1962

Sales and Secured Transactions

Douglass Boshkoff

*Indiana University Maurer School of Law*

Follow this and additional works at: [https://www.repository.law.indiana.edu/facpub](https://www.repository.law.indiana.edu/facpub)

Part of the Commercial Law Commons, Secured Transactions Commons, and the Torts Commons

**Recommended Citation**

Boshkoff, Douglass, "Sales and Secured Transactions" (1962). *Articles by Maurer Faculty*. 1022. [https://www.repository.law.indiana.edu/facpub/1022](https://www.repository.law.indiana.edu/facpub/1022)

This Article is brought to you for free and open access by the Faculty Scholarship at Digital Repository @ Maurer Law. It has been accepted for inclusion in Articles by Maurer Faculty by an authorized administrator of Digital Repository @ Maurer Law. For more information, please contact rvaughan@indiana.edu.
SALES AND SECURED TRANSACTIONS

DOUGLASS G. BOSHKOFF†

I

IMPLIED WARRANTY AND PRIVITY

BEFORE discussing a recent decision concerned with warranty liability, it is advisable to review a 1958 opinion in the same area, Spence v. Three Rivers Builders & Masonry Supply, Inc.,¹ in which lack of privity as a defense was raised. In the Spence case, plaintiff claimed breach of an implied warranty arising out of the sale of some defective cinder blocks, and she did not alternatively allege negligence, although it turned out that the evidence at trial would have supported recovery on a negligence theory. On appeal, the defendant, a remote vendor, argued that lack of privity was a bar to the warranty action. Justice Voelker, writing for the majority, found the Michigan authorities on the relationship between warranty, negligence, and privity quite confusing, and then compounded the confusion by holding that this particular plaintiff could recover, while making the following comments:

We observe—and the defendant seeks to make much of the fact—that the declaration in the present action is not in terms grounded upon negligence of the defendant, although certain of the proofs, as already indicated, tend rather clearly to show its negligence. We also find that in Michigan—whatever the rule may be elsewhere—there is authority for treating actions of this kind based upon implied warranty by the manufacturer as though they were explicitly grounded upon negligence.

Thus we said in Hertzler v. Manshun, 228 Mich. 416, 423 (although we limited our remark to foodstuffs):

"The implied warranty, so-called, reaching from the manufacturer of foodstuffs to the ultimate purchaser for immediate consumption is in the nature of a representation that the highest degree of care has been exercised and a breach of such duty inflicting personal injury is a wrong in the nature of a tort and not a mere breach of contract to be counted on in assumpsit. Except in name and to establish privity between the manufacturer and the ultimate consumer it is the same thing as negligence. Plaintiff's case, in its last analysis, is bottomed on negligence. (Italics added.)"

Again in Ebers v. General Chemical Co., 310 Mich. 261, 275, we stated (in countenancing recovery by a remote vendee against the manufacturer of a defective insecticide for peach trees), "Although plaintiff claims under the theory of an implied warranty, the real question is

† Visiting Associate Professor, Indiana University School of Law; Member of the Michigan and New York Bars.

¹. 353 Mich. 120, 90 N.W.2d 873 (1958).

181
whether or not defendant was negligent." We then proceeded to quote approvingly the language just quoted from Hertzler.

Whether this notion only adds to the confusion or is any sounder legal reasoning than some of the other things we have said in the past in this area may be open to some dispute, but if we have thus soundly told litigants and their counsel that suing for a breach of an implied warranty is in effect tantamount to suing for negligence (one might think, for one thing, that the burden of proof might in some cases be more onerous on the plaintiff in the latter situation) we lack the heart to banish this plaintiff in this case because she trustingly took us at our word. We suggest in the future, however, that, where warranted by the circumstances, such declarations should sound explicitly in negligence as well as for claimed breach of warranty.2

Commentators have indicated some division of opinion as to the meaning of this language.3 The case of Manzoni v. Detroit Coca-Cola Bottling Co.4 provided an opportunity for clarification of the court's position but, unfortunately, the opportunity was not taken.

