniform Commercial Code. In the sale of goods, §2-210 is the relevant section. Read it and then resolve the following Problems.

Problem 183

Jay Eastriver promised to sell to Gerald Czeck all of the mufflers that Gerald needed to operate the Czech Muffler Shop for the years 2012 through 2014. Gerald decided to sell the shop to a corporation called Texas Auto and assigned to it his right to purchase the mufflers from Jay. Jay now refuses to sell any mufflers to Texas Auto, complaining that the contract was not assignable. Who wins? Does Jay have any intermediate recourse if he is unsure of how Texas Auto will perform? Read UCC §§2-210, 2-306, and 2-609. Can §2-306 be used as an argument for Jay? For Texas Auto? See Official Comment 4. Does it matter if Texas Auto requires more or fewer mufflers than Gerald would have?

B. *Payment Obligations*

Problem 184

Joseph Armstrong went down to Wonder Spa and signed a contract agreeing to pay the spa $1,000 in return for the use of its facilities for a two-year period. A week later the Nightflyer Finance Company sent him a notice that the contract he had signed with Wonder had been assigned to Nightflyer. Joseph read the notice but promptly forgot it and continued to pay Wonder, who pocketed the money. Wonder is bankrupt, and Nightflyer now insists that Joseph pay Nightflyer. Joseph told them they were crazy if they thought he was going to pay twice. Nightflyer has sued Joseph, and he has retained you. Does he owe the money or doesn't he? See UCC §9-406(a) and the case that follows this Problem. Could he validly claim that his payment obligation was too personal to be assigned?

HERZOG v. IRACE
Supreme Judicial Court of Maine, 1991
594 A.2d 1106

BRODY, Justice. Anthony Irace and Donald Lowry appeal from an order entered by the Superior Court (Cumberland County, Cole, J.) affirming a District Court (Portland, Goranites, J.) judgment in favor of Dr. John P. Herzog in an action for breach of an assignment to Dr. Herzog of personal injury settlement proceeds[1] collected by Irace and Lowry, both attorneys, on behalf of their client, Gary G. Jones. On appeal, Irace and Lowry contend that the District Court erred in finding that the assignment was valid and enforceable against them. They also argue that enforcement of the assignment interferes with their ethical obligations toward their client. Finding no error, we affirm.

The facts of this case are not disputed. Gary Jones was injured in a motorcycle accident and retained Irace and Lowry to represent him in a personal injury action. Soon thereafter, Jones dislocated his shoulder, twice, in incidents unrelated to the motorcycle accident. Dr. Herzog examined Jones's shoulder and concluded that he needed surgery. At the time, however, Jones was unable to pay for the surgery and in consideration for the performance of the surgery by the doctor, he signed a letter dated June 14, 1988, written on Dr. Herzog's letterhead stating:

> I, Gary Jones, request that payment be made directly from settlement of a claim currently pending for an unrelated incident, to John Herzog, D.O., for treatment of a shoulder injury which occurred at a different time.

Dr. Herzog notified Irace and Lowry that Jones had signed an "assignment of benefits" from the motorcycle personal injury action to cover the cost of surgery on his shoulder and was informed by an employee of Irace and Lowry that the assignment was sufficient to allow the firm to pay Dr. Herzog's bills at the conclusion of the case. Dr. Herzog performed the surgery and continued to treat Jones for approximately one year.

In May, 1989, Jones received a $20,000 settlement in the motorcycle personal injury action. He instructed Irace and Lowry not to disburse any

1. This case involves the assignment of proceeds from a personal injury action, not an assignment of the cause of action itself.

funds to Dr. Herzog indicating that he would make the payments himself. Irace and Lowry informed Dr. Herzog that Jones had revoked his permission to have the bill paid by them directly and indicated that they would follow Jones's directions. Irace and Lowry issued a check to Jones for $10,027 and disbursed the remaining funds to Jones's other creditors. Jones did send a check to Dr. Herzog but the check was returned by the bank for insufficient funds and Dr. Herzog was never paid.

Dr. Herzog filed a complaint in District Court against Irace and Lowry seeking to enforce the June 14, 1988 "assignment of benefits." The matter was tried before the court on the basis of a joint stipulation of facts. The court entered a judgment in favor of Dr. Herzog finding that the June 14, 1988 letter constituted a valid assignment of the settlement proceeds enforceable against Irace and Lowry. Following an unsuccessful appeal to the Superior Court, Irace and Lowry appealed to this court. Because the Superior Court acted as an intermediate appellate court, we review the District Court's decision directly. See Brown v. Corriveau, 576 A.2d 200, 201 (Me. 1990). . . .

Validity of Assignment

An assignment is an act or manifestation by the owner of a right (the assignor) indicating his intent to transfer that right to another person (the assignee). See Shiro v. Drew, 174 F. Supp. 495, 497 (D. Me. 1959). For an assignment to be valid and enforceable against the assignor's creditor (the obligor), the assignor must make clear his intent to relinquish the right to the assignee and must not retain any control over the right assigned or any power of revocation. Id. The assignment takes effect through the actions of the assignor and assignee and the obligor need not accept the assignment to render it valid. Palmer v. Palmer, 112 Me. 149, 153, 91 A. 281, 282 (1914). Once the obligor has notice of the assignment, the fund is "from that time forward impressed with a trust; it is . . . impounded in the [obligor's] hands, and must be held by him not for the original creditor the assignor, but for the substituted creditor, the assignee." Id. at 152, 91 A. 281. After receiving notice of the assignment, the obligor cannot lawfully pay the amount assigned either to the assignor or to his other creditors and if the obligor does make such a payment, he does so at his peril because the assignee may enforce his rights against the obligor directly. Id. at 153, 91 A. 281.

Ordinary rights, including future rights, are freely assignable unless the assignment would materially change the duty of the obligor, materially increase the burden or risk imposed upon the obligor by his contract impair the obligor's chance of obtaining return performance, or materially reduce the value of the return performance to the obligor, and unless the law restricts the assignability of the specific right involved. See Restatement (Second) Contracts §317(2)(a) (1982). In Maine, the transfer of a future right to *proceeds* from pending litigation has been recognized as a valid and enforceable equitable assignment. McLellan v. Walker, 2(Me. 114, 117-18 (1896). An equitable assignment need not transfer th entire future right but rather may be a partial assignment of that right. *Palmer,* 112 Me. at 152, 91 A. 281. We reaffirm these well established principles.

Relying primarily upon the Federal District Court's decision in *Shiro,* 174 F. Supp. 495, a bankruptcy case involving the trustee's power to avoid a preferential transfer by assignment, Irace and Lowry contend that Jones's June 14, 1988 letter is invalid and unenforceable as an assignment because it fails to manifest Jones's intent to permanently relinquish all control over the assigned funds and does nothing more than request payment from a specific fund. We disagree. The June 14, 1988 letter gives no indication that Jones attempted to retain any control over the funds he assigned to Dr. Herzog. Taken in context, the use of the word "request" did not give the court reason to question Jones's intent to complete the assignment and, although no specific amount was stated, the parties do not dispute that the services provided by Dr. Herzog and the amounts that he charged for those services were reasonable and necessary to the treatment of the shoulder injury referred to in the June 14 letter. Irace and Lowry had adequate funds to satisfy all of Jones's creditors, including Dr. Herzog, with funds left over for disbursement to Jones himself. Thus, this case simply does not present a situation analogous to *Shiro* because Dr. Herzog was given preference over Jones's other creditors by operation of the assignment. Given that Irace and Lowry do not dispute that they had ample notice of the assignment, the court's finding on the validity of the assignment is fully supported by the evidence and will not be disturbed on appeal.

Ethical Obligations

Next, Irace and Lowry contend that the assignment, if enforceable against them, would interfere with their ethical obligation to honor their client's instruction in disbursing funds. Again, we disagree.

Under the Maine Bar Rules, an attorney generally may not place a lien on a client's file for a third party. M. Bar R. 3.7(c). The Bar Rules further require that an attorney "promptly pay or deliver to the client, as requested by the client, the funds, securities, or other properties in the possession of the lawyer which the client is entitled to receive." M. Bar R. 3.6(f) (2) (iv). The rules say nothing, however, about a client's power to assign his right to proceeds from a pending lawsuit to third parties. Because the client has the power to assign his right to funds held by his attorney, McLellan v. Walker, 26 Me. at 117-18, it follows that a valid assignment must be honored by the attorney in disbursing the funds on the client's behalf. The assignment does not create a conflict under Rule 3.6(f) (2) (iv) because the client is not entitled to receive funds once he has assigned them to a third party. Nor does the assignment violate Rule 3.7(c), because the client, not the attorney, is responsible for placing the incumbrance upon the funds. Irace and Lowry were under no ethical obligation, and the record gives no indication that they were under a contractual obligation, to honor their client's instruction to disregard a valid assignment.

The District Court correctly concluded that the assignment is valid and enforceable against Irace and Lowry.

The entry is judgment affirmed.

All concurring.

III. THE FORMALITIES OF AN ASSIGNMENT

A. *Gifts*

Problem 185

The publication of her sensational memoirs made Lynn Brown a rich woman. One day she met her good friend Polly Travis on the street and, hearing Polly's tale of financial woe, said to her, "I'll tell you what. I have a savings account with Octopus National Bank that has a healthy amount in it. I have no need of the money, and I hereby give it to you." Polly thanked her with enthusiasm. Polly's friend Mary Bush was present throughout the conversation and is willing to testify to it. That evening Polly was shocked to hear that Lynn had been killed in a car accident. She was also shocked to learn that Octopus National Bank and Lynn's executor refused to give her the amount in the savings account. Will the law give it to her?

RESTATEMENT (SECOND) OF CONTRACTS

§332. Revocability of Gratuitous Assignments

(1) Unless a contrary intention is manifested, a gratuitous assignmen is irrevocable if

(a) the assignment is in a writing either signed or under seal that i delivered by the assignor; or
(b) the assignment is accompanied by delivery of a writing of a typ customarily accepted as a symbol or as evidence of the righ assigned.

(2) Except as stated in this Section, a gratuitous assignment is revoca ble and the right of the assignee is terminated by the assignor's death o incapacity, by a subsequent assignment by the assignor, or by notificatio from the assignor received by the assignee or by the obligor.

(3) A gratuitous assignment ceases to be revocable to the extent tha before the assignee's right is terminated he obtains

(a) a payment or satisfaction of the obligation, or
(b) judgment against the obligor, or
(c) a new contract of the obligor by novation.

(4) A gratuitous assignment is irrevocable to the extent necessary to avoid injustice where the assignor should reasonably expect the assignment to induce action or forbearance by the assignee or a sub-assignee and the assignment does induce such action or forbearance.

(5) An assignment is gratuitous unless it is given or taken

(a) in exchange for a performance or return promise that would be consideration for a promise; or
(b) as security for or in total or partial satisfaction of a preexisting debt or other obligation.

B. *Assignments for Consideration*

RESTATEMENT (SECOND) OF CONTRACTS

§324. Mode of Assignment in General

It is essential to an assignment of a right that the obligee manifest an intention to transfer the right to another person without further action or manifestation of intention by the obligee. The manifestation may be made to the other or to a third person on his behalf and, except as provided by statute or by contract, may be made either orally or by writing.

An assignment of an interest in real property requires a writing under the statute of frauds. If the assignment is a transfer of an interest in accounts receivable and is not exempt under UCC §9-109(d), Article 9 of the Code requires a written agreement signed by the assignor; see UCC §9-203. The same section mandates some sort of an authenticated record for any agreement using personal property or fixtures as collateral for a debt. Article 9 does not apply to the creation of interests in realty, wages, bank accounts, insurance, or certain other collateral described in §9-109(d). These matters are regulated either by the common law or by special statutory provisions.

