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THE TRIPARTITE CREDIT CARD TRANSACTION:
A LEGAL INFANT

“All of a sudden, the credit card was just like an Aladdin’s lamp and you didn’t even have to rub it.”¹ These words, expressing something more akin to pride than to remorse, were recently offered by a nineteen-year-old boy in explanation of a one-month trip back and forth across the North American Continent. During his escapade, the boy purchased nearly ten thousand dollars² worth of goods and services by the simple expedient of making frequent and extravagant use of his all-purpose credit card. The omnipotent credit card was used to procure U-Drive automobiles, airline tickets, luxurious hotel suites, food and drink, multifarious items of men’s wear, a silver mink stole for a newly-acquired girl friend, and a puppy dog for himself.² This brief case history certainly bears out the assertions of all-purpose credit card advertisements and brochures that credit cards can be used to purchase almost any conceivable item or service. It also indicates that credit cards are subject to grave abuse³ and that the potential liabilities of the credit card issuer, credit card holder, and honoring merchant are not hypothetical or trifling, but very real and very great.

The nature of the credit card transaction has been changed in recent years from a modest two-party arrangement, enabling a retail buyer to purchase on credit one special type of item or service, into a tripartite plan involving a card-issuing company, card-holding members, and merchant members who sell diverse goods and services on credit to card holders. It is this newer and more complex three-party transaction that is the subject of this Comment.⁴

It must be stated at the outset that there is virtually no authority, judicial or statutory, that directly controls the legal problems which may be expected to arise from the tripartite credit card transaction. And it will be shown that in spite of certain functional similarities to the factoring of accounts and letter of credit transactions, it is not feasible to conclude that the law of either of these transactions should be applied automatically to the credit card arrangement.⁵

The discussion will begin with a short presentation of the historical development of the credit card, followed by an explanation of the basic mechanics of the tripartite credit card plan. Next, the credit card plan will be examined in the light of two recognized commercial transactions, the letter of credit transaction and the factoring of accounts receivable. Attention will then be directed to particular legal

² Ibid. Apparently the boy’s $73-a-week occupation will not provide sufficient remuneration to pay for the items that he obtained on credit.
³ For another example of such abuse see, Brean, The Great Credit Card Spree, Life, June 1, 1959, p. 119, describing the methods, successes, and ultimate failure of a convicted credit card thief.
⁴ Much of what follows, particularly Parts V, VI, and VII infra, is equally applicable to the less pretentious two-party arrangement in which a “one-purpose” card is used. The typical two-party transaction involves an agreement between a card holder and a department store or chain which occupies the dual role of card issuer and retail seller. The card is honored only by that store or chain of stores.
⁵ See Part III infra.
problems of the credit card transaction: the ability of the card holder to assert defenses and counterclaims that he has against the merchant in a suit brought for payment by the card issuer; the card holder's responsibility to pay for authorized and unauthorized purchases made with his card; the criminal liabilities of the authorized and unauthorized user of the credit card; and the applicability of revolving credit statutes to the tripartite credit card transaction.

I

HISTORY OF THE CREDIT CARD

The precursor of the present day credit card, the "credit coin," had its beginning sometime before 1920. Apparently the first business enterprises to issue them were retail department stores. The primary purpose of the retailer in issuing coins, and later cards, was simply to stimulate sales by encouraging credit purchases. A secondary motive prompting the issuance of credit coins or cards was to provide charge customers with a ready means of identification in order to protect against the possibility of an imposter charging items to someone else who maintained a charge account with the retailer. In earlier days, the customer generally paid no fee for the privilege of purchasing goods on credit. However, it has now become more common for the retailer to exact a service charge calculated each month as a percentage of the unpaid balance.

In the 1920's petroleum companies began issuing courtesy cards which were honored by all company-owned retail outlets and all authorized independent dealers. It became common for oil companies whose retail stations were confined to a particular area of the country to make reciprocal agreements with other companies in different areas, whereby each company agreed to honor credit cards

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6 The difference between the credit coin and the credit card is primarily one of physical appearance. Whereas the familiar credit card is a wallet-sized piece of plastic or stiff paper imprinted with the name and address of its owner, the credit coin is a small piece of metal which displays only the name of the merchant and a series of numerals identifying the customer's account.


8 See Donovan, Controlled Identification and Authorization with Authorite, 1952-53 Credit Management Yearbook 306, where the author discusses the merits and demerits of tokens of identification ranging from coins to charge cards and address plates. He concludes that the most satisfactory device to protect against fraudulent use is the "Authorite Key," a cylinder smaller than the cap of a fountain pen, with a printing and identification element locked inside. The locking mechanism is so controlled that it can be opened only by a machine in a store where the customer has an account. Although the sense of mystery created by this device is appealing, considering it in the context of the multi-credit-card owner signifies its impracticability.

9 This is often termed "revolving credit" because the customer is given a maximum amount of credit which is diminished by each purchase and then gradually restored as he makes installment payments on the amount due. Usually the customer is given the option each month of paying his bill in full within thirty days or paying in installments over a period of months, in which case a service charge of 1% to 13/2% of the outstanding balance is exacted each month. Romney, Revolving Credit and Option Charge Accounts, Credit World, July 1959, p. 10. See Trotta, New Developments and Analysis of Revolving Credit, 1955-56 Credit Management Yearbook 163, for a discussion of the advantages and costs of revolving credit plans to department stores. Recent legislation in at least six states establishes maximum allowable service charges for these two-party revolving credit accounts. See Part VII infra.

10 Rutter, Consumer Credit Heads for a Peak, N.Y. Times, May 10, 1959, § 3, p. 1, col. 8. This article explains that hotel chains, telephone and telegraph companies, travel organizations, and common carriers followed the lead of the oil companies in issuing courtesy cards.
issued by the other.\textsuperscript{11} It was thus made possible for the credit card holder to make nation-wide use of his card, but only for the limited purpose of purchasing goods and services available at service stations.