Manzoni was an action for breach for implied warranty resulting from the presence of mold in a coca-cola bottle. The defendant did not urge lack of privity as a defense since even before Spence it was admitted that this defense was not a bar where the offending product was food.5 However, defendant's counsel relied specifically on the

---

2. 353 Mich. at 130-131, 90 N.W.2d at 878-879.
3. No matter what legal tools the courts may use, it is clear that their primary concern is with clipping away an artificial concept.... Without employing casuistical argument, Spence has discarded nonliability in the absence of privity because it is no longer a just rule of law.


One leading authority feels that because of ... [the] strong tortious element, a convincing argument can be made for removing the "privity" rule in actions on implied warranty. Consequently, the similarity of the actions, added to the expense involved in re-litigating the case, and the possibility that the defenses of the statute of limitations or res judicata would be raised to bar a new action may have persuaded the court in ... [the] instant case to cut through the preventative form for the purpose of doing justice.

Note, 34 Notre Dame Law. 149, 151 (1958).

Michigan has for years talked of a "warranty" running with the product to the consumer, but has defined it to mean only a warranty that due care has been used. ... [citations omitted]. In the recent case of Spence v. Three Rivers Builders & Masonry Supply, Inc. ... the court found a "warranty" from the maker of cinder building blocks—and apparently of other products, including food—to the consumer, even in the absence of negligence.

Prosser, The Assault upon the Citadel (Strict Liability to the Consumer), 69 Yale L.J. 1099, 1107 n.54 (1960).

[D]efendant contends that plaintiff cannot recover for breach of an implied warranty because of lack of privity of contract between the parties. There is no doubt that there are authorities supporting this contention of defendant. However, the Supreme Court of Michigan has departed from that rule in [the Spence case]

---

5. Hertzler v. Manshum, 228 Mich. 416, 200 N.W. 155 (1924). The concurring judges in Manzoni felt that the case was controlled by Hertzler and wished to limit discussion to a statement of that point. See 363 Mich. at 243-244, 109 N.W.2d at 923.
language of Justice Voelker, quoted above, and argued that, according to it, the plaintiff would have to show lack of care to establish breach of warranty. In other words, since Justice Voelker thought that warranty was bottomed on negligence with reference to privity, it followed that it was necessary to establish negligence in a warranty action.

The supreme court quickly disposed of this forced argument and affirmed a judgment for the buyer. However, the opinion of Justice Smith is more interesting from the point of view of what it failed to say than for what it said. Spence was cited to the court in a manner which could not help but draw in question its underlying rationale. While there appears in Justice Smith’s opinion a refutation of defendant’s argument, there is no mention of the fact that this argument was bottomed on Spence. In fact, there seems almost to be a deliberate attempt to avoid discussion of that case. It is true that the court twice cites Spence in footnotes, but in both instances the use of the case in no way indicates the court’s opinion on lack of privity as a defense.

All this leaves this writer somewhat in the dark regarding privity as a defense to warranty actions in Michigan. It seems hard to believe that the supreme court is still uncommitted to the view that this defense will no longer be effective in all warranty actions, and yet Justice Smith’s failure to explain the meaning of Spence, in a situation where explanation could be expected, makes one wonder whether silence does not still indicate hesitation. Until this question is resolved, it is necessary to echo Professor Strichartz’s 1958 caveat and caution practitioners to still plead and attempt to prove negligence in every case where privity is factually a problem.