Problem 186

Assume that Betty entered into a written agreement assigning contract rights immediately to Stateside. However, the assignment provided for an assignment of Betty's rights to purchase 2,000 carloads, not the entire 4,000 carloads promised by Sammy. Is this enforceable? To what extent? See UCC §2-210.

RESTATEMENT (SECOND) OF CONTRACTS

§326. Partial Assignment

(1) Except as stated in Subsection (2), an assignment of a part of a right, whether the part is specified as a fraction, as an amount, or otherwise, is operative as to that part to the same extent and in the same manner as if the part had been a separate right.

(2) If the obligor has not contracted to perform separately the assigned part of a right, no legal proceeding can be maintained by the assignor or assignee against the obligor over his objection, unless all the persons entitled to the promised performance are joined in the proceeding, or unless joinder is not feasible and it is equitable to proceed without joinder.

NOTE ON WAGE ASSIGNMENTS

At one time creditors who loaned money to individuals often asked for security in the form of a "wage assignment." The obligor would agree to give the creditor a right in the obligor's wages for the repayment of the obligation. Such an assignment might begin to operate immediately, with the employer paying a portion of the debtor's wages directly to the creditor, or be designed to operate only when the debtor was in default.

Nearly every state has some limitation on the assignment of wages. (Why, do you suppose?) A few states, such as Alabama, Code Ann. §8-5-21, prohibit wage assignments entirely in most kinds of transactions. More commonly, states limit wage assignments only in certain loans made by "small loan companies" (specially licensed lenders who are allowed higher interest rates for loans with a principal not exceeding specified amounts. These are known as "finance companies" in many states.) Such small loan legislation generally is restricted to procedural and signature requirements. A common limitation, for example, requires the employer and the borrower's spouse to sign an agreement for a wage assignment.

A few states with comprehensive consumer credit codes limit wage assignments in all consumer credit transactions. Such limitations typically make all wage assignments voidable at will by the consumer. See Wis. Stat. §422.404.

IV. LIMITATIONS ON THE ASSIGNMENT

A right of a contracting party to performance under an executory contract was historically known as a *chose in action* (meaning the right to sue someone in contract or tort). Common law once prohibited the assignment of a chose in action because it was considered too personal in nature, but a major exception developed. A contracting party could give another party a *power of attorney,* which would enable the person holding the power to enforce the contract. There were procedural and substantive problems that restricted the use of this ruse, including a requirement that any action at law had to be brought and prosecuted in the name of the assignor. However, the rival courts of equity were quick to recognize a suit by an assignee in the assignee's own name. Not to be outdone in the race for more customers, common law courts loosened up some of the substantive restrictions placed on the power of attorney; for example, allowing the assignment to survive the death of the assignor. However, the common law courts still refused to allow a suit in the name of the assignee. Most states have adopted statutes of civil procedure that now permit, and in fact require, an action to be brought in the name of the assignee. See generally, Murray on Contracts §135 (4th ed. 2001). There are other statutes outside of the UCC that also encourage assignment. In resolving the following Problems, ask yourself what the cited UCC sections indicate about the drafters' feelings concerning the freedom of assignment.

Problem 187

Assume in the banana transaction set out at the beginning of this chapter that the parties' contract contained the following provision:

> The parties promise not to assign this contract. Any purported assignment will be void from the beginning. The parties recognize the significance of this limitation and agree it controls over any trade usage or any other limitation allowing contract rights to be assigned.

Shortly after the contract was entered into, Sammy's Produce assigned its right to payment from Betty to Equity Farm Coop. Must Betty pay Equity when Sammy delivers the bananas? See UCC §2-210(2).

Problem 188

If the contract Joseph Armstrong originally signed with Wonder Spa had contained a clause stating that "The Spa promises that it will not assign this contract to a finance company," could he refuse to pay Nightflyer Finance Company when it proves to him that the contract was nonetheless assigned to it? See UCC §9-406(a) and its Official Comment 4. Would it make a difference if the clause had stated, "Any assignment of this contract to a finance company is void"?

CHENEY v. JEMMETT
Supreme Court of Idaho, 1984
107 Idaho 829, 693 P.2d 1031

DONALDSON, C.J. On February 10, 1977, plaintiff, Ernest Cheney, and his then-wife, Janet Cheney, entered into a real estate purchase agreemen with the defendants, Blaine and Nita Jemmett (the Cheney/Jemmet agreement). By the terms of that agreement, the plaintiff and his wife agreed to sell certain real property situated in Gem County, Idaho, to the defendants. The agreement stated a purchase price of $32,500, with $5,000 being paid by the first of March, 1977, and the balance of $27,50 plus interest at 9½% per annum, to be paid through an escrow at the Treasure Valley Bank, McCall, Idaho. The principal balance had bee reduced to the sum of $22,745.27 at the time of trial.

This agreement contained a term which specified that "[t]he Purchasers agree that they will not assign this agreement, nor any interes herein or in the property hereby agreed to be sold and purchased, withou first obtaining the written consent of Sellers." The contract furthe contained a default clause which specified what would happen in the event the purchasers defaulted on any of the terms of the agreement.

Sometime later, the defendants contacted an Emmett real estate broker to sell the property involved in the Cheney/Jemmett agreement The restriction on assignment was noted, and the plaintiff was contacted to obtain his consent. Plaintiff refused to consent to the proposed assign ment. Thereafter, the real estate broker, his salesman and a prospective purchaser, Douglas Honn, consulted an Idaho attorney about the assign ment problem. The attorney advised these parties to enter into a separate rental and sales agreement.

The defendants proceeded to set up a "Real Estate Agreement" (the Jemmett/Honn agreement) dated June 24, 1980, accompanied by a sepa rate and independent escrow agreement. Pursuant to this agreement, the defendants agreed to rent the property to the Honns whereupon,

> said agreement to rent continues until such time as the Jemmett-Cheney escrow in McCall, Idaho, is paid in full, whereupon, Seller does sell to Purchaser and Purchaser does purchase from Seller all of the real property and improvements thereon, subject to the terms of this agreement set out herein below.

Pursuant to the Jemmett/Honn agreement, the payments made by th Honns to the defendants, were remitted by the defendants to the escrow at the Treasure Valley Bank, McCall, Idaho, to be credited to the origina Cheney/Jemmett contract. The Honns were entitled to possession of th premises after June 24, 1980.

During the course of closing the final transaction between th Jemmetts and the Honns the real estate broker discovered an encum brance held by Treasure Valley Bank, McCall, Idaho, against the propert Plaintiff had assigned his interest in the Cheney/Jemmett contract to th bank in March of 1981, to secure a loan made by the bank to the plaintif

The assignment was supported by a UCC financing statement filed with the Gem County recorder describing the land in question. The real estate broker contacted plaintiff about the encumbrance and requested plaintiff to obtain a release from the bank removing this encumbrance. Plaintiff consented to deliver a satisfaction of the encumbrance to the real estate broker for the transaction between the Jemmetts and the Honns.

On March 17, 1981, and again on May 5, 1981, plaintiff sent the defendants written notices stating his intention to declare default, based on the alleged assignment the defendants made to the Honns. Twice, defendants claimed no such assignment had occurred. In the second notice, plaintiff advised defendants that unless they corrected their default, the entire purchase price then remaining unpaid, would be immediately due and payable. The defendants did not take any steps to cure the alleged default, but rather continued to make payments on the Cheney/Jemmett contract. Plaintiff (and Treasure Valley Bank, McCall, Idaho, by virtue of plaintiff's assignment of the Cheney/Jemmett contract to the bank) accepted all payments including those made after the first Notice of Intention to Declare Default sent on March 17, 1981.

The plaintiff brought an action against the defendants to compel the defendants to pay the balance due and owing on the contract, claiming that defendants were in default of the non-assignment clause. The case went to trial before the court, and at the conclusion of plaintiff's case, the defendants moved for an involuntary dismissal pursuant to I.R.C.P. 41(b). The record reveals that the district judge ruled from the bench, granting defendant's motion for dismissal and directing both parties to submit proposed findings of fact and conclusions of law.

The plaintiff first contends that the district court committed reversible error by adopting in their entirety, the "enormously sweeping and self-serving" findings of fact to their terms. The district court's conclusions of law 1 and 2 state as follows:

> 1. That the June 24, 1980 agreement between Defendants and Douglas and Barbara Honn did not constitute an assignment within the meaning of the language in the February 10, 1977 agreement restricting an assignment.
> 2. That the Plaintiff, Cheney, unreasonably and arbitrarily withheld his consent to the original request for consent to assignment.

We do not reach the issue of whether the Jemmett/Honn agreement constituted an assignment within the meaning of the Cheney/Jemmett agreement because, in any event, we are persuaded that plaintiff unreasonably and arbitrarily withheld his consent to the request for assignment.

It must first be noted that "[p]rovisions in bilateral contracts which forbid or restrict assignment of the contract without the consent of the obligor have generally been upheld as valid and enforceable when called into question, although the meaning of such terms becomes a matter of interpretation." 6 Am. Jur. 2d Assignments §22 (1963); see Annot., 37 A.L.R.2d 1251, 1253 (1954); Masterson v. Sine, 68 Cal. 2d 222, 65 Cal. Rptr. 545, 436 P.2d 561 (1968). While this is generally true, it must be noted that the non-assignment clause in the present case was not absolute in its terms. The purchasers agreed not to assign "without first obtaining the written consent of Sellers." In our view, the interpretation of a non-assignment clause conditioned on the consent of the seller as in the present case, necessarily implies that the seller will act reasonably and in good faith in exercising his right of approval. Cf. Mitsui & Co. v. Puerto Rico Water Resources Authority, 528 F. Supp. 768 (D.P.R. 1981) (consent cannot be arbitrarily withheld by party imposing restriction). The Utah Supreme Court cogently expressed our views in this regard.

> Where a contract provides that the matter of approval of performance is reserved to a party, he must "act fairly and in good faith in exercising that right. He has no right to withhold arbitrarily his approval; there must be a reasonable justification for doing so."

Prince v. Elm Investment Co., 649 P.2d 820, 825 (Utah 1982); (quoting William G. Vandever & Co. v. Black, 645 P.2d 637, 639 (Utah 1982)); see also W. P. Harlin Construction Co. v. Utah State Road Commission, 19 Utah 2d 364, 431 P.2d 792 (1967). Additionally, the Supreme Court of Montana has stated that "[w]hen a matter in a contract is left to the determination of one party alone, that party's determination is conclusive *if he acts in good faith.*" Brown v. First Federal Savings and Loan Association, 154 Mont. 79, 460 P.2d 97, 100 (1969) (emphasis added); cf. Meredith Corp. v. Design & Lithography Center, Inc., 101 Idaho 391, 614 P.2d 414 (1980) (satisfaction requirement determined by reasonable person standard).

In Funk v. Funk, 102 Idaho 521, 633 P.2d 586 (1981), we examined the right of a lessee to sublease without the consent of the lessor when the contract between the parties conditioned the right to sublease on obtaining the lessor's consent. Therein, we concluded that a lessor may not unreasonably withhold his consent to a prospective sublease.

> A landlord may and should be concerned about the personal qualities of a proposed subtenant. A landlord should be able to reject a proposed subtenant when such rejection reflects a concern for the legitimate interest of the landlord, such as assurances of rent receipt, proper care of the property and in many cases the use of the property by the subtenant in a manner reasonably consistent with the usage of the original lessee. Such concerns by the landlord should result in the upholding of a withholding of consent by a landlord. However, no desirable public policy is served by upholding a landlord's arbitrary refusal of consent merely because of whim or caprice or where, as here, it is apparent that the refusal to consent was withheld for purely financial reasons and that the landlord wanted the lessees to enter into an entirely new lease agreement with substantial increased financial benefits to the landlord. If the lessor is allowed to arbitrarily refuse consent to a sublease for what is in effect no reason at all, such would virtually nullify the right of a lessee to sublet.