In 1950 Diners' Club transformed the courtesy credit card into a large-scale profit-making device.\textsuperscript{12} Unlike previous firms which issued credit cards, Diners’ Club sells no goods. It performs credit and collection services for the merchant members of the plan, and makes it possible for card-holding members to purchase goods and services at an increasing number and variety of retail outlets without having to enter into a direct credit relationship with any of them. Once approved by the “Club,” the credit rating of a card holder is automatically established with each merchant member of the plan. The pattern established by Diners’ Club is equally descriptive of every “all-purpose” credit card plan that has since come into existence.

Diners’ Club had no serious competition until October 1958,\textsuperscript{13} when the American Express Company initiated its own world-wide credit card system, followed six months later by the Hilton Credit Corporation.\textsuperscript{14} The competition among these three organizations to get more cards into circulation and to sign agreements with merchants,\textsuperscript{15} particularly with merchants in types of businesses that have

\textsuperscript{11} Recently it has been proposed that the oil companies band together and issue one comprehensive credit card, in view of the fact that over 50% of the oil company card holders possess cards of more than one company. The opinion was expressed that costs of the oil companies’ credit systems could be minimized by establishing one central agency to make credit checks and handle billing procedures and collections. Dorgan & Sullivan, How About One Credit Card for the Whole Oil Industry?, National Petroleum News, Aug. 1959, p. 168. It seems likely that this proposal was offered as an alternative to the already successful invasion of the oil industry by the “all-purpose” credit card companies. In late 1959 it was stated that all but three of the major oil companies that distribute in the West had contracted with one or another of the all-purpose card companies, promising that their retail dealers would honor the all-purpose card in addition to the oil company card. How Effective are Universal Credit Cards?, National Petroleum News, Oct. 1959, p. 117. Under these contracts the oil company rather than the dealer usually pays the service charge required by the all-purpose card company. It is estimated that the cost to the oil company under such contracts is from 0.125\ to 2\ euro per gallon higher—depending upon the card company contracted with—than the cost when the oil company’s own card is used. The oil companies that oppose the use of all-purpose credit cards argue that they do not increase the total demand for gasoline products, and that they cut into profits and destroy brand loyalty. Id. at 122.

\textsuperscript{12} The circumstance that led to the founding of this company is such an instructive example of American logic that it deserves relating. One evening a New York credit specialist dined at a restaurant. Upon being confronted with the bill he discovered that he had left his wallet at home. A telephone call brought his wife to the rescue. After he consulted with an attorney the next day, Diners’ Club was founded, consisting initially of fourteen restaurants and two hundred card holders.

\textsuperscript{13} Prior to this time fifteen competitors had either withered away or had been absorbed by Diner’s. Restaurant Management, Oct. 1959, p. 52.

\textsuperscript{14} There is no exaggeration in the boasts of these three companies that they issue “all-purpose” cards which are honored at diverse establishments throughout the world. The variegated purposes for which their cards can be used defy rational categorization. See N.Y. Times, Nov. 8, 1959, \textsuperscript{\textsection} 6, p. 64, 68. As might be expected, our more conservative brethren across the Atlantic have spoofed this country’s naive fascination with credit cards: “In the welter of excitement over the potentialities of this new toy, the sweet simplicity of cash—with no bills, no commissions, and no tedious long lists of co-operating hotels and petrol companies—has largely been overlooked.” The Economist, Oct. 4, 1958, p. 43, 44. But not wholly overlooked. The Rozee Bonus Club issues a “cash” card for a $5 annual fee which entitles its owner to get a 10\% cash discount at 2600 retail establishments. Rutter, Consumer Credit Heads for a Peak, N.Y. Times, May 10, 1959, \textsuperscript{\textsection} 3, p. 1, col. 8.

\textsuperscript{15} One of the most recent counts of card holders: Diners, over 1,000,000; Hilton, 1,000,000; American Express, 700,000. Diners claims 26,000 merchant outlets; Hilton, 60,000; American Express, 37,000. Restaurant Management, Oct. 1959, p. 61.
made to a card holding members an annual fee which varies from five to six dollars, and charge
previously not honored their cards.\textsuperscript{10} has been nothing less than fierce.\textsuperscript{17} As compensation for their services, these three credit card companies charge their card-
holding members an annual fee which varies from five to six dollars, and charge

While these three credit card systems cater primarily to the needs of the busi-
nessman,\textsuperscript{19} since early 1959 the nation's two largest banks, Bank of America and

\textsuperscript{10} See note 11 supra as to the card companies' invasion of the oil industry. As a group,
the major scheduled airlines have strenuously resisted the attempt of all-purpose credit card com-
panies to subvert the airlines' own credit card system (Universal Air Travel Plan). It has been
reported that the International Air Transport Association has sought the aid of the Civil Aeron-
autics Board in the airlines' battle with the card companies. Wall Street Journal, Aug. 5,
1959, p. 5+., col. 5. See also Newsweek, Aug. 17, 1959, p. 72.

\textsuperscript{17} To meet the challenge of American Express, Diners' Club, late in 1958, planned to triple
its expenditures for advertising and promotion to the amount of $2,000,000 annually. Jones,

\textsuperscript{19} Late in 1958 it was reported that more than half of these card memberships were held
by company officials required to travel and entertain. Jones, Credit Card Clash, Wall Street
Journal, Nov. 17, 1958, p. 1, col. 1. The use of credit cards by businessmen has been stimulated
by the necessity of keeping records of entertainment expenses for tax purposes and by the desire
of companies to protect against expense account padding by employees. Jones, Credit Card

\textsuperscript{17} The fact that bad debts are generally rising at a faster rate than credit card sales volume
has been partially attributed to the issuers' increasing willingness to issue cards to people who
are poorer credit risks. Diners' Club estimates that bad debts now total .6\% of sales volume,
 triple the percentage of seven or eight years ago. Jones, Errant Chargers, Wall Street Journal,

A revolt by a significant portion of the restaurant industry against the credit card companies
in 1958–1959 was caused by dissatisfaction with the amount of the charge exacted from them
by the card companies and with the practice of some card issuers of making restaurant owners
wait from thirty to sixty days for payments on assigned sales slips. Business Week, March 21,
1959, p. 36. Various means have been devised by restaurant owners to avoid these disadvan-
tages: e.g., withdrawing from credit card plans; using credit cards as a credit reference and
billing customers directly; charging card holders a price higher than cash customers, equal to
the amount of the charge by the issuer; and organizing their own cooperative credit card plans
with a central billing system. Restaurant Management, Oct. 1959, p. 70. The Hilton card
company placated many of the malcontents by lowering the charge to restaurants from 4.5\%
and promising prompt payment to restaurants to cover charges incurred by card hold-
ers. This action brought a frank endorsement of the Hilton plan by the National Restaurant
Association. Restaurant Management, Oct. 1959, p. 47. Hilton's 4\% charge is computed on the
gross amount (i.e., including tax and tip) of each bill, compared to Diners' 7\% on the net
amount, and American Express' 5\% to 7\% on the net amount. The fluctuation of the American
Express charge is explained by its rebate system.