II

SECURED TRANSACTIONS

Recordings of Conditional Sales. By statute in Michigan, conditional sales of goods for the purpose of resale must be recorded in

7. There a discussion of privity in Manzoni which is purely gratuitous. Much of the discussion is an extensive quotation from the landmark case of Hennigsen v. Bloomfield Motors, Inc., 32 N.J. 358, 161 A.2d 69 (1960). During this discussion Spence is cited ambiguously as an example of a products liability case involving cinder blocks. It would have been expected that if the court had believed that Spence should be interpreted as abolishing privity altogether, it would have so noted this fact in the discussion in the case. Later in the opinion, Spence is cited a second time, this time for the proposition that in Michigan recovery can be had either on a theory of negligence or implied warranty. This statement comes directly after a statement that privity has been directly abolished or abolished through the use of fictions in many jurisdictions. Again, the failure to cite Spence as an example of such abolition seems quite significant.
the same manner as chattel mortgages. Failure to record renders the reservation of title void against all but the conditional vendee. In *Pioneer Fin. Co. v. Dart Nat'l Bank*, \(^{10}\) manufacturer had sold to dealer a mobile home under a conditional sales contract. This contract, which we will call Contract No. 1, was assigned to plaintiff who failed to record it. The mobile home was subsequently sold to buyer by dealer under a second conditional sales contract, the dealer assigning Contract No. 2 to defendant. Dealer did not use the proceeds of the retail sale to discharge conditional sales Contract No. 1, and when buyer defaulted the defendant-assignee under Contract No. 2 took possession. Plaintiff-assignee under Contract No. 1 then brought this action of replevin to recover the value of the mobile home. There was a dispute at trial, and on appeal, as to whether Contract No. 2 was a valid conditional sales agreement. Nevertheless, the Michigan Supreme Court refused to inquire into the exact status of the defendant and held that plaintiff was barred from recovery by its failure to comply with the recording statute. Since it was obvious to the court that defendant had been misled by plaintiff's failure to record, \(^{11}\) plaintiff could not succeed in the replevin action.

Retail installment sales of motor vehicles: deficiency judgments. Perhaps the most interesting sales case to come along in many years is *Gersonde Equip. Co. v. Walters*, \(^{12}\) involving an attempted use of suretyship doctrines to avoid the consequences of failure to comply with the statute regulating retail installment sales of motor vehicles. In this case plaintiff had sold defendant a truck on time and had taken a conditional sales note as security for the unpaid balance. Plaintiff endorsed this note, guaranteeing payment, to the Benton Harbor State Bank. When buyer defaulted in his payments, plaintiff-seller made several payments to bank and then took a reassignment of the note and repossessed the truck. A subsequent sale of the truck did not produce a sum equal to the unpaid balance of buyer's debt at the date of default. Plaintiff then sought to recover, in some manner, for the installments which he had paid to the bank.

The Michigan statute regulating retail installment sales on motor vehicles provides that the seller may not recover a deficiency judgment after a sale of the motor vehicle unless the installment sales contract specifically provides for personal liability. \(^{13}\) Seller, in *Gersonde*, did not seek a deficiency recovery as such, but did sue to recover the installments paid to the bank after buyer defaulted and before seller

\(^{10}\) 365 Mich. 455, 113 N.W.2d 775 (1962).

\(^{11}\) 365 Mich. at 458 n.3, 113 N.W.2d at 776 n.3.


reacquired the note. The question presented in this case was whether the statutory prohibition against a deficiency recovery should also lead to a denial of compensation to seller on some suretyship theory. Since there was no provision for personal liability in the note, the majority saw the case as one in which the statutory provision clearly prevented any recovery at all. Dissenting Justices Smith and Souris believed that seller made the payments as a surety and was entitled to reimbursement.

The case presents a difficult problem. To take an extreme situation, suppose that seller had paid the bank the total amount due, then reacquired the note and sold the truck at a loss as in Gersonde. Permitting a recovery of the deficiency on a suretyship theory, absent a provision in the installment sales contract, would provide an easy way around the statutory prohibition. Arguably, this would not be in accord with the statutory purpose, since the payments could be regarded as equivalent to all or part of the deficiency recovery referred to in the statute. On the other hand, denial of recovery in Gersonde case left buyer with the benefit of the use of the truck during the time when seller was making the four payments to the bank and would seem to violate fundamental principles of suretyship and restitution. The resolution of this difficult problem must lie in a close analysis of seller's status as a surety.