102 Idaho at 524, 633 P.2d at 589.

We believe the principles and reasoning enunciated in *Funk* are equally applicable to the case before us today. Accordingly, we hold that when a contract grants the purchaser the right to assign his interest in the contract, or in the property in issue, conditioned upon obtaining the consent of the seller, the seller must act reasonably and in good faith in withholding his consent to a proposed assignment. Our holding today applies only to those cases where the contract specifically conditions the proposed assignment on obtaining the seller's consent. As to those contracts which absolutely prohibit the right of assignment, we express no opinion.

The record herein discloses that the plaintiff had no objection to Honn's credit, Honn's reputation, or towards Honn personally. In the circumstances of the present case, we believe the plaintiff's refusal was not given in good faith and was totally unreasonable. Thus, we affirm the order of the district court dismissing plaintiff's claims pursuant to I.R.C.P. 41(b).

The last issue before us concerns the allowance of attorney fees in this case. The contract between Cheney and the Jemmetts provided that "[i]n the event dispute arises between the parties hereto for interpretation or enforcement of this agreement, the prevailing party shall be entitled to reasonable attorney's fees and costs." On the basis of this provision, the trial court awarded attorney fees and costs to the Jemmetts.

Jemmetts were the prevailing parties at the trial level, and therefore were properly awarded attorney's fees and costs at the trial level. In view of our holding today, the Jemmetts are the prevailing party on appeal, and accordingly are entitled to reasonable attorney fees and costs on appeal.

The decision of the district court is affirmed.

Costs and attorney fees on appeal to respondents.

SHEPARD, BISTLINE and HUNTLEY, JJ., concur.

BISTLINE, J., specially concurring. As Justice Bakes correctly notes in his dissent, the Court's opinion extends the principle of the *Funk* case. In *Funk*, four members of the Court knowingly wrote new law in Idaho, and, in doing so, pointed out that the rule of *Funk* was decidedly a minority view, but tending otherwise.

Despite the continued criticism of *Funk* by Justice Bakes, on further reflection I am fully convinced that *Funk* continued Idaho jurisprudence in a good direction. As most practitioners know, when the parties to a lease or a contract have reached an attorney's office, they have already agreed generally, and are the best of friends, or at least amicable. It is the unfortunate function of the attorney to cast some gloom on the affair by mentioning such things as default, forfeiture, lawsuits, assignability, and non-assignability. Ordinarily, when asked, they agree to assignability, and to a proper question, submit to the proposition that the lessor or seller should be asked to give his consent. This usually finds its way into the written agreement. What experience teaches practitioners, however, is that the amicable parties almost invariably assure each other that the requirement of consent will present no problem. This assurance seldom finds itself the agreement. Sometimes it does, and is couched in terms of consent being not unreasonably withheld. Our decision in *Funk* did no more than own up to reality.

There is nonetheless much to what Justice Bakes has written. We wrote *new* laws in *Funk*; Justice Bakes, in dissent in that case, did not suggest, as he does in this case, that our opinion is overruling prior case law. Today, in the view of Justice Bakes, we are not only making new, but overruling prior law, and he cites the 1960 *Simplot* case [J. R. Simplot Co. v. Chambers, 82 Idaho 104, 350 P.2d 211] in his opinion. In all likelihood the 1960 *Simplot* court would not have, in 1960, read into the contract (or the lease in *Funk*) the implication that consent to an assignment cannot be unreasonably withheld. Case law, however, is subject to change. Just six years prior to the *Simplot* case, the Court in Graves v. Cupic, 75 Idaho 451, 272 P.2d 1020 (1954), worked a drastic change in existing Idaho case law by declaring that forfeitures of land contracts would no longer be upheld in Idaho, unless based on a stipulation for liquidated damages which was not disproportionate. 75 Idaho at 456, 272 P.2d at 1023. That which is not disproportionate is reasonable. 75 Idaho at 459, 272 P.2d at 1025. Clearly, the Court, even in 1952, was not a court which was averse to change.

Today, as readily distinguishable from 1950, or from 1960, Idaho's society has become far more transient. Many members of the work force are subject to new assignments and new locations, including some which are out-of-state. As I comprehend the situation, it is just as much a penalty to in 1984 refuse the right to assign a contract, or sell a property subject to mortgage, as it was a penalty in 1950 and forever prior thereto to strip a man of all equity in a property because he has fallen on hard times and failed to make monthly payments.

Not mentioned in the Court's opinion, but a salient factor is a finding by the trial court that the Jemmetts suffered unfortunate financial circumstances and found it imperative to move from Emmett, Idaho, to Oregon. It is inescapable that the trial court's decision was supported by this Court's *Funk* decision. Moreover, it is a furtherance of the equitable philosophies of this Court, beginning with *Graves* and continuing thereafter without interruption other than for the aberrational Ellis v. Butterfield.

So viewing the opinion for the Court, I am nonetheless troubled at the award of attorney's fees, both at the trial level and in this Court. *Funk* was non-existent when the contract was drawn between Cheney and the Jemmetts. Nor was it available when arose the change in the Jemmetts' circumstances giving rise to this case. Nor was it available when the issues were framed by the pleadings. It was only on hand, and argued strongly to the trial court, at the time the written decision was being drafted.

It seems to my mind that an award of attorney's fees to be paid by Cheney is not within the language of their contract — "In the event dispute arises between the parties hereto for interpretation or enforcement of this agreement, the prevailing party shall be entitled to reasonable attorney's fees and costs." While a dispute did arise, the resolution thereof did not hinge upon an interpretation of the parties' agreement, although perhaps it might have. This Court has upheld the lower court's determination on only one ground, that of reading into the agreement the implicit covenant of acting reasonably and in good faith. [The Jemmetts' answer did allege, in language reminiscent of *Graves*: "To enforce specific performance under circumstances of this case would be unfair and unjust. The consequences would be harsh, inequitable, oppressive and unconscionable. . . . The refusal of plaintiff to give consent herein is unreasonable and is motivated by the plaintiff's desire to force a pay-off. . . ."]

Other than for *Funk*, however, the Court today might have followed along with Justice Bakes' view that *a contract is a contract*, and the courts do not sit to write language into them which the parties failed to include. Where attorney's fees are concerned, as per the agreement, I am hard-pressed to see that we are "interpreting" the agreement. Justice Bakes drives home very clearly that we are not doing so, and for that reason I am not comfortable in seeing Mr. Cheney penalized for attorney's fees in proceedings below, or here. In the year 1977 it is surmisable that Mr. Cheney very well might have been the prevailing party.

BAKES, J. dissenting. I dissent from the majority's application of the principles enunciated in Funk v. Funk, 102 Idaho 521, 633 P.2d 586 (1981), to this contract dispute. As I explained in my dissent in *Funk*, a contract should be carried out as the parties negotiated it, and not as the majority of this Court thinks they should have negotiated it.

In reading a "good faith" requirement into the Cheney/Jemmett contract, the majority has ignored both the contract provisions and existing Idaho law. It is well established that a court must respect the contract provisions to which parties have lawfully agreed. Nichols v. Knowles, 87 Idaho 550, 555, 394 P.2d 630, 633 (1964); Howard v. Bar Bell Land & Cattle Co., 81 Idaho 189, 197, 340 P.2d 103, 107 (1959). The Jemmetts signed this real estate purchase agreement despite the presence of the clause conditioning assignment of the contract on the sellers' approval. If a "good faith" or "reasonability" requirement was desired, it was for the parties, not this Court, to make that determination.

This Court has previously refused to read a reasonability requirement into the assignment clauses of contracts. Speaking to just such a clause in J. R. Simplot Co. v. Chambers, 82 Idaho 104, 350 P.2d 211 (1960), this Court stated:

> It will be noted that said section 31 specifies the only qualification of the assignee to be a controlled corporation. . . . To construe said section 31 as restricting the right to assign to a corporation which may be by appellants considered "reasonable" would necessitate the insertion of words and the making by the court of a new contract. This we cannot do. Courts cannot make for the parties better agreements than they themselves have been satisfied to make, and by a process of interpretation relieve one of the parties from the terms which he voluntarily consented to; nor can courts interpret an agreement to mean something the contract does not itself contain. (Citations omitted.) 82 Idaho at 109-110, 350 P.2d at 214.

Here, by reading a reasonability requirement into the non-assignment clause of this contract, the Court has reworded the contract. This is contrary to Simplot v. Chambers, supra, which the Court neither overrules nor distinguishes, but merely ignores.

The majority suggests that bilateral contracts which absolutely forbid assignment of the contract might be valid, ante at 1034, but holds that a non-assignment clause conditioned on the consent of the seller implies a reasonability requirement which is subject to the approval of the court. This merely enhances the uncertainty which the Court's opinion today injects into the law of contracts.

Following the Court's decision today, a seller would be ill advised tc enter into a contract which permits an assignment subject to the seller's approval. By entering such a contract, the seller would essentially be surrendering any control over that assignment. Sellers will no doub routinely insert provisions in the contract containing complete restriction on assignment. But under the majority opinion even the validity o complete restrictions is still up in the air.

The only certain thing to result from this case is that there will be a lo of litigation between buyers and sellers over what the courts may think i reasonable. Since this Court has not set down any standards as to what i to be considered in determining reasonableness, all such determination must of necessity be *ad hoc* decisions. This will no doubt assure litigatioı in every case. Such a rule of law which requires litigation to settle ever dispute does not have much to commend it.

I dissent.

On Denial of Petition on Rehearing

Per Curiam. On consideration and denial of the Petition for Rehearin we now conclude that it would be unjust to award attorney fees on appea and also that the award of attorney fees in the trial court below wa improper. The judgment below is modified by striking therefrom th award of attorney fees, and as modified is affirmed.

Costs on appeal to respondent.

Rehearing denied.

In all other respects the Court adheres to its prior opinions issue October 15, 1984.

NOTES

1. Federal law restricts the assignment of claims against the Unite States before the issuance of a warrant for payment and the assignment c any public contract or order. There is an exception in the Assignment c Claims Act of 1940. That act permits a single assignment to a financial inst tution where (a) the contract does not restrict assignment and (b) writte notice is filed with the appropriate government agency and with any suret on a bond issued in connection with the contract. 31 U.S.C. §203; 4 U.S.C. §15.

2. In the hypothetical transaction at the beginning of this chapter, it clear that both Betty and Sammy have existing contractual rights. The rights may be subject to a condition (Sammy's right to payment, fc example, is conditioned upon its delivery of the bananas as required), bı their rights are something more than just an expectation arising from hope that a contract will come into being in the future.

Should an assignment by Sammy of rights that Sammy expects wi arise in future contracts be enforceable? The modern answer is yes. Und

UCC §9-204, a party can take a security interest in "after-acquired" property; that is, property that the debtor will acquire after the time when the debtor and creditor first enter into their secured transaction. In the context of the hypothetical, Equity Farm Coop might ask Sammy to assign it all of the rights that Sammy has in currently existing contracts (including the one with Betty) plus any rights to payment under banana sale contracts that may arise in the future. Equity would have an after-acquired security interest in "accounts." As Sammy entered into banana contracts, Equity's security interest would "attach" to Sammy's rights to payment under these new contracts; that is, the security interest would be valid as to the payment rights Sammy acquired under later contracts.

V. DEFENSES OF THE OBLIGOR

A. *Waiver of Defense Clauses*

Generally, the rights of an assignee, like those of a third party beneficiary, are derivative. The assignee gets no better rights against the obligor than the assignor had, so that the obligor can assert contractual defenses when pursued by the assignee. There are two major exceptions to this concept.