The cases of the oil industry, the airlines, and the restaurant owners suggest that the
credit card companies are able to overcome a particular industry's opposition to the costs of
the plan by negotiating with members of the industry on an individual basis. Once the card
companies have obtained a foothold, competitive pressures force many former dissidents to join.
have similar credit card plans. Whereas the bank plans are usually geographically limited to one metropolitan area or state, Seaboard Finance Company, the third largest consumer finance company in the country, has launched a similar credit card plan through a subsidiary, International Charge, Inc., which is soon expected to extend its operations to most of the fifty states and parts of Canada.

II

MECHANICS OF THE CREDIT CARD PLAN

Although the mechanics of the various tripartite credit card plans adhere to one general pattern, it is often helpful to draw a distinction between plans which appeal primarily to the businessman and travelling man and those which appeal to the retail purchaser of everyday items and services. Whenever a distinction must be drawn, the former will be referred to as “entertainment” plans, and the latter as “consumer” plans.

Credit card plans involve one card issuer and many merchants and card holders. Because the form contracts used are drafted by the issuer and because only one merchant and one card holder are involved in a particular credit card transaction, it is convenient to consider the plans as three-party arrangements, referring collectively to all merchants as “the merchant” and to all card holders as “the card holder.” The issuer is the moving force of the plan, and the success of its endeavor is dependent upon the solicitation of both merchants and retail buyers.

The issuer distributes credit cards either upon application or, if the cards are issued free of charge, by sending them unsolicited through the mails. The issuer of entertainment cards collects an annual fee of from five to six dollars from the holder, whereas consumer cards are issued free of charge.

The entertainment or consumer card holder is entitled to purchase goods and services on credit at any retail outlet which has become a merchant member of the

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The bank-sponsored credit card plans are to be distinguished from the revolving credit or ready credit check plans also offered by banks. In the ready credit check plans, the customer and bank agree upon a prearranged credit limit or “line of credit,” which might vary from twelve to twenty-four times the amount the customer can afford to pay each month. As the customer makes monthly payments he restores the amount of credit available to him. The ready credit check plans involve no credit cards and no contractual relationships between the bank and merchants. They simply allow the customer to pay for major expenses by check, without having to apply for a loan each time such an expense arises. See Jedlica, A Revolving Credit Plan for Banks, Credit World, June, 1959, p. 18; N.Y. Times, Jan. 13, 1959, p. 40, col. 6.


Some all-purpose credit card plans involve a fourth party, the functions of the issuer in the tripartite plan being divided between a card issuer and a bank. In the four-party plans, the issuer collects fees from card holders and promotes the plan, while the bank serves as a central agency for the billing and collecting of card holders’ accounts. Claflin, The Credit Card—A New Instrument, 33 Conn. B.J. 1 (1959). The rights and obligations of the four parties should be basically the same as in the tripartite transaction discussed here except that reference must be made to the issuer-bank contract in order to determine in what manner those two parties have apportioned the rights and duties that belong solely to the issuer in the tripartite arrangement.

23 The identifying words are arbitrarily chosen and are not intended to be entirely satisfactory as descriptive terms.

Generally it can be said that the issuer-merchant form contract used in entertainment plans is more general in its terms, less complex, and more informal in its language than the corresponding form contract used in consumer plans.
For this privilege, the card holder contracts to pay the issuer for "all credit extended on the basis of the card" or for "all purchases made with the card" until the issuer receives written notice of the loss or theft of the card. At the end of each billing period, the issuer consolidates all of the purchases made by the card holder from merchant members during the period and sends him one all-inclusive statement. Under the consumer plans, upon receipt of each monthly statement the holder has the option of paying the face amount of the bill within a specified period, usually twenty-five to thirty days from the date the statement is mailed, or of paying according to a deferred payment schedule. If he selects the latter method of payment, he must pay approximately ten to twenty percent of the total bill within twenty-five to thirty days, depending upon the particular plan. The remainder is paid in monthly installments and is subject to a service charge which is computed each month as one and one-half percent of the previous month's balance less all appropriate credits.

As for the merchant member of the plan, his rights and duties are contained in a form contract drafted by the issuer. He is obligated to "assign" or "endorse" to the issuer all "sales drafts," "charge slips," or "accounts," which represent sales made to card holders. With certain exceptions, the issuer's "purchase" of

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25 Such merchants are identifiable by their prominent display of the issuer's emblem. Entertainment card issuers also distribute wallet-sized directories to their card holders, listing the names and locations of all merchant members. In addition to issuing directories, one company has announced the intention of listing all merchant members in every large city in the yellow pages of the telephone book. Each merchant will also be identified as a member by a tag-line in the regular white pages. Restaurant Management, Oct. 1959, p. 65.

26 The terms of the "contract" are contained in small print on the reverse side of the card or on the inside front cover of the directory. As to the binding effect of these provisions see generally Part V infra.

27 There are two possible interpretations of such language. See Part III C infra. For its relation to defenses and counterclaims available to the card holder in a suit brought by the issuer, see Part IV infra.

28 As to the liability of the holder for purchases made by an imposter see Part V B infra.

29 The holder of an entertainment card has no such option, nor does he pay a service charge. The sole cost imposed upon him is the annual fee. Upon receipt of his statement, he is expected promptly to pay his bill in full.