Since seller's claim for compensation rested on the existence of a principal-surety relation, the first question to be answered was whether he was in fact a surety. Plaintiff argued that he became a surety through the endorsement of the note to the bank. The majority of justices, citing a statement from American Jurisprudence, were of the opinion that plaintiff could not be a surety because the Negotiable Instruments Law rejected doctrines of suretyship as applied to negotiable instruments. The statement from American Jurisprudence relied upon cases where the NIL was in conflict with the suretyship rule antedating the statute. However, where there is no conflict, the NIL should not control and ordinary suretyship doctrines should apply. Therefore, there appears to be no authority for the propo-

---

15. The cases relied upon by the Am. Jur. text writer involved the question of whether traditional suretyship doctrine on the discharge of sureties was replaced by the NIL. This problem is discussed by Hilpert in Discharge of Latent Sureties on Negotiable Instruments Because of Release or Extension of Time, 50 Yale L.J. 387 (1941). The cases do not support the proposition that suretyship doctrines are abrogated by the NIL where there is no conflict between the two.
16. An endorser is one who signs a negotiable promissory note or bill of exchange otherwise than as maker, drawer, or acceptor. Unless the endorser is the party for whose accommodation the negotiable instrument is executed, the endorser is a surety. Any party to a negotiable instrument may be a surety if he signs for
sition that the NIL rejected all suretyship rules, and because there is no conflict between the NIL and suretyship principals in Gersonde, ordinary suretyship doctrines should apply, thereby, making seller a surety.\textsuperscript{17} The question now is to determine what kind of surety seller was.

In this connection, we should distinguish between consensual and non-consensual sureties. Professor Morton Campbell once wrote in this regard:

Whenever two persons are under obligation or under property liability to a third, who is legally or equitably entitled to but one performance, it is necessary to fix the relation between the first two and thus determine the ultimate incidence of loss. Consensual suretyship exists when there is an understanding between the two persons, express or implied in fact, that one shall bear the loss in the end. If there is no such mutual understanding, a relation must be established in accordance with the requirements of equity and good conscience, and special economic and social interests involved, if any, so that the final imposition of loss will not be left to depend on accidental, capricious, collusive or corrupt action on the part of the third person. If the loss should be born by one alone, the relation may be fittingly described as non-consensual suretyship. . . .\textsuperscript{18}

We will see that although the principles of suretyship seek to accomplish the aims stated above, there are two important differences between consensual and non-consensual suretyship. First, the type of suretyship involved will determine the effect of the statute regulating personal liability on installment sales of motor vehicles. Second, the difference also measures the surety's recovery, if in fact there be any.

In his brief, plaintiff argued:

In the case at bar, it can be argued that plaintiff is a consensual surety since defendant gave him a negotiable note which he might have reason to believe would be negotiated under normal business practice and that plaintiff would thereby become a surety on the note. Consent in advance would be implied from customary business usage. . . .\textsuperscript{19}

the accommodation of another party. The rules pertaining to negotiable instruments determine the right of the parties to them so far as those rules have been codified in the Uniform Negotiable Instruments Law. In other respects the rules of suretyship apply where suretyship exists.

Restatement, Security § 82 comment k (1941).

The surety's obligation is frequently expressed by signing as a party to a negotiable instrument or by signing a writing on a negotiable instrument other than as a party. . . . So far as he is a party on such instrument, his obligation to a holder is determined by the law of negotiable instruments. The rules of suretyship, however, are important in determining the mutual rights and duties of parties to the negotiable instruments where these matters are not controlled by the law of negotiable instruments.

Id. § 83 comment b.