Problem 189

Joseph Armstrong signed a contract with Wonder Spa, and at the same time he signed a promissory note for $1,000, payable to the order of the spa. A week later he received a payment booklet from Nightflyer Finance Company, and he dutifully began making payments to it. Six months later the spa burned to the ground, so Armstrong stopped making payments. The finance company brought suit against him on the promissory note, claiming to be a "holder in due course" of the note, and thus free of his defense of failure of consideration. See UCC §§3-302, 3-305. Must he pay?

Problem 190

Instead of the above, the original contract Armstrong signed with the spa provided that "Any problems the customer has with the spa will be settled by negotiations with the spa's management alone, and will in no way be asserted against any finance company to whom this obligation may be assigned." Is such a clause (called a *waiver of defenses against assignee* clause) valid to insulate the finance company from the same defense, i.e., the destruction of the spa by fire? Read UCC §9-403.

UNICO v. OWEN
New Jersey Supreme Court, 1967
50 N.J. 101, 232 A.2d 405

FRANCIS, J. The issue to be decided here is whether plaintiff Unico, a New Jersey partnership, is a holder in due course of defendant's note. I so, it is entitled to a judgment for the unpaid balance due thereon, fo which this suit was brought. The District Court found plaintiff was no such a holder and that it was therefore subject to the defense interpose by defendant, maker of the note, of failure of consideration on the part o the payee, which endorsed it to plaintiff. Since it was undisputed that th payee failed to furnish the consideration for which the note was given judgment was entered for defendant. The Appellate Division affirmed, an we granted plaintiff's petition for certification in order to consider th problem. 47 N.J. 241 (1966).

The facts are important. Defendant's wife, Jean Owen, answered a advertisement in a Newark, N.J. newspaper in which Universal Stere Corporation of Hillside, N.J., offered for sale 140 albums of stereophoni records for $698. This amount could be financed and paid on an install ment basis. In addition the buyer would receive "without separate charge (as plaintiff puts it) a Motorola stereo record player. The plain implicatio was that on agreement to purchase 140 albums, the record player woul be given free. A representative of Universal called at the Owens' home an discussed the matter with Mr. and Mrs. Owen. As a result, on November 6 1962, they signed a "retail installment contract" for the purchase of 14 albums on the time payment plan proposed by Universal.

Under the printed form of contract Universal sold and Owen bough "subject to the terms and conditions stipulated in Exhibit 'A' heret annexed and printed on the other side hereof and made part here-of, th following goods . . . 12 stereo albums to be delivered at inception o program and every 6 months thereafter until completion of program," "new Motorola consolo [sic]" and "140 stereo albums of choice. . . ." Th total cash price was listed as $698; a down-payment of $30 was noted; th balance of $668, plus an "official fee" of $1.40 and a time price differenti of $150.32, left a time balance of $819.72 to be paid in installments. Owe agreed to pay this balance in 36 equal monthly installments of $22.77 eac beginning on December 12, 1962, "at the office of Universal Stereo Corp 8 Hollywood Avenue, Hillside, N.J., or any other address determined b assignee." The contract provided:

> If the Buyer executed a promissory note of even date herewith in the amount of the time balance indicated, said note is not in payment thereof, but is a negotiable instrument separate and apart from this contract even though at the time of execution it may be temporarily attached hereto by perforation or otherwise.

It was part of Universal's practice to take notes for these contract and obviously there was no doubt that it would be done in the Owen cas Owen did sign a printed form of note which was presented with th contract. The name of Universal Stereo Corporation was printed thereon, and the note provided for the monthly installment payments specified. On the reverse side was an elaborate printed form of endorsement which began "Pay to the order of Unico, 251 Broad St., Elizabeth, New Jersey, with full recourse"; and which contained various waivers by the endorser, and an authorization to the transferee to vary the terms of the note in its discretion in dealing with the maker.

Exhibit "A," referred to as being on the reverse side of the contract, is divided into three separate parts, the body of each part being in very fine print. The *first* section sets out in 11 fine print paragraphs the obligations of the buyer and rights of the seller. Under paragraph 1 the seller retains title to the property until the full time price is paid. Here it may be noted that Universal recorded the contract in the Union County Register's Office a few days after its execution. Paragraph 2 says that the term "Seller" as used shall refer to the party signing the contract as seller "or *if said party has assigned said contract, any holder of* said contract." (Emphasis added.) It is patent that Universal contemplated assigning the contract forthwith to Unico, and it was so assigned. Of course, it was a bilateral executory contract, and since under the language just quoted "assignee" and "seller" have the same connotation, the reasonable and normal expectation by Owen would be that performance of the delivery obligation was a condition precedent to his undertaking to make installment payments. See, 3 Williston on Contracts (3d ed. Jaeger 1960) §418, 418A. It has not been suggested that this assignment provision which equates "seller" with "assignee" creates such an intimate relationship between Universal and Unico as to impose Universal's delivery performance obligation on Unico as well as to transfer Universal's right to payment to Unico. Consequently the question is reserved for future consideration in an appropriate case under the Uniform Commercial Code. See NJS 12A:2-210(4). In view of the comprehensive language employed, is such an assignment one for security only? Note New Jersey Study Comment 5, and Uniform Commercial Code Comment 5, to subsection 4. Universal sought under paragraph 5 to deprive Owen of his right to plead failure of consideration against its intended assignee, Unico. The paragraph provides:

> Buyer hereby acknowledges notice that the contract may be assigned and that assignees will rely upon the agreements contained in this paragraph, and agrees that the liability of the Buyer to any assignee shall be immediate and absolute and not affected by any default whatsoever of the Seller signing this contract; and in order to induce assignees to purchase this contract, the Buyer further agrees not to set up any claim against such Seller as a defense, counterclaim or offset to any action by any assignee for the unpaid balance of the purchase price or for possession of the property.

The validity and efficacy of this paragraph will be discussed hereinafter. At this point it need only be said that the design of Universal in adopting this form of contract and presenting it to buyers, not for bargaining purposes but for signature, was to get the most and give the least. Overall it includes a multitude of conditions, stipulations, reservations, exceptions and waivers skillfully devised to restrict the liability of the seller within th narrowest limits, and to leave no avenue of escape from liability on th part of the purchaser. . . .

At this point the hyperexecutory character of the performance agree to by Universal in return for the installment payment stipulation by Owe must be noted. Owen's time balance of $819.72 was required to be pai by 36 monthly installments of $22.77 each. Universal's undertaking was t deliver 24 record albums a year until 140 albums had been delivered Completion by the seller therefore would require $5^{1}/_{3}$ years. Thus although Owen would have fully paid for 140 albums at the end of thre years, Universal's delivery obligation did not have to be completed unti $2^{1}/_{3}$ years thereafter. This means that 40 percent of the albums, althoug fully paid for, would still be in the hands of the seller. It means also tha for $2^{1}/_{3}$ years Universal would have the use of 40 percent of Owen's mone on which he had been charged the high time-price differential rate. I contrast, since Universal discounted the note immediately with Unico o the strength of Owen's credit and purchase contract, the transaction, s far as the seller is concerned, can fairly be considered as one for cash In this posture, Universal had its sale price almost contemporaneousl with Owen's execution of the contract, in return for an executory perform ance to extend over $5^{1}/_{3}$ years. And Unico acquired Owen's note which, o its face and considered apart from the remainder of the transaction appeared to be an unqualifiedly negotiable instrument. On the othe hand, on the face of things, by virtue of the ostensibly negotiable note an the waiver or estoppel clause quoted above which was intended to bar an defense against an assignee for the seller's default, Owen had no recours and no protection if Universal defaulted on its obligation and was finan cially worthless.

Owen's installment note to Universal for the time balance of $819.7 is dated November 6, 1962. Although the endorsement on the revers side is not dated, Unico concedes the note was received on or about th day it was made. The underlying sale contract was assigned to Unico a the same time, and it is admitted that Owen was never notified of th assignment.

Owen received from Universal the stereo record player and th original 12 albums called for by the contract. Although he continued t pay the monthly installments on the note for the 12 succeeding month he never received another album. During that period Mrs. Owe endeavored unsuccessfully to communicate with Universal, and finall ceased making payments when the albums were not delivered. Nothin further was heard about the matter until July 1964, when the attorne for Unico, who was also one of its partners, advised Mrs. Owen tha Unico held the note and that payments should be made to it. She tol him the payments would be resumed if the albums were delivered. N further deliveries were made because Universal had become insolven Up to this time Owen had paid the deposit of $30 and 12 installment of $22.77 each, for a total of $303.24. Unico brought this suit for th balance due on the note plus penalties and a 20 percent attorney' fee. . . .

I

This brings us to the primary inquiry in the case. Is the plaintiff Unico a holder in due course of defendant's note?

The defendant's note was executed on November 6, 1962. The Uniform Commercial Code, NJS 12A:1-101 et seq., was adopted by the Legislature in 1961 (L.1961 c.120), but it did not become operative until January 1, 1963. The note, therefore, is governed by the Uniform Negotiable Instruments Law, NJSA 7:1-1 et seq. Section 52 thereof defined a holder in due course as one who (among other prerequisites) took the instrument "in good faith and for value." NJSA 7:2-52. If plaintiff is not a holder in due course it is subject to the defense of failure of consideration on the part of Universal, both under the Negotiable Instruments Law, NJSA 7:2-58, and the Uniform Commercial Code, NJS 12A:3-306(c).

In the field of negotiable instruments, good faith is a broad concept. The basic philosophy of the holder in due course status is to encourage free negotiability of commercial paper by removing certain anxieties of one who takes the paper as an innocent purchaser knowing no reason why the paper is not as sound as its face would indicate. It would seem to follow, therefore, that the more the holder knows about the underlying transaction, and particularly the more he controls or participates or becomes involved in it, the less he fits the role of a good faith purchaser for value; the closer his relationship to the underlying agreement which is the source of the note, the less need there is for giving him the tension-free rights considered necessary in a fast-moving, credit-extending commercial world.

We are concerned here with a problem of consumer goods financing. Such goods are defined in the Uniform Commercial Code as those used or bought for use primarily for personal, family or household purposes. NJS 12A:9-109(1). Although the Code as such is not applicable in this case, the definition is appropriate for our purposes. And it is fair to say also that in today's society, sale of such goods and arrangements for consumer credit financing of the sale are problems of increasing state and national concern. The consumer-credit market is essentially a process of exchange, the general nature of which is shaped by the objectives and relative bargaining power of each of the parties. In consumer goods transactions there is almost always a substantial differential in bargaining power between the seller and his financer, on the one side, and the householder on the other. That difference exists because generally there is a substantial inequality of economic resources between them, and of course, that balance in the great mass of cases favors the seller and gives him and his financer the power to shape the exchange to their advantage. Their greater economic resources permit them to obtain the advice of experts; moreover, they have more time to reflect about the specific terms of the change prior to the negotiations with the consumer; they know from experience how to strengthen their own position in consumer-credit arrangements; and the financer-creditor is better able to absorb the impact of a single imprudent or unfair exchange. See Curran, Legislative Controls as a Response to Consumer-Credit Problems, 8 B.C. Ind. and Com. L. Rev. 409, 435-437 (1967).