30 At the time of the customer's application for a credit card, he is given a maximum amount of credit. At any given time the credit available to him is dependent upon the amount owing to the issuer. This "revolving credit" feature is not unique to the three-party credit card arrangement. See notes 9 and 21 supra.

By way of illustration, assume that a new card holder makes purchases amounting to $225 in January. The statement mailed on January 31 indicates that his balance is $225. If he pays the full amount within thirty days, there is no service charge. Suppose, however, that he chooses to pay in installments. He refers to the deferred payment schedule which indicates that when the balance owing is between $200 and $250 a minimum of $25 must be paid. He pays $25, his balance being reduced to $200. During the month of February he purchases items amounting to $100. The statement of February 28 will show a balance of $303: $100 (for February purchases plus $200 plus a $3 service charge. The 1½% service charge is calculated on the previous month's balance ($225) less payments made in the succeeding thirty-day period ($25), i.e., 1½% of $200. If during the month of March he makes a $40 payment and $10 in purchases, the statement of March 31 will show a balance of $276.95: $10 (for March purchases) plus $263 (February 28 balance of $303 less March payment of $40) plus $3.95 (1½% of $263).

31 Some of the plans exact an initial membership fee of up to $25 and require the merchant to pay a monthly rental of $1 for each sales draft imprinter necessary to operate the plan. In addition, some of the bank-sponsored plans require the merchant to maintain a commercial account with the bank.

32 The words inside quotation marks indicate the variance of terminology in the contracts of the different credit card plans.
sales drafts or accounts is without recourse to the merchant in the event of non-payment by card holders. In addition to assuming the credit risk, the issuer handles the billing procedures, makes all collections from card holders, and investigates the credit rating of credit card applicants. The issuer's compensation for these services is obtained by discounting the sales drafts assigned to it by the merchant at a rate established by the contract.

III

THE LETTER OF CREDIT, THE FACTORING OF ACCOUNTS, AND THE CREDIT CARD

It requires no boldness to assert that there is no credit card law in the same sense that there is a law of negotiable instruments or a law of wills. Indeed, there has been no attempt to formulate a comprehensive legal definition of the exact nature of the tripartite relationship found in the modern credit card transaction. In an economic and legal sense the tripartite credit card arrangement is a hybrid, the pivot of the system being the card-issuing company, which solicits and serves retail sellers and buyers by offering to each a service that is more commonly extended by a bank or finance company to commercial sellers and buyers. To the retail buyer is extended the opportunity of buying goods and services from merchants on the credit of the card issuer. Observed from this standpoint, the credit card arrangement is similar to the commercial letter of credit transaction. The seller, on the other hand, is able to take advantage of services of the card issuer that are similar to those offered by a firm that "factors" or purchases accounts receivable.

Observing the workings of the credit card transaction against the background of these other two transactions is helpful in explaining the economic realities and legal problems of the credit card plans. It is also suggestive of two different approaches which might be used in solving legal problems arising from the credit card transaction.

A. The Commercial Letter of Credit Transaction

The primary purpose of the commercial letter of credit is to substitute, in a contract of sale, the credit of a recognized, financially responsible person for the

33 These exceptions are defined in some of the form contracts in vague and uncertain terms, apparently for the issuer's own protection. But generally it can be said that the issuer will have recourse to the merchant when the face of the card indicates that it has expired; when the card is on the current void list sent by the issuer to the merchant; when the sales slip is illegible or not signed by the person who made the purchase; when there is non-delivery of merchandise; when there is a breach of warranty or fraudulent acts on the part of the merchant; or when the merchant, without prior clearance from the issuer, allows the card holder to make a purchase in excess of the single-purchase credit limit established by the issuer.

34 The consumer plans operate almost uniformly on a 6% discount rate and provide for a quarterly rebate to the merchant based upon the volume of his sales and the dollar average per sale. See note 18 supra for the discount rates charged by the entertainment card issuers.

35 For a discussion of letters of credit generally see DAVIS, THE LAW RELATING TO COMMERCIAL LETTERS OF CREDIT (2d ed. 1954); FINKELSTEIN, LEGAL ASPECTS OF COMMERCIAL LETTERS OF CREDIT (1930); GUTTERIDGE, THE LAW OF BANKER'S COMMERCIAL CREDITS (1932); McCurdy, Commercial Letters of Credit (pts. 1-2), 35 HARV. L. REV. 539, 715 (1922).

Although there are many different forms and types of letters of credit, the present discussion deals with a letter of credit which is generally referred to as special, documentary, and irrevocable. For the meaning of these different terms and for a discussion of the distinctions between the different types of letters of credit see DAVIS, op. cit. supra, at 23-41.
credit of a buyer of unknown or doubtful credit standing. To accomplish this purpose the commercial letter of credit transaction requires three parties—the letter writer, the buyer, the seller—and three contracts.

The contract of sale between the buyer and seller may precede the other two contracts and stipulate that payment be made under a letter of credit, or it may be made subsequently, the buyer having previously arranged for the letter of credit. The contract between the letter writer and the buyer provides for the issuance of the letter of credit and specifies the conditions which the seller must fulfill before the letter writer is to become obligated to the seller. It also provides for the repayment of the letter writer and for a charge for the use of the letter writer's credit. The letter writer-seller contract is embodied in the letter of credit which states, in effect, that if the seller will deliver or ship specified merchandise to the named buyer, the letter writer will pay for it. The letter of credit usually takes the form of a promise to accept bills of exchange drawn by the seller on the letter writer if those drafts, when presented, are accompanied by specified documents; when the seller acts on this promise a contract is formed. The documents required to accomodate the drafts are specified by the buyer in the letter writer-buyer contract, and are usually shipping documents such as bills of lading.

38 Davis, op. cit. supra note 35, at 20. "The commercial letter of credit is essentially an adaptation of the older traveler's letter of credit to a transaction involving the sale of merchandise." Finkelstein, op. cit. supra note 35, at 12. The traveler's letter of credit is used to enable a person away from home to obtain money, allowing him to travel without a great amount of cash. It is obtained from the traveler's home bank and is addressed to banks in the locations the traveler expects to visit, authorizing those banks to advance money or credit to the person possessing the letter. The home bank assumes responsibility for advances made.