17. Ibid.
If analysis shows that the consensual character of the suretyship is vital, then it seems that this should have been treated as an issue of fact for the lower court to decide. However, none of the supreme court justices found any reason to ask for further findings of fact, or even to consider whether they were necessary. The majority did not deal with the question of whether there was a consensual or non-consensual suretyship relation and the dissenters assumed that the relationship was consensual or that if it was not, it made no difference.20

However, there is a big difference in this case between the consequences of a consensual and a non-consensual suretyship relationship. Defendant is arguing, in essence, that the payment by plaintiff to the bank deprived defendant of something resembling a defense. Essentially, the statute gives buyer the ability to say to the holder of the conditional sales note, "Either hold me on the note or take back the car, but you cannot do both because the statute prevents this in the absence of a stipulation that I should be liable for the deficiency." While we may not admire buyer's ethics, this is the effect of the statute.21 If the surety pays the note, in part or in full, and bank or its successor retakes the car, buyer would be deprived of his chance to force creditor to make an election if he is still obliged to pay the surety for the amounts advanced. His right to force the holder of the note to elect is a valuable one although it is not a complete shield against loss. However, a consensual surety may pay creditor when debtor has a defense and still be entitled to reimbursement. This is because in making the payment such a surety is discharging his primary obligation to creditor and not just acting as one secondarily liable for debtor's obligation. Thus, in our case if bank had retained the car and sold it, surety would still have to pay if the proceeds of the sale were not sufficient to discharge buyer's debt. Buyer would then be obliged to reimburse surety if a consensual suretyship was involved because the original consent of buyer to the suretyship indicated his willingness to incur the risk that he could not effectively force creditor to elect. There also seems to be no policy in the statute which would deny effect to this consequence of the consensual suretyship relation.

20. In his dissenting opinion, Justice Smith stated, "The case would not be different in principle if Walters had borrowed the money from Gersonde for the very purpose of making the payments, or if there had been an express contract between Walters and Gersonde that Gersonde would make the payments and Walters would repay him." 363 Mich. at 64, 109 N.W.2d at 8.

21. Both majority and minority felt compelled to comment on the doctrine of election of remedies as applied to conditional sales contracts. The correct or medieval nature of such doctrine, however, is not an issue in this case and such discussion is wide of the mark. Although the statute may owe some of its provisions to the old election doctrine, it now maintains its vitality as law without regard to the rationality of making the conditional vendor elect.
Should we, however, regard surety as being non-consensual, then he no longer can recover if he pays when buyer has a defense.\textsuperscript{22} The rationale for this rule appears in a comment to section 78 of the Restatement of Restitution.

A person who becomes a surety for another without the other person's consent or fault is not thereby so officious that he is barred from restitution if he discharges the other's duty on the obligation, but he is not entitled to restitution from the other if he makes payment thereon, whether or not in the performance of his own duty, unless he discharges the other from a duty. This is true irrespective of his reasonable belief that the other owed the duty; the other has not benefitted and there is no contractual or other relation between him and the other to support a duty of reimbursement.\textsuperscript{23}

If we regard buyer's right to force bank to elect as being analogous to a defense, then a non-consensual surety's act should not be able to prejudice the right to this election. Therefore, the question of whether the suretyship was consensual or non-consensual becomes quite important.

This distinction is also important in connection with one other point. The non-consensual surety is limited to a recovery measured by the unjust enrichment of the defendant, that is by the benefit conferred on the principal debtor, while the consensual surety is entitled to recover his outlay without regard to the enrichment of the principal debtor.\textsuperscript{24} In our case, the plaintiff sued for the amount of money paid on defendant's account, a sum to which it would be entitled as a consensual surety. On the other hand, it would seem that if plaintiff were a non-consensual surety, recovery, if permitted, should be measured by the value of the use of the truck for four months and this probably would not be exactly the amount of the payments made.

In conclusion, it seems that the majority opinion is correct only if the seller is considered to be a non-consensual surety. Although this conclusion might be drawn from the facts appearing in the record, it would have been better to have had a full presentation of evidence on this point in the trial court.

\textsuperscript{22} \textit{Restatement, Restitution} § 78(a) (1937); \textit{Restatement, Security} § 105(2) (1941).

\textsuperscript{23} \textit{Restatement, Restitution} § 78 comment b (1937).

\textsuperscript{24} \textit{Restatement, Security} § 104(2) (1941). For the position that a non-consensual surety is not even entitled to a restitutional recovery see Sipmson, Suretyship, 225-27 n.71 (1950).