Mass marketing in consumer goods, as in many other commercia activities, has produced standardized financing contracts. Henningsen Bloomfield Motors, Inc., 32 N.J. 358, 389 (1960). As a result there is n real arms-length bargaining between the creditor (seller-financer) and th consumer, beyond minimal negotiating about amount of credit, terms c installment payment and description of the goods to be purchased, all c which is accomplished by filling blanks left in the jungle of finely printec creditor-oriented provisions. In the present case the purchase contrac was a typical standardized finely printed form, focused practically in it entirety upon the interests of the seller and its intended assignee. Littl remained to be done but to describe the stereo record player and to fi the price and terms of installment payment by filling in the blanks. Even a to the matter inserted in the blanks, it cannot be said that there was an real bargaining; the seller fixed the price of the albums, and, as we sha see, the plaintiff Unico as the financer for Universal established th maximum length of the installment payment period under its contrac with Universal. The ordinary consumer goods purchaser more often tha not does not read the fine print; if he did it is unlikely that he woul understand the legal jargon, and the significance of the clauses is nc explained to him. This is not to say that all such contracts of adhesion ar unfair or constitute imposition. But many of them are, and the judicia branch of the government within its sphere of operation in construing an applying such contracts must be responsive to equitable considera tions. . . .

The courts have recognized that the basic problem in consumer gooc sales and financing is that of balancing the interest of the commercia community in unrestricted negotiability of commercial paper against th interest of installment buyers of such goods in the preservation of the normal remedy of withholding payment when, as in this case, the selle fails to deliver as agreed, and thus the consideration for his obligation fail Many courts have solved the problem by denying to the holder of th paper the status of holder in due course where the financer maintains close relationship with the dealer whose paper he buys; where th financer is closely connected with the dealer's business operations c with the particular credit transaction; or where the financer furnishes th form of sale contract and note for use by the dealer, the buyer signs th contract and note concurrently, and the dealer endorses the note an assigns the contract immediately thereafter or within the perio prescribed by the financer. Other courts have said that when the finance supplies or prescribes or approves the form of sales contract, or cond tional sale agreement, or chattel mortgage as well as the installmen payment note (particularly if it has the financer's name printed on th face or in the endorsement), and all the documents are executed b the buyer at one time and the contract assigned and note endorsed to th financer and delivered to the financer together (whether or not attache or part of a single instrument), the holder takes subject to the rights an obligations of the seller. The transaction is looked upon as a species c tripartite proceeding, and the tenor of the cases is that the financer shoul not be permitted "to isolate itself behind the fictional fence" of th

Negotiable Instruments Law, and thereby achieve an unfair advantage over the buyer.

Before looking at the particular circumstances of the above cases, it seems advisable to examine into the relationship between Universal and the financer Unico.

Unico is a partnership formed expressly for the purpose of financing Universal Stereo Corporation, and Universal agreed to pay all costs up to a fixed amount in connection with Unico's formation. The elaborate contract between them, dated August 24, 1962, recited that Universal was engaged in the merchandising of records and stereophonic sets, and that it desired to borrow money from time to time from Unico, "secured by the assignment of accounts receivable, promissory notes, trade acceptances, conditional sales contracts, chattel mortgages, leases, installment contracts, or other forms of agreement evidencing liens." Subject to conditions set out in the agreement, Unico agreed to lend Universal up to 35 percent of the total amount of the balances of customers' contracts assigned to Unico subject to a limit of $50,000, in return for which Universal submitted to a substantial degree of control of its entire business operation by the lender. As collateral security for the loans, Universal agreed to negotiate "to the lender" all customers' notes listed in a monthly schedule of new sales contracts, and to assign all conditional sale contracts connected with the notes, as well as the right to any monies due from customers.

Specific credit qualifications for Universal's record album customers were imposed by Unico; requirements for the making of the notes and their endorsement were established, and the sale contracts had to be recorded in the county recording office. All such contracts were required to meet the standards of the agreement between lender and borrower, among them being that the customer's installment payment term would not exceed 36 months and "every term" of the Unico-Universal agreement was to "be deemed incorporated into all assignments" of record sales contracts delivered as security for the loans. It was further agreed that Unico should have all the rights of Universal under the contracts as if it were the seller, including the right to enforce them in its name, and Unico was given an irrevocable power to enforce such rights.

In the event of Universal's default on payment of its loans, Unico was authorized to deal directly with the record buyers with respect to payment of their notes and to settle with and discharge such customers. Unico was empowered to place its representatives on Universal's premises with full authority to take possession of the books and records; or otherwise, it could inspect the records at any time; and it was given a "special property interest" in such records. Financial statements were required to be submitted by Universal "at least semi-annually" and two partners of Unico were to be paid one-quarter of one percent interest on the loans as a management service charge, in addition to the interest to be paid Unico. Significant also in connection with the right to oversee Universal's business is a warranty included in the contract. It warrants that Universal owns free and clear "all merchandise referred to and described in [the sales] contracts, . . . at the time of making the sale creating such contracts." Obviously this was not the fact, otherwise Universal would not have discontinued shipping records to its customers, such as Owen. If Universa did not have such a store of records, as warranted, Unico might well hav had reason to suspect its borrower's financial stability.

This general outline of the Universal-Unico financing agreement serve as evidence that Unico not only had a thorough knowledge of the natur and method of operation of Universal's business, but also exercised exten sive control over it. Moreover, obviously it had a large, if not decisive, han in the fashioning and supplying of the form of contract and note used b Universal, and particularly in setting the terms of the record album sale agreement, which were designed to put the buyer-consumer in an unfai and burdensome legal strait-jacket and to bar any escape no matter what th default of the seller, while permitting the note-holder, contract-assignee t force payment from him by enveloping itself in the formal status of holder i due course. To say the relationship between Unico and the business opera tions of Universal was close, and that Unico was involved therein, is to put mildly. There is no case in New Jersey dealing with the contention that th holder of a consumer goods buyer's note in purchasing it did not meet th test of good faith negotiation because the connection between the selle and the financer was as intimate as in this case. Compare, James Talcott, In v. Shulman, 82 N.J. Super 438 (App. Div. 1964); Westfield Investment Co. Fellers, 74 N.J. Super 575 (Law Div. 1962).

There is a conflict of authority in other jurisdictions (Annotation, 4 A.L.R.2d 8 (1955), but we are impelled for reasons of equity and justice t join those courts which deny holder in due course status in consume goods sales cases to those financers whose involvement with the seller business is as close, and whose knowledge of the extrinsic factors — i.e the terms of the underlying sale agreement — is as pervasive, as it is in th present case. Their reasoning is particularly persuasive in this case becaus of the unusually executory character of the seller's obligation to furnis the consideration for the buyer's undertaking. . . .

For purposes of consumer goods transactions, we hold that where th seller's performance is executory in character and when it appears fro the totality of the arrangements between dealer and financer that th financer has had a substantial voice in setting standards for the underlyin transaction, or has approved the standards established by the dealer, an has agreed to take all or a predetermined or substantial quantity of th negotiable paper which is backed by such standards, the financer shoul be considered a participant in the original transaction and therefore no entitled to holder in due course status. We reserve specifically the que tion whether, when the buyer's claim is breach of warranty as distin guished from failure of consideration, the seller's default as to the forme may be raised as a defense against the financer. Cf. Eastern Acceptanc Corp. v. Kavlick, 10 N.J. Super. 253 (App. Div. 1950).

II

Plaintiff argues that even if it cannot be considered a holder in du course of Owen's note, it is entitled to recover regardless of the failure consideration on the part of Universal, because of the so-called waiver of defenses or estoppel clause contained in the sale contract. The clause says:

> Buyer hereby acknowledges notice that this contract may be assigned and that assignees will rely upon the agreements contained in this paragraph, and agrees that the liability of the Buyer to any assignee shall be immediate and absolute and not affected by any default whatsoever of the Seller signing this contract; and in order to induce assignees to purchase this contract, the Buyer further agrees not to set up any claim against such Seller as a defense, counterclaim or offset to any action by any assignee for the unpaid balance of the purchase price or for possession of the property.

This provision is the fifth of 11 fine print paragraphs on the reverse side of the sale contract. The type is the same as in the other clauses; there is no emphasis put on it in the context, and there is no evidence that it was in any way brought to Owen's attention or its significance explained to him. But regardless, we consider that the clause is an unfair imposition on a consumer goods purchaser and is contrary to public policy.

The plain attempt and purpose of the waiver is to invest the sale agreement with the type of negotiability which under the Negotiable Instruments Law would have made the holder of a negotiable promissory note a holder in due course and entitled to recover regardless of the seller-payee's default.

In our judgment such a clause in consumer goods conditional sale contracts, chattel mortgages, and other instruments of like character is void as against public policy for three reasons: (1) it is opposed to the policy of the Negotiable Instruments Law which had established the controlling prerequisites for negotiability, and provided also that the rights of one not a holder in due course were subject to all legal defenses which the maker of the instrument had against the transferor. NJSA 7:2-58; (2) it is opposed to the spirit of NJS 2A:25-1, which provides that an obligor sued by an assignee "shall be allowed . . . all . . . defenses he had against the assignor before notice of such assignment was given to him." (It is conceded here that plaintiff gave no notice of the assignment to defendant); and (3) the policy of our state is to protect conditional vendees against imposition by conditional vendors and installment sellers.

[The court then quoted what is now UCC §9-403.]

In this section of the Code, the Legislature recognized the possibility of need for special treatment of waiver clauses in consumer goods contracts. Such contracts, particularly those of the type involved in this case, are so fraught with opportunities for misuse that the purchasers must be protected against oppressive and unconscionable clauses. And [§9-403] in the area of consumer goods sales must as a matter of policy be deemed closely linked with §2-302, NJS 12A:2-302, which authorizes a court to refuse to enforce any clause in a contract of sale which it finds is unconscionable. We see in the enactment of these two sections of the Code an intention to leave in the hands of the courts the continued application of common law principles in deciding in consumer goods cases whether such waiver clauses as the one imposed on Owen in this case are so one-sided as to be contrary to public policy. . . .

For the reasons stated, we hold the waiver clause unenforceable and invalid against Owen.

III

We agree with the result reached in the tribunals below. Plaintif offered no proof in the trial court to show that the value of the 12 albums Owen received before breach of the contract by Universal, together with that of the record player at the time of the breach (assuming its value was material in view of the seller's representation that there was to be no charge for it), was in excess of the $303.24 paid by Owen under the contract. Moreover, there has been no suggestion throughout this proceeding that plaintiff is entitled to a partial recovery on the note in its capacity as an assignee thereof. Accordingly, the judgment for the defendant is affirmed.

NOTES

1. Until recent times, the common law typically favored the finance company in the above situation, using negotiable instruments law, the contractual waiver of defenses clause, or both to strip the consumer o defenses. The policy here was to promote the free marketability of the note/contract. Where such paper is signed by someone in business, thi policy makes sense, but consumers, not having the bargaining ability o knowledge to avoid these tangles, are thought to deserve greater protec tion. Consequently, the Federal Trade Commission has promulgated regulation having the force of law that requires sellers of goods or service on credit to put on the contract a legend preserving the ability o consumers to assert defenses against assignees. See Federal Trad Commission Holder-in-Due-Course Regulations, 16 C.F.R. §433.1-433. (the legend preserving these defenses is quoted in the following case) State statutes frequently give similar protection to consumers and some times others, such as farmers.

2. Business obligors do not escape so easily. Section 9-403 of th Code, which you should read, enforcesing waiver-of-defenses-against assignee clauses where the obligor is not a consumer, except as to the ver few defenses that are permitted against holders in due course (the so called "real" defenses listed in §3-305(a)(1)). Before an assignee qualifie for the protection of §9-403, the assignee must take the assignment fo value, in good faith, and without notice of problems with the obligatio assigned; i.e., the assignee must meet the same qualifications imposed o someone trying to become a holder in due course of commercial pape (§3-302). A lawyer reviewing a contract for a client should alert the clien to the consequences of waiving almost all defenses against later assignee of the paper, pointing out that even if the other side breaches the contrac the client will still have to pay the assignee.