Although a credit card may be compared with a traveler's letter of credit in that both are carried by the buyer and shown to the person extending money or goods on the credit of a third party, the credit card does not in itself entitle the card holder to obtain goods and services on the credit of the card issuer as would a traveler's letter of credit. Before the credit card holder may make use of the card there must exist an antecedent agreement between the card issuer and the merchant which provides that the latter must honor the credit card. In this context, the credit card serves more as an identification card, informing the merchant that he may deliver goods to the card holder in reliance on the card issuer's promise of reimbursement.

One writer has suggested that the credit card itself is a commercial letter of credit. Note, Credit Cards—Civil and Criminal Liability for Unauthorized or Fraudulent Use, 35 Notre Dame Law. 225 (1960). This view seems to ignore the existence of the contract existing between the card issuer and the merchant which provides the terms of the agreement between them. The commercial letter of credit itself is the contract between the letter writer and the seller. The credit card clearly does not perform this function since it represents the agreement between the card issuer and the card holder and not between the card issuer and the merchant.

37 It has been stated that the modern method of operating under a commercial letter of credit is to insert a provision for payment under a letter of credit into the contract of sale. Davis, op. cit. supra note 35, at 15.

38 This contract usually takes the form of a request by the buyer asking the letter writer to issue a letter of credit in favor of a named seller. This request, when complied with, brings the buyer and the letter writer into a contractual relationship. Davis, op. cit. supra note 35, at 51. On the legal relationship between the buyer and the letter writer see generally, Davis, op. cit. supra note 35, at 51-55.

39 The use of a bill of exchange makes possible a negotiation by the seller so that he may obtain immediate cash for the sale, even though the letter writer may be a great distance away. For a discussion of the negotiating bank's rights after such negotiation, see Davis, op. cit. supra note 35, at 91-100. See also Old Colony Trust Co. v. Continental Bank, 288 Fed. 979 (S.D.N.Y. 1921); Bank of Laddonia v. Bright-Coy Commission Co., 139 Mo. App. 110, 120 S.W. 648 (1909).

40 Russell v. Wiggins, 21 Fed. Cas. 68 (No. 12165) (C.C.D. Mass. 1842); Story, Bills of Exchange 462 (1860). The promise is considered irrevocable from the time it is made. For a review of the suggested legal theories behind the irrevocability of the letter writer's promise see Davis, op. cit. supra note 35, at 57-69.
but may also include certificates of quality.\footnote{Davis, \textit{op. cit. supra} note 35, at 19. The documents required usually give the letter writer title to or a security interest in the goods sold. In this manner the letter writer is protected from default on the part of the buyer. On the role the documents play in the letter of credit transaction see generally Davis, \textit{op. cit. supra} note 35, at 120-66.}

In this manner the buyer is able to protect himself, since the letter writer agrees not to honor drafts unaccompanied by the documents specified and since the buyer need only reimburse the letter writer for payments authorized by the contract.\footnote{Davis, \textit{op. cit. supra} note 35, at 51, 52.}

As in the letter of credit transaction, the credit card purchase is accomplished by a substitution of credit—the credit of the card issuer for that of the card holder. Thus, the card holder is able to make a credit purchase on terms which the merchant might have been unwilling to extend on the personal credit of the card holder, including in some instances a long-term repayment schedule. The card holder, moreover, is in contractual privity with the card issuer, as is the buyer under a letter of credit with the letter writer, the contract providing for the reimbursement of the card issuer.

Although the primary purposes of credit card and letter of credit transactions appear similar and the methods of realizing these purposes are superficially much the same, it is difficult to say that the nature of the obligations incurred by the parties to the two transactions are alike. In the letter of credit transaction it is clear that the obligations under the three contracts, except as expressly provided otherwise, are independent of each other, and are understood to be so by the parties. Compliance with one contract is not a condition precedent to the enforceability of another.\footnote{Kingdom of Sweden v. New York Trust Co., 197 Misc. 431, 96 N.Y.S.2d 779 (Sup. Ct. 1949); Overseas Trading Corp. v. Irving Trust Co., 82 N.Y.S.2d 72 (Sup. Ct. 1948).}

Thus, performance of the sales contract by the seller is not a condition precedent to the obligation of the letter writer to pay the seller,\footnote{Continental Nat'l Bank v. National City Bank, 69 F.2d 312 (9th Cir. 1934); Bank of Taiwan v. Union Nat'l Bank, 1 F.2d 65 (3d Cir. 1924); S. L. Jones & Co. v. Vincent Bond, 191 Cal. 551, 217 Pac. 725 (1923).} nor, in turn, of the obligation of the buyer to reimburse the letter writer.\footnote{Generally the letter writer's obligation is to pay against documents and not against goods. Therefore, if the documents are in order, he must pay without inquiry into questions such as quality or quantity of the goods sold. Continental Nat'l Bank v. National City Bank, 69 F.2d 312 (9th Cir. 1934); Maurice O'Meara Co. v. National Park Bank, 239 N.Y. 386, 146 N.E. 636 (1925).} The letter writer has promised to pay the seller on the receipt of specified documents. If these documents are in order, even though there has been a breach of the sales contract by the seller, the letter writer is nevertheless obligated to pay,\footnote{See National Wholesale Grocery Co. v. Mann, 251 Mass. 238, 146 N.E. 791 (1925).} and since the buyer has agreed to reimburse the letter writer for all payments required to be made to the seller, the buyer is obligated to fulfill his promise of reimbursement regardless of any claims he may have against the seller arising out of the sale or otherwise. The buyer's payment does not, however, preclude him from proceeding against the seller for breach of contract.\footnote{S. L. Jones & Co. v. Vincent Bond, \textit{supra} note 44; Frey & Son v. E. R. Sherburne Co., 193 App. Div. 849, 184 N.Y. Supp. 661 (1920).} Whether it can be said that the obligations incurred by the parties to a credit card purchase are the same as those incurred in the letter of credit trans-

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action is at least doubtful. Certainly it is not the express undertaking of the card issuer in the credit card transaction to pay the merchant without regard to the sale itself. Nor can it be said that the card holder has clearly undertaken to reimburse the card issuer for all justified payments the latter has made to the merchant. If the card holder’s obligation is merely conditional upon the card issuer’s making payments to the merchant, then he certainly stands in a less desirable position than the buyer under a commercial letter of credit, since the card holder has no opportunity to specify the requirements the merchant must fulfill before he is entitled to payment from the issuer.