3. When a business assigns its accounts receivable to a finance company, sometimes the parties agree that the finance company will collect the accounts as they mature. But because some account debtors become worried if they must deal with a strange creditor, and also for practical reasons of convenience, instead the assignor and assignee may agree to *nonnotification financing*, whereby the assignor collects the accounts and turns the money over to the assignee. While the common law courts had some doubts as to the validity of an assignment allowing the assignor such continued control over the accounts receivable, these procedures are now clearly authorized by the UCC. See §9-205.

FORD MOTOR CREDIT CO. v. MORGAN
Massachusetts Supreme Judicial Court, 1989
404 Mass. 537, 536 N.E.2d 587, 8 U.C.C Rep. Serv. 2d 524

O' Connor, J. The defendants, Rose and William Morgan, appeal from a judgment denying them recovery on their counterclaims in an action brought by the plaintiff, Ford Motor Credit Company (Ford Credit), to recover amounts due on an automobile instalment contract and to recover possession of the automobile covered thereby. We affirm the judgment.

The trial judge's findings of fact made in conjunction with Ford Credit's complaint and two counts of the counterclaim may be summarized as follows. On June 27, 1978, the Morgans purchased a new 1978 Mercury Zephyr automobile from Neponset Lincoln Mercury, Inc. (dealer). The Morgans had made several visits to the dealer who assured them that the automobile was reliable and economical. In order to finance their purchase through Ford Credit, the Morgans signed a "Massachusetts Automobile Retail Instalment Contract," a standard printed form contract prepared by Ford Credit. Printed in capital letters at the bottom of the first page of the form was the following statement:

> NOTICE[:] ANY HOLDER OF THIS CONSUMER CREDIT CONTRACT IS SUBJECT TO ALL CLAIMS AND DEFENSES WHICH THE DEBTOR COULD ASSERT AGAINST THE SELLER OF GOODS OR SERVICES OBTAINED PURSUANT HERETO OR WITH THE PROCEEDS HEREOF. RECOVERY HEREUNDER BY THE DEBTOR SHALL NOT EXCEED AMOUNTS PAID BY THE DEBTOR HEREUNDER.

Section 19 of the contract requires purchasers to procure and maintain insurance on the vehicle at their own expense, "for so long as any amount remains unpaid" under the contract.

Ford Credit financed the automobile for $3,833. Payment was to be in thirty-six consecutive monthly instalments of $137.13 each. On July 11, 1978, a certificate of title was issued to Rose Morgan listing Ford Credit as first lienholder. The Morgans drove the automobile for approximately eighteen months, for a distance of over 11,500 miles. During this time, they experienced several problems with the automobile, such as water leaking into the trunk, a faulty head gasket, rust, hood misalignment, and loss of shine. Their greatest complaint was that, when left unattended, the transmission would shift from "park" to "reverse," and would have to be shifted back to "park" before the vehicle could be started.

During the fall of 1979, the Morgans began having financial difficulty, and missed their monthly automobile payments for November and December. Before January 1, 1980, William Morgan rented a garage in which he concealed the automobile. He removed the battery and removed or deflated the tires. He also failed to renew his insurance for 1980. In January, Ford Credit notified the Morgans that they were in default on the credit contract and requested that the default be cured by February 6, 1980. The Morgans made no further payments. To that time, they had made fifteen of their monthly payments totalling $2,056.95. The Morgans continued to hide their automobile for approximately two months after the court issued a surrender order. As a result, William Morgan received what the trial judge termed a "well earned" contempt judgment, which Morgan subsequently purged by surrendering the vehicle. The court later authorized Ford Credit to sell the vehicle. William Morgan successfully moved to delay the sale of the vehicle pending inspection, examination and testing. By the time it was inspected, it had been extensively vandalized and was a total loss. The loss was not recoverable due to the Morgans' failure to obtain insurance for 1980.

Ford Credit sought recovery of $2,628.87 plus costs and attorney's fees. The Morgans counterclaimed in three counts, each of which is predicated on the theory, which we reject, that as assignee of the contract, Ford Credit stands fully in the same position as the assignor-dealer, and thus any wrongful acts of the dealer are fully attributable to, and may provide the basis of affirmative recovery from, Ford Credit. The first count alleged the dealer's fraud and deceit in making false representations to the Morgans on which they relied. The second count alleged a G.L. c.93A, §2 (1986 ed.), violation for unfair and deceptive practices. The third count was for the dealer's breach of express and implied warranties of merchantability and fitness for a particular purpose. The Morgans sought $7,061.68 in damages on each of the counts, and damages treble that amount under counts I and II.

Count I, except for damages, was submitted to a jury on special questions. The jury found that the dealer knowingly made false representations to the Morgans, on which the Morgans relied. Thereafter, the judge heard the complaint and counts II and III of the counterclaim without jury. The judge determined that the jury's special verdict provided the Morgans with a valid defense against Ford Credit's collection claim, but that the Morgans were not entitled to damages on any count of their counterclaim. The judge entered judgment for the Morgans on Ford Credit's complaint, and for Ford Credit on each of the counterclaims. The Morgans appealed to the Appeals Court, claiming that the judge erred in allowing their counterclaims to be used only defensively to extinguish Ford Credit's claim for the balance due on the credit contract. They also contend that the jury should have been permitted to assess damages as to counts I and III. We transferred the case to this court on our own initiative.

The Morgans' first contention is that the explicit language of the notice provision contained in the contract, which subjects holders to all "claims and defenses which the debtor could assert against the seller" permits them to recover affirmatively from Ford Credit for the dealer's wrongdoing. As the Morgans acknowledge, that notice provision is mandated by a Federal Trade Commission (FTC) rule which provides that it is an unfair or deceptive act or practice to take or receive a consumer credit contract which fails to include that provision. 16 C.F.R. §433.2 (1978). Therefore, we look to the FTC's purpose in enacting the rule as a guide to our interpretation of the contract provision.

The rule was designed to preserve the consumer's claims and defenses by cutting off the creditor's rights as a holder in due course.[2] Federal Trade Commission, Preservation of Consumers' Claims and Defenses, Final Regulation, Proposed Amendment and Statement of Basis and Purpose, 40 Fed. Reg. 53505, 53524 (Nov. 18, 1975) (to be codified at 16 C.F.R. §433). See Thomas v. Ford Motor Credit Co., 48 Md. App. 617, 622 (1981). Under the holder in due course principle, which would apply were it not for the contract provision mandated by the FTC rule, the creditor could "assert his right to be paid by the consumer despite misrepresentation, breach of warranty or contract, or even fraud on the part of the seller, and despite the fact that the consumer's debt was generated by the sale." 40 Fed. Reg. at 53507. Thus, "[being] prevented from asserting the seller's breach of warranty or failure to perform against the assignee of the consumer's instrument, the consumer [would lose] his most effective weapon nonpayment." Id. at 53509. Eliminating holder in due course status prevents the assignee from demanding further payment when there has been assignor wrongdoing, and rearms the consumer with the "weapon" of nonpayment.[3]

The FTC anticipated that in addition to nonpayment, affirmative recovery, that is, a judgment for damages against the assignee-creditor,

2. The FTC rule operates as follows. The required language that the assignee takes the contract "subject to" the consumer's claims and defenses against the seller places an express condition on the consumer's promise to pay a sum certain, thus destroying the negotiability precedent to an assignee's having holder in due course status. J. J. White & R. S. Summers, Uniform Commercial Code §14-8, at 722 (3d ed. 1988). Thomas, supra at 622. "It is as though the note said the following: 'The promise to pay embodied by this note is conditioned upon the absence of any valid defense in the hands of the maker.'" White & Summers, supra at 723. The language operates not due to any statute or regulation, but to the effect the notice has when it becomes part of the contract. Thomas, supra at 622. H. J. Alperin & R. F. Chase, Consumer Rights and Remedies §280 (1979 & Supp. 1988).

3. Merely raising a valid claim does not fully insulate the consumer from payments due if the value of the claim is less than payments outstanding. "Laymen, particularly automobile dealers, are wont to complain that under the rule any microscopic defect in the goods will give the buyer a right to quit paying, return the goods, and demand his money back. This is not an accurate statement of the law. . . . [M]ost defects in the underlying transaction do not give the buyer the right to stop paying entirely." White & Summers, supra at 729-730. However, in the present case, Ford Credit does not contest the judge's determination that the Morgans may raise their valid claim for fraud and deceit against the dealer as a complete defense to further payment.

would be available in limited circumstances. Thus, in its statement o: policy and purpose, the FTC spelled out the avenues of relief under the rule as follows: "[A] consumer can (1) defend a creditor suit for paymen of an obligation by raising a valid claim against a seller as a set-off, anc (2) maintain an affirmative action against a creditor who has receivec payments for a return of monies paid on account." 40 Fed. Reg. at 53524 However, the FTC made clear that "[t]he latter alternative will onl be available where a seller's breach is so substantial that a court i persuaded that rescission and restitution are justified. The most typica example of such a case would involve non-delivery, where delivery wa scheduled after the date payments to a creditor commenced." Id. The FTC re-emphasized this point in stating, "[c]onsumers will not be in a posi tion to obtain an affirmative recovery from a creditor, unless they have actually commenced payments and received little or nothing of value from the seller. In a case of non-delivery, total failure of performance, o the like, we believe the consumer is entitled to a refund of monies paic on account." Id. at 53527. Finally, the FTC anticipated that the rule woulc enable the courts to weigh the equities in the underlying sale, anc "remain the final arbiters of equities between a seller and a consumer." Id. at 53524. Thus, the function of the rule is to allow consumers to sto payments, and, in limited circumstances, not present here, where equit requires, to provide for a return of monies paid. The FTC did not intenc that the rule would, as a matter of course, entitle a consumer to a ful refund of monies paid on account.[4] It follows, of course, that there is nc merit to the Morgans' assertions that the contractual language allow them affirmative recovery even beyond the amount they paid in. To expose a creditor to further affirmative liability would not only contra vene the intention of the FTC, but would "place the creditor in the posi tion of an absolute insurer or guarantor of the seller's performance." Home Sav. Ass'n v. Guerra, 733 S.W.2d 134, 136 (Tex. 1987). Michelir Tires (Canada) Ltd. v. First Nat'l Bank, 666 F.2d 673, 679-680 (1st Cir 1981). This we decline to do.

The Morgans do not quarrel with the judge's conclusion that, in the circumstances, they had no right to rescind the sale. Further, they do no argue that they received little or nothing of value from the dealer. We do no imply that such an argument would have been appropriate. However, absen such a showing, and absent any support for the argument that the language in the contract should receive any interpretation other than the one the FTC

4. The cases addressing affirmative recovery go no further than to hold that affirma tive recovery is available up to the amounts paid in by the debtor. None has addressed the question whether a showing of rescission and restitution is a necessary precedent to sucl recovery. In each of the cases, it is arguable that the goods received were valueless. Home Sav. Ass'n v. Guerra, 733 S.W.2d 134 (Tex. 1987) (rock siding installed crumbled). Thomas v Ford Motor Credit Co., 48 Md. App. 617 (1981) (car argued to be "valueless"). Hempstead Bank v. Babcock, 115 Misc. 2d 97 (N.Y. Sup. Ct. 1982) (solar heating system "neve worked"). Tinker v. DeMaria Porsche Audi, Inc., 459 So. 2d 487 (Fla. App. 1984) (car "totall inoperable").

intended it to have, the Morgans' contention that the language mandated by 16 C.F.R. §433.2, affords them a right to affirmative recovery is without merit.[5]

The Morgans also argue that Article 9 of the Uniform Commercial Code, G.L. c.106, §9-318(1) (1986 ed.)[now §9-404 — Eds.] lends statutory support to their claim for affirmative recovery. That section provides:

> Unless an account debtor has made an enforceable agreement not to assert defenses or claims arising out of a sale as provided in section 9-206 the rights of an assignee are subject to (a) all the terms of the contract between the account debtor and assignor and any defense or claim arising therefrom; and (b) any other defense or claim of the account debtor against the assignor which accrues before the account debtor receives notification of the assignment.