B. The Factoring of Accounts Receivable

While the analogy is by no means perfect, the credit card issuer most nearly resembles the modern factor with regard to the services it performs for the merchant member of the credit card plan. Although factors were originally commission merchants, their functions gradually changed until the term “factor” came to designate a company which purchased the accounts receivable of a manufacturer or merchant and performed other valuable credit services.48

A factor is to be distinguished from a bank or finance company which lends money to a manufacturer or merchant on the basis of the latter’s accounts receivable.49 The factor purchases outright the accounts receivable of his client for immediate cash without recourse to the client should the buyer default on his payments. In addition to assuming the credit risk, the factor relieves the seller of accounts receivable bookkeeping, notifies the buyer that he has acquired the accounts of the seller, and collects them directly from the buyer. In the financing of accounts receivable, on the other hand, the bank or finance company holds only a security interest in the seller’s accounts receivable. The buyer, who is usually not notified of the assignment of the accounts, pays the seller directly for the goods purchased, and the seller in turn remits the proceeds to the assignee finance company.50 If the buyer defaults, it is the seller who bears the loss. Also the seller must continue to maintain a credit department to establish the credit ratings of potential customers and must continue to mail invoices and make collections. One who finances accounts receivable, in short, performs the modest function of lending money to a seller, in contrast to the factor whose services virtually eliminate the seller’s need for a credit department, and permit him to devote his energy exclusively to the sale and distribution of merchandise.51

Theoretically at least, the credit card issuer performs the services of a factor for the merchant member of the plan. It purchases the “accounts” or “sales

50 “As the assignor collects accounts receivable and remits the proceeds, he delivers new schedules of accounts and acquires from the assignee further advances in the same ratio. Thus payment comes automatically from the security and the proportion of loans outstanding to accounts assigned generally remains constant.” Comment, 67 YALE L.J. 402, 404 (1958).
51 As one writer has aptly put it: “Both factoring and accounts receivable financing involve a continuing arrangement whereby cash is made available to business concerns as accounts receivable are created. There the similarity ends. Accounts receivable financing is a method of financing and nothing more.” Moore, supra note 48, at 724.
drafts" of the merchant arising from credit card sales, notifies the buyer of the assignment, accepts the credit risk, does the credit checking and bookkeeping, and makes collections of the accounts. But the similarity between the card issuer and the factor is somewhat illusory for the reason that the factor normally contracts to purchase all of the seller’s accounts, whereas the card issuer purchases only those that represent credit card purchases. Since many merchants permit their non-card holding customers to buy on credit independently of any credit card plans of which they may be members, these merchants are required to maintain a staff to make credit checks, keep account ledgers, mail invoices, and make collections. Only if a merchant permits credit purchases to be made exclusively by those customers who are members of one or another of the credit card plans can it be truly said that he has acquired all of the benefits which accrue to the seller who assigns all of his receivables to a factor.

Another difference between the factor and credit card issuer is that the factor has no contractual privity with the buyer of merchandise, whereas the card issuer has a direct contractual relationship with the card holder as well as with the merchant. The fact that the issuer has rights under two independent contracts creates a conceptual difficulty that casts some doubt upon the propriety of regarding the issuer as an assignee for the purpose of determining its legal rights and obligations.

C. The Credit Card Transaction

Any attempt to integrate the three contracts of the credit card transaction into a meaningful legal pattern must begin by recognizing that the card issuer may derive his right to receive payment from the card holder from one of two sources,

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52 While many of the consumer credit card issuers and one of the three major entertainment card issuers, like the factor, pay immediate cash for the accounts of the merchant member, under the other two major entertainment plans the merchant must often wait one or two months before receiving payment from the issuer. In such circumstances the comparison between the factor and the card issuer wears thin indeed.

53 Contractually and procedurally, the factor and credit card issuer operate in much the same manner. In both situations the seller warrants the authenticity of the accounts and represents that they arise from bona fide sales, not subject to set-off, defense, or counterclaim. Whereas each sale is submitted to the factor for credit approval, in the credit card transaction the merchant must get authorization for a credit purchase only when it is in excess of a predetermined amount. The invoice mailed to the buyer in the factor situation and the copy of the sales slip given to the card holder at the time of the purchase clearly notify the purchaser that payment is to be made not to the seller, but to the factor or card issuer. The factor’s fee, as the issuer’s fee in plans which have a rebate schedule, is partially based on the value of sales and the average amount of invoice. See Silverman, *Factoring: Its Legal and Economic Justification*, 13 LAW & CONTEMP. PROB. 593 (1948). For a specimen factoring contract see Silverman, *supra* note 48, at 610-11.

54 Although this is the apparent goal of the credit card issuers, it has not yet been generally realized.

55 One article has noted the “underlying similarity in function” of the factor and the letter of credit writer in the following terms: “He [the banker] positively buys or makes advances on receivables—but they must be in negotiable form. Indeed, in many cases now, he makes advances against the same type of receivables as does the factor. And while his efforts to guarantee accounts long were obstructed by the *ultra vires* doctrine, he now does the same thing by issuing a letter of credit undertaking himself to accept and pay the seller’s draft. The circumstance that it is the buyer in the letter of credit transaction who arranges for the credit, while it is the seller who initiates things in the factor set-up, would seem to be of no especial functional significance. It is the sale that is being financed in either event.” Steffen & Danziger, *The Rebirth of the Commercial Factor*, 36 COLO. L. REV. 745, 770 (1936). This pertinent observation can be updated twenty-four years by simply adding that the credit card issuer “does the same thing” as the factor and the writer of a letter of credit, and that it is “of no especial functional significance” that in the credit card transaction it is neither the buyer nor the seller, but the financier of the rules who “initiates things.”
i.e., from either the card holder or the merchant. It must be decided whether the card holder's promise to make payments for purchases directly to the issuer creates an obligation owing directly from the card holder to the issuer, or whether his promise merely indicates that he will make payments to the issuer only after the right to enforce the obligation has been assigned to the issuer by the merchant, to whom the obligation was initially owed. Otherwise stated, the question is whether the merchant transfers goods to the card holder in reliance upon the card holder's obligation to pay him and then makes an assignment to the issuer, as in the factoring of accounts, or whether he relies on the issuer's obligation to pay him, as in the letter of credit transaction.

A choice of one of these two possible interpretations of the credit card transaction, which hereafter will be referred to as the "assignment" and "direct obligation" theories, is not purely an academic one. For example, the availability of defenses and counterclaims to the card holder may be substantially affected by the adoption of one theory instead of the other, and the applicability of accounts receivable notice-filing statutes to the credit card transaction depends upon whether there is or is not an assignment. The courts have not consciously weighed the merits of the two theories and indicate only inferentially which interpretation is preferred.

Although the assignment theory is seemingly supported by language in issuer-merchant contracts which refers to an undertaking by the merchant to assign, sell, or endorse accounts or sales drafts representing credit card purchases, it is entirely possible that there is no actual assignment of a contract right. At no point in the transaction does the card holder expressly promise to make payments to the merchant, nor do the contracts among the three parties contemplate such payments so long as the merchant lives up to his agreement with the issuer. This suggests that once there has been a sale, the issuer is obligated to pay the merchant and the card holder is obligated to pay the issuer so that the merchant does not acquire a right against the card holder that can be "assigned" from the merchant to the issuer. This interpretation is in accord with the direct obligation theory.

Because neither theory has been definitely sanctioned by the courts, the legal problems selected for discussion will be examined in the light of both of them in order to indicate how the rights and obligations of the parties may be affected by the adoption of one theory instead of the other.

58 The terms of the card holder-issuer contract are set forth on the reverse side of the credit card. One representative provision reads as follows: "Responsibility for all credit extended on the basis of this card is accepted. Payment of such credit will be made to [issuer] . . . in accordance with billings and the current customer payment schedule." One interpretation of this language is that on use of the credit card an obligation to pay arises immediately in favor of the issuer, which payment is due as provided in the payment schedule. On the other hand, it is possible to argue that the language contains (1) the card holder's acknowledgment of the fact that the card issuer is going to obtain the right to payment for credit card purchases by an assignment from the merchant, and (2) his promise to pay the issuer under the agreed upon schedule when that right is so obtained. This interpretation is supported by clauses in the issuer-merchant contract which place a duty upon the merchant to "assign" sales slips or drafts to the issuer.

57 E.g., Union Oil Co. v. Lull, 349 P.2d 243 (Ore. 1960), talked the language of assignment without recognizing the possibility of the direct obligation theory, while United States v. Golden, 166 F. Supp. 799 (S.D.N.Y. 1958), seemed to assume the existence of a direct obligation owing from the card holder to the issuer without the necessity of a transfer of any right to collect from the merchant. In neither case was the determination of this issue necessary for the decision.

58 See note 33 supra for situations in which the issuer reserves a right of recourse against the merchant.
THE ABILITY OF THE CARD HOLDER TO ASSERT DEFENSES AND COUNTERCLAIMS

Although the foundation of the credit card transaction is a purchase of goods or services by the card holder from the merchant, the purchase price is collected by the card issuer. This fact presents the question of whether the card holder may assert a defense or counterclaim against the issuer which would have been available against the merchant were the merchant seeking payment on the sales contract. This question is important not only because of the possibility of multiplicity of actions, but also because a denial of the right to assert defenses and counterclaims may leave the card holder without any effective remedy at all, as, for example, where the merchant is insolvent, making useless any subsequent action against him, or where it is difficult or impossible to obtain jurisdiction over the merchant, a consideration especially relevant in the nation-wide and world-wide credit card systems. As yet, the reported cases have not dealt with this problem. The following discussion is, therefore, only an indication of how the question may be treated when it does arise.

Although the facts giving rise to a defense or counterclaim problem can be almost as variable as the circumstances surrounding each credit card purchase, for purposes of this discussion the problem is limited to three general situations: (1) where there are facts showing an infirmity in the sale itself and the card holder defends on the ground that there is no valid claim; (2) where there are facts showing a breach of duty on the part of the merchant and the card holder seeks by way of counterclaim to reduce in whole or in part the amount sought by the card issuer; (3) where there is a claim existing in favor of the card holder against the merchant unrelated to the credit card purchase and the card holder seeks by way of counterclaim to offset the amount of this independent claim against the recovery sought by the issuer.\[59\]

Whether defenses and counterclaims will be available to the card holder necessarily depends upon the legal relationships existing among the three parties to the credit card transaction and upon the nature of the right under which the card issuer seeks payment. As previously indicated, there are two conflicting theories

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59 The first category includes situations in which the contract of sale is void for lack of consideration or mutual assent, or voidable because of fraud, duress, or infancy, or in which there has been a failure of a condition in the sale, as where there is justified return of the goods.

In the second category are counterclaims which arise out of the sale itself, and they are to be distinguished from mere defenses, which could be asserted only to defeat the action. See CLARK, CODE PLEADING 639-41 (2d ed. 1947); Pomeroy, Code Remedies § 609 (5th ed. 1929). There are situations, however, in which the same facts could constitute either a defense or a counterclaim. Such a situation might be a breach of the sales contract by the seller which the buyer might either assert as an excuse for his own non-performance or raise by way of a counterclaim seeking damages.