This court has never addressed the question whether the statute enables a consumer to recover affirmatively against an assignee-creditor.

There is nothing in §9-318 which suggests that such affirmative recovery is appropriate. As the First Circuit noted in *Michelin Tires (Canada) Ltd.*, supra at 677, "[t]he key statutory language is ambiguous. That 'the rights of an assignee are *subject to* . . . (a) all the terms of the contract' connotes only that the assignee's rights to recover are limited by the obligor's rights to assert contractual defenses as a set-off, implying that affirmative recovery against the assignee was not intended. . . . The words 'subject to,' used in their ordinary sense, mean 'subordinate to,' 'subservient to,' or 'limited by.' There is nothing in the use of the words 'subject to,' in their ordinary sense, which would even hint at the creation of affirmative rights." While the First Circuit recognized that the use of the word "claim" appears to contemplate affirmative recovery, the court noted that the title of §9-318, "Defenses Against Assignee," and the Official Comment to this provision of the Uniform Commercial Code argue otherwise. Id. at 677-678. The Morgans attempt to distinguish *Michelin* on the ground that *Michelin* involved a suit against a creditor-bank which was a nonparticipating assignee, whereas here, as the judge found, the creditor knowingly participated in or was directly connected with the consumer sale. However, beyond making this factual distinction, the Morgans do not argue why the First Circuit's interpretation of the statute in *Michelin* should not extend to cases involving a participatory assignee, and no such reason is otherwise apparent. Moreover, G.L. c.255, §12F, suggests

5. We do not hold that a consumer may only assert his rights defensively in response to a claim initiated by an assignee for balance due on the contract. This would be in clear contravention of the FTC's intention. 40 Fed. Reg. at 53526. Eachen v. Scott Hous. Sys., Inc., 630 F. Supp. 162, 164-165 (M.D. Ala. 1986). "Under such circumstances the financer may elect not to sue, in the hopes that the threat of an unfavorable credit report may move the consumer to pay." 40 Fed. Reg. at 53527. Therefore, it is clear that the account debtor may initiate suit to enforce his right, however limited it may be, to discontinue credit payments. See *Eachen,* supra at 164-165; Tinker v. DeMaria Porsche Audi, Inc., supra at 492-493.

otherwise. That statute applies where the proceeds of a loan are used for a consumer purchase, and the creditor and seller are closely related. General Laws c.255, §12F, provides only that the creditor is "subject to all of the defenses of the borrower" arising from the sale or lease. Thus, to read §9-318 to allow affirmative recovery where a creditor and seller are closely connected would contradict the Legislature's later enactment c.255, §12F. . . .

We conclude that in the circumstances of this case, the judge was correct in ruling that the Morgans were not entitled to affirmative recovery against Ford Credit. Thus, error, if any, that may have occurred in reference to counts II and III of the counterclaim was harmless. The Morgans were entitled to no more than a judgment in their favor on Ford Credit's original claim as ordered by the judge. Judgment affirmed.

NOTE ON DEBTOR'S RIGHT TO SEEK AFFIRMATIVE RELIEF

Is this case right? While there are cases agreeing with the decision, see Mardis v. Ford Motor Cred. Co., 642 So. 2d 701 (Ala. 1994), many courts addressing the issue have found that the clear language of the FTC legend creates an affirmative cause of action against the assignee without the necessity of proving a substantial ground for rescission o the underlying contract. See Lozada v. Dale Baker Oldsmobile, Inc., 91 F. Supp. 2d 1087 (W.D. Mich.2000); Maberry v. Said, 911 F. Supp. 139 (D. Kan. 1995); Milchen v. Bob Morris Pontiac-GMC Truck, 113 Ohio App. 3d 190 (1996); Oxford Fin. Co. v. Velez, 807 S.W.2d 460 (Tex. App 1991).

B. *Setoff and Recoupment*

Problem 191

Joseph Armstrong signed the usual contract with Wonder Spa. I contained the required FTC legend preserving his ability to assert defense against assignees. The spa assigned his contract to Nightflyer Finance Company, which notified Armstrong that in the future he should make payment directly to it. Two weeks later one of the instructors at the sp negligently dropped a barbell on Armstrong's foot. May he subtract the doctor's bills from the payment to Nightflyer? What if the sole owner o the spa was driving around town in the spa's car and accidentally ran ove Armstrong's dog? May Armstrong subtract the value of the dog from th payments due to Nightflyer? Does your answer to this last question chang if the dog were already dead before Armstrong learned of the assignmen of his contract to the finance company? To answer these questions, se UCC §9-404.

SEATTLE-FIRST NATIONAL BANK v. OREGON PACIFIC INDUSTRIES

Supreme Court of Oregon, 1972
262 Or. 578, 500 P.2d 1033

DENECKE, J. The plaintiff bank obtained a judgment against the defendant for the amount of an invoice assigned to the bank by Centralia Plywood. The trial court denied defendant's right to a setoff and defendant appeals.

The issue is the interpretation of the assignment section of the secured transactions chapter of the Uniform Commercial Code (ORS 79.3180).

On December 12, 1968, the defendant purchased plywood from Centralia. Centralia assigned the invoice evidencing the purchase to the bank on December 13, and the bank notified the defendant of the assignment. The defendant refused payment and the bank brought this action.

The defendant argues that it has a setoff against the bank's claim. Prior to the bank's assignment the defendant had placed two plywood orders, not included in the assigned invoice, with Centralia. Delivery was never made by Centralia and defendant contends it can set off the damages it suffered thereby against the bank's claim.

Centralia Plywood was insolvent when it assigned the invoice to the bank on December 12 and the bank knew of the insolvency at that time. Both Centralia and the bank are nonresidents. The defendant contends that because of these circumstances it is entitled to the setoff and cites our opinion in Pearson v. Richards, 106 Or. 78, 92, 211 P. 167 (1922), in support.

Assuming defendant's contention is correct in cases not involving the Code, we hold the principle contended for by defendant is not applicable when the Code applies. ORS 79.3180(1) provides:

> [T]he rights of an assignee are subject to:
> (a) All the terms of the contract between the account debtor and assignor and any defense or claim arising therefrom; and
> (b) Any other defense or claim of the account debtor against the assignor which accrues before the account debtor receives notification of the assignment.

The Code does not expressly provide that a claim can be set off if the assignor was insolvent at the time of the assignment and the assignee had knowledge of this fact or because the assignor and assignee are nonresidents.

One of the prime purposes of the Code was to create a statutory scheme incorporating within its provisions the complete regulation of certain types of commercial dealings. This purpose would be blunted if the rules created by some pre-code decisions and not expressly provided for in the statutory scheme were nevertheless grafted onto the Code by implication. In Evans Products v. Jorgensen, 245 Or. 362, 372, 421 P.2d 978 (1966), we held generally that we would not engage in this practice.

We recently observed in Investment Service Co. v. North Pacific Lbr. Co., Or., 492 P.2d 470-471 (1972), that the comment to this section of the Code states that this section "makes no substantial change in prior law." Upon further examination, we must acknowledge that while the Code retains the essence of the previous law of assignments, the Code has, by specific language, changed some of the details of the previous law of assignments.

The Code distinguishes "between what might be called the contract-related and the unrelated defenses and claims. Defenses and claims 'arising' from the contract can be asserted against the assignee whether they 'arise' before or after notification. . . . Under the Code, 'any other defense or claim' is available against the assignee only if it 'accrues before . . . notification.' " 2 Gilmore, Security Interests in Personal Property, 1090-1091, §41.4 (1965).

The setoff or claim the defendant seeks to assert is an unrelated setoff because it arises out of a breach of a contract not connected with the invoice assigned to the bank. For this reason the defendant can assert the setoff only if it accrued before the defendant was notified of Centralia's assignment to the bank.

The controversy thus narrows down to the issue of whether the setoff "accrued" to the defendant before it received notice of the assignment. We could be aided in defining "accrued" if we could determine why the accrual of the setoff was selected as the cutoff event. Accruing of the setoff, however, apparently, was selected arbitrarily. The choice of the event of the accrual was based upon previous decisions, some of which used the phrase "matured" rather than "accrued" claim. 4 Corbin, Contracts, 599, §897 (1951). 1 Restatement 211, Contracts §167(1), provided that the obligor could assert its setoff if the setoff was "based on facts arising . . . prior to knowledge of the assignment by the obligor."

It was necessary to permit at least some setoffs to be asserted in order to protect the obligor from being unduly prejudiced by the assignment; but this right of setoff had to be limited in order to give some value and stability to the assignment so that it could be used as an effective security device. If an obligor could not assert any of the defenses or setoffs against an assignee which he could have asserted against his creditor, the assignor, the obligor would be extremely prejudiced by an assignment. On the other hand, if the obligation assigned could be obliterated or diminished by events happening after the assignment and notice of assignment to the obligor, the assignment would be precarious collateral.

The comments to the Oregon Code are of no assistance in interpreting "accrue." The comments to the Washington Code state: "The term 'accrues' appears to mean that the 'claim' shall exist as such, i.e., as a cause of action, before such knowledge." RCWA 62A.9-318, p.439.

"Accrue," aside from its fiscal use, generally is used in the law to describe when a cause of action comes into being. Its chief use is to determine when the statute of limitations commences. We believe it is advisable to use "accrue" in the Code in its usual sense; that is, a claim or setoff accrues when a cause of action exists.

The parties stipulated that the "breaches of contract [the failure to deliver by Centralia] occurred on or about January 3, 1969." Therefore the claim "accrued" at that time. Since the claim accrued after defendant had notification of the assignment, the setoff cannot be asserted successfully.

Defendant on appeal contends that by stipulating that the breaches of contract occurred on January 3 it did not intend to stipulate that the cause of action accrued at that time. The normal inference is that the cause of action accrues at the time the breach of contract occurs. In addition, the record indicates that the trial court and the parties so understood the import of the stipulation.

Affirmed.

QUESTION

The subtraction process that a debtor engages in when paying a creditor varies in terminology depending on the nature of the debt subtracted. If the debtor is relying on damages that arose from the *same* transaction, the subtraction process is called a *recoupment.* If the damages arose from a transaction *unrelated* to the assigned contract, the process is called a *setoff* (bankers, perversely, call it "offset"). Which was which in the last Problem?

C. *Modifications*

Problem 192

Prester John made maps for a living and sold them to National Auto Club. It was agreed that he would receive $5,000 for each map he produced under the contract. Needing money, Prester John went to Medieval National Bank and borrowed $30,000, assigning to the bank the payments due to him from National Auto Club. The quality of his maps was not as good as the parties had originally contemplated, and National Auto Club threatened to cancel and sue. Prester John agreed to accept $4,000 for each map, but Medieval National Bank protested this change. Is the bank bound by the modification in the contract? See UCC §9-405.

VI. WARRANTIES BY THE ASSIGNOR

RESTATEMENT (SECOND) OF CONTRACTS

§333. Warranties of an Assignor

(1) Unless a contrary intention is manisfested, one who assigns or purports to assign a right by assignment under seal or for value warrants to the assignee

(a) that he will do nothing to defeat or impair the value of the assignment and has no knowledge of any fact which would do so;
(b) that the right, as assigned, actually exists and is subject to no limitations or defenses good against the assignor other than those stated or apparent at the time of the assignment;
(c) that any writing evidencing the right which is delivered to the assignee or exhibited to him to induce him to accept the assignment is genuine and what it purports to be.

(2) An assignment does not of itself operate as a warranty that the obligor is solvent or that he will perform his obligation.

(3) An assignor is bound by affirmations and promises to the assignee with reference to the right assigned in the same way and to the same extent that one who transfers goods is bound in like circumstances.

(4) An assignment of a right to a sub-assignee does not operate as an assignment of the assignee's rights under his assignor's warranties unless an intention is manifested to assign the rights under the warranties.

VII. DELEGATION OF DUTIES

LANGEL v. BETZ
Court of Appeals of New York, 1928
250 N.Y. 159, 164 N.E. 890

POUND, J. Plaintiff, on August 1, 1925, made a contract with Irving W. Hurwitz and Samuel Hollander for the sale of certain real property. This contract the vendees assigned to Benedict, who in turn assigned it to Isidor Betz, the defendant herein. The assignment contains no delegation to the assignee of the performance of the assignor's duties. The date for performance of the contract was originally set for October 2, 1925. This was extended to October 15, 1925, at the request of the defendant, the last assignee of the vendees. The ground upon which the adjournment was asked for by defendant was that the title company had not completed its search and report on the title to the property. Upon the adjourned date the defendant refused to perform. The vendor plaintiff was ready, able, and willing to do so, and was present at the place specified with a deed, ready to tender it to the defendant, who did not appear.

The plaintiff as vendor brought this action against the defendant assignee for specific performance of the contract. Upon the foregoing undisputed facts he has had judgment therefor.

The question is: "Can the vendor obtain specific performance of a contract for the sale of real estate against the assignee of the vendee where the assignee merely requests and obtains an extension of time within which to close title?"

Here we have no novation, no express assumption of the obligations of the assignor in the assignment, and no demand for performance by the assignee.

The mere assignment of a bilateral executory contract may not be interpreted as a promise by the assignee to the assignor to assume the performance of the assignor's duties, so as to have the effect of creating a new liability on the part of the assignee to the other party to the contract assigned. The assignee of the vendee is under no personal engagement to the vendor where there is no privity between them. Champion v. Brown, 6 Johns. Ch. 398, 10 Am. Dec. 343; Anderson v. New York & H.R. Co., 132 App. Div. 183, 187, 188, 116 N.Y.S. 954; Hugel v. Habel, 132 App. Div. 327, 328, 117 N.Y.S. 78. The assignee may, however, expressly or impliedly, bind himself to perform the assignor's duties. This he may do by contract with the assignor or with the other party to the contract. It has been held (Epstein v. Gluckin, 233 N.Y. 490, 135 N.E. 861) that, where the assignee of the vendee invokes the aid of a court of equity in an action for specific performance, he impliedly binds himself to perform on his part and subjects himself to the conditions of the judgment appropriate thereto. "He who seeks equity must do equity." The converse of the proposition, that the assignee of the vendee would be bound when the vendor began the action, did not follow from the decision in that case. On the contrary, the question was wholly one of remedy rather than right, and it was held that mutuality of remedy is important only so far as its presence is essential to the attainment of the ends of justice. This holding was necessary to sustain the decision. No change was made in the law of contracts nor in the rule for the interpretation of an assignment of a contract.

A judgment requiring the assignee of the vendee to perform at the suit of the vendor would operate as the imposition of a new liability on the assignee which would be an act of oppression and injustice, unless the assignee had, expressly or by implication, entered into a personal and binding contract with the assignor or with the vendor to assume the obligations of the assignor.

It has been urged that the probable intention of the assignee is ordinarily to assume duties as well as rights, and that the contract should be so interpreted in the absence of circumstances showing a contrary intention. The American Law Institute's Restatement of the Law of Contracts (section 164) proposes a change in the rule of interpretation of assigned contracts to give as full effect to the assumed probable intention of the parties as the law permits. The following statement is proposed:

Section 164 Interpretation of Words Purporting to Assign a Bilateral Contract and Effect of Acceptance of the Assignment by the Assignee

(1) Where a party to a bilateral contract which is at the time wholly or partially executory on both sides, purports to assign the whole contract, his action is interpreted, in the absence of circumstances showing a contrary intention, as an assignment of the assignor's rights under the contract and a delegation of the performance of the assignor's duties.

(2) Acceptance by the assignee of such an assignment is interpreted, in the absence of circumstances showing a contrary intention, as both as assent

to become an assignee of the assignor's rights and as a promise *to the assignor to assume the performance of the assignor's duties.*

This promise to the assignor would then be available to the other party to the contract. Lawrence v. Fox, 20 N.Y. 268; 1 Williston on Contracts, §412. The proposed change is a complete reversal of our present rule of interpretation as to the probable intention of the parties. It is, perhaps, more in harmony with modern ideas of contractual relations than is "the archaic view of a contract as creating a strictly personal obligation between the creditor and debtor" (Pollock on Contracts [9th ed.] 232), which prohibited the assignee from suing at law in his own name and which denied a remedy to third party beneficiaries. "The fountains out of which these resolutions issue" have been broken up if not destroyed (Seaver v. Ransom, 224 N.Y. 233, 237, 120 N.E. 639, 2 A.L.R. 1187), but the law remains that no promise of the assignee to assume the assignor's duties is to be inferred from the acceptance of an assignment of a bilateral contract, in the absence of circumstances surrounding the assignment itself which indicate a contrary intention.

With this requirement of the interpretation of the intention of the parties controlling we must turn from the assignment to the dealings between the plaintiff and the defendant to discover whether the defendant entered into relations with the plaintiff whereby he assumed the duty of performance. The assignment did not bring the parties together, and the request for a postponement differs materially from the commencement of an action in a court of equity, whereby the plaintiff submits himself to the jurisdiction of the court or from a contractual assumption of the obligations of the assignor. If the substance of the transaction between the vendor and the assignee of the vendee could be regarded as a request on the part of the latter for a postponement of the closing day and a promise on his part to assume the obligations of the vendee if the request were granted, a contractual relation arising from an expression of mutual assent, based on the exchange of a promise for an act, might be spelled out of it; but the transaction is at least as consistent with a request for time for deliberation as to the course of conduct to be pursued as with an implied promise to assume the assignor's duties if the request were granted. The relation of promisor and promisee was not thereby expressly established, and such relation is not a necessary inference from the nature of the transaction. When we depart from the field of intention and enter the field of contract, we find no contractual liability; no assumption of duties based on a consideration.

Plaintiff contends that the request for an adjournment should be construed (time not being the essence of the contract) as an assertion of a right to such adjournment, and therefore as a binding act of enforcement whereby defendant accepted the obligations of the assignee. Here again we have an equivocal act. There was no demand for an adjournment as a matter of right. The request may have been made without any intent to assert a right. It cannot be said that by that act alone the assignee assumed the duty of performance.

Furthermore, no controlling authority may be found which holds tha a mere demand for performance by the vendee's assignee creates a righ in the complaining vendor to enforce the contract against him. H.&H. Corporation v. Broad Holding Corporation, 204 App. Div. 569, 198 N.Y.S. 763. See 8 Cornell L.Q., 374; 37 Harv. L. Rev., 162. That question may be reserved until an answer is necessary.

The judgment of the Appellate Division and that of the Special Term should be reversed and the complaint dismissed, with costs in all courts.

Judgments reversed, etc.

QUESTIONS

1. Read UCC §2-210(5). Section 328 of the Restatement (Second) of Contracts is similar to the UCC provision. It states:

> (1) Unless the language or the circumstances indicate the contrary, as in an assignment for security, an assignment of "the contract" or of "all my rights under the contract" or an assignment in similar general terms is an assignment of the assignor's rights and a delegation of his unperformed duties under the contract.
>
> (2) Unless the language or the circumstances indicate the contrary, the acceptance by an assignee of such an assignment operates as a promise to the assignor to perform the assignor's unperformed duties, and the obligor of the assigned rights is an intended beneficiary of the promise.
>
> *Caveat:* The Institute expresses no opinion as to whether the rule stated in subsection (2) applies to an assignment by a purchaser of his rights under a contract for the sale of land.

What is the status of *Langel* under the Restatement section? See Kunzman v. Thorsen, 303 Or. 600, 740 P.2d 754 (1987).

2. In the opinion at one point the court cites to Lawrence v. Fox, the famous third party beneficiary case that began the last chapter. What is the relevance of that citation in this delegation of duty case?

Problem 193

When ballet star Vera Toes suddenly got the chance to dance the part of Pat Nixon in the new ballet called *Watergate,* she was thrilled and quickly signed the contract with the Wilma Arts Dance Company. A week before rehearsals were to begin, the State Department asked Vera if she would be willing to tour South America as part of a cultural exchange program. She decided that helping her government was more important than the Watergate show, so she called her good friend Carla Pas de Deux and they agreed that Carla would assume her obligation to the dance company. Then Vera phoned Wilma Arts, president of the organization, and received her permission to substitute Carla in her stead. Vera went off to Russia on the tour, but Carla never honored her agreement to appear in *Watergate.* When the dance company threatened suit, Carla replied that any contract she had was with Vera and not the Wilma Arts Dance

Company. Is Vera liable here to the dance company? Is Carla? What are the legal theories involved?

ROUSE v. UNITED STATES
United States Court of Appeals, D.C. Circuit, 1954
215 F.2d 872

EDGERTON, Circuit Judge. Bessie Winston gave Associated Contractors, Inc., her promissory note for $1,008.37, payable in monthly installments of $28.01, for a heating plant in her house. The Federal Housing Administration guaranteed the note and the payee endorsed it for value to the lending bank, the Union Trust Company.

Winston sold the house to Rouse. In the contract of sale Rouse agreed to assume debts secured by deeds of trust and also "to assume payment of $850 for heating plant payable $28 per Mo." Nothing was said about the note.

Winston defaulted on her note. The United States paid the bank, took an assignment of the note, demanded payment from Rouse, and sued him for $850 and interest.

Rouse alleged as defenses (1) that Winston fraudulently misrepresented the condition of the heating plant and (2) that Associated Contractors did not install it satisfactorily. The District Court struck these defenses and granted summary judgment for the plaintiff. The defendant Rouse appeals.

Since Rouse did not sign the note he is not liable on it. D.C. Code 1951, §28-119; N.I.L. Sec. 18. He is not liable to the United States at all unless his contract with Winston makes him so. The contract says the parties to it are not "bound by any terms, conditions, statements, warranties or representations, oral or written" not contained in it. But this means only that the written contract contains the entire agreement. It does not mean that fraud cannot be set up as a defense to a suit on the contract.[1] Rouse's promise to "assume payment of $850 for heating plant" made him liable to Associated Contractors, Inc., only if and so far as it made him liable to Winston; one who promises to make a payment to the promisee's creditor can assert against the creditor any defense that the promisor could assert against the promisee.[2] Accordingly Rouse, if he had been sued by the corporation, would have been entitled to show fraud on the part of Winston. He is equally entitled to do so in this suit by an assignee of the corporation's claim. It follows that the court erred in striking the first defense. We do not consider whether Winston's alleged fraud, if shown, would be a complete or only a partial defense to this suit, since that question has not arisen and may not arise.

We think the court was right in striking the second defense. "If the promisor's agreement is to be interpreted as a promise to discharge

1. 3 Williston, Contracts §811A (rev. ed. 1936).
2. 2 id. §394.

whatever liability the promisee is under, the promisor must certainly be allowed to show that the promisee was under no enforceable liability. . . . On the other hand, if the promise means that the promisor agrees to pay a sum of money to A, to whom the promisee says he is indebted, it is immaterial whether the promisee is actually indebted to that amount or at all. . . . Where the promise is to pay a specific debt . . . this interpretation will generally be the true one."[3]

The judgment is reversed and the cause remanded with instructions to reinstate the first defense.

Reversed and remanded.

3. 2 id. §399.

TABLE OF CASES

Principal cases are italicized.

INDEX