The third category includes situations in which the card holder has a cause of action against the merchant upon which the card holder could have brought an independent action against the merchant, but, unlike counterclaims of the second category, it is unrelated to the credit card transaction. These situations may exist when, through previous dealings, the merchant has become indebted to the card holder either in contract or in tort. The California counterclaim statute, CAL. CODE CIV. PROC. § 438, does not require a counterclaim to arise out of the same transaction upon which the plaintiff's action is based. Terry Trading Corp. v. Barsky, 210 Cal. 428, 292 Pac. 474 (1930). The question in the credit card transaction is whether an independent claim may be set up against the card issuer in order to reduce or defeat his recovery, admitting the ability of the card holder to assert the cause of action against the merchant in the form of a counterclaim.
which could be used to define these legal relationships—the "assignment" theory and the "direct obligation" theory. The card holder's defense and counterclaim rights may vary substantially depending upon which theory is accepted and it is, therefore, necessary to consider both. The analysis is rendered more complex by the lack of uniformity in the terms of the agreements used by the different credit card plans, by the possibility of the card holder's being estopped to assert defenses and counterclaims, and by the introduction in at least one plan of what purports to be a negotiable instrument.

A. The Direct Obligation Theory

Under the direct obligation theory, where the promise of payment made by the card holder to the issuer is interpreted as creating the issuer's right to collect, there exists a situation similar to the letter of credit transaction. The merchant has parted with goods or services in consideration of the issuer's promise to pay; the card holder is obligated to pay the issuer, not the merchant. Unlike the letter of credit transaction, however, the card holder's promise is not expressly conditioned upon the receipt of any document by the issuer, nor is it necessarily understood to be independent of the credit card purchase. The card holder's promise is simply to pay for "credit extended" or for "purchases made."

Although it is necessary to interpret the terms "purchase" and "credit extended" in order to determine the defenses available to the card holder, it is apparent that under the direct obligation theory the card holder will be unable to interpose against the issuer a counterclaim which would have been available against the merchant, whether or not this claim arises from the sale. A counterclaim must be based upon a cause of action which could have been brought against the plaintiff, and no action could be brought against the card issuer by the card holder on facts constituting a cause of action against the merchant.

With regard to the defenses available to the card holder, the terms "purchase" and "credit extended" could be construed to result in an unconditional promise to pay the price of the goods or services. In other words, the card holder would be obligated to pay the issuer the amount of the purchase regardless of any defense which would be available to him against the merchant. But perhaps a more reasonable interpretation of these terms would be to assign to them their usual meaning in a typical two-party sale, i.e., not that there is an obligation to pay

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60 See Part III C supra.

61 Although the sales slip, which is executed at the time of the credit card purchase and subsequently sent to the card issuer, could be considered a document analogous to the documents present in the letter of credit transaction, this possibility is not mentioned in the card holder-issuer agreement, and, therefore, no express condition of payment based upon receipt of that slip exists. It is doubtful, however, whether a card holder would voluntarily pay a bill received unless the issuer could produce the sales slip.

62 See, e.g., the credit card provision quoted in note 56 supra.

63 "When we say that a defendant has a counterclaim, we mean that the plaintiff has committed a breach of duty to the defendant." 4 CORBIN, CONTRACTS § 896 at 594 (1951).

64 An exception to the rule that the counterclaim must exist against the plaintiff is found in the situation in which the assignee of a chose in action is suing the obligor, in which case a counterclaim existing against the assignor may be available against the assignee. See CLARK, CODE PLEADING § 106 (2d ed. 1947).

65 If the promise to pay were found unconditional, it might be considered unreasonable and therefore not binding on the card holder. See note 135 infra.
irrespective of any defects in the sale, but that the obligation is conditioned upon
the full and satisfactory completion of the sale. In a two-party sale the buyer pays
for the "purchase" or for "credit extended" only if he receives what he bargained
for. If the sale was infirm or was not completed by the seller, the buyer would have
a defense to an action for the purchase price. There appears no reason why these
terms should assume any different meaning in the credit card context. Thus inter-
preted, the card holder would be able to assert against the card issuer any defense
arising out of the sale itself which would have been available against the merchant
were the merchant seeking payment.

B. The Assignment Theory

The assignment theory looks at the credit card transaction from the point of
view of the sale. It assumes an obligation arising in favor of the merchant against
the card holder, an obligation present in the ordinary two-party sales transaction.
But the card holder, by virtue of his previous agreement with the issuer, is treated
as having acknowledged that the right to collect this obligation will be assigned to
the card issuer and as having promised that payments will be made to the issuer
after it is so assigned. Under the assignment theory, the card issuer, in a position
similar to that of the factor, will stand as an assignee of the claim against the
card holder for the purchase price. Thus, the ability of the card holder to assert
defenses and counterclaims against the card issuer will be determined by the law
of assignment.

In general, the assignee may obtain no better right than was held by the as-
signor. Thus, any defense or counterclaim arising out of the sale itself will be
available against the card issuer and its claim is to that extent impaired. Def-
enses not inherent in the sale itself will generally be available against the card
issuer if the facts constituting the defense existed prior to receipt by the card
holder of notice of the assignment. Similarly, if the facts constituting a counter-

60 4 CORBIN, CONTRACTS § 892 at 584 (1951); 2 WILLISTON, CONTRACTS § 432 (rev. ed.
1936); RESTATEMENT, CONTRACTS § 167, comment 1 (1932).

67 If the sales contract between the merchant and the card holder were void, as for lack of
consideration or mutual assent or for illegality, the card issuer would obtain no right against the
card holder. 4 CORBIN, CONTRACTS § 893 (1951); Beck v. Sheldon, 259 N.Y. 208, 181 N.E. 360
(1932). If the sales contract were voidable, as for fraud, duress, infancy, mistake or lack of
capacity, the card holder would be able to avoid the contract when sued by the issuer in the
same manner as if the merchant had brought the action. 4 CORBIN, CONTRACTS § 893 (1951);
RESTATEMENT, CONTRACTS § 167, ill. 2 (1932). Furthermore, the right of the card issuer would
be subject to the same condition as was the right of the merchant. 4 CORBIN, CONTRACTS § 895
(1951). Thus, if the goods were not delivered, or if there was a failure of consideration, e.g.,
a justified return of the goods, the card holder would be able to defeat the action of the card
issuer to the same extent as if the merchant were seeking payment. See Bliss v. California
Cooperative Producers, 30 Cal. 2d 240, 181 P.2d 369 (1947); Sponge Divers' Ass'n v. Smith,
Kline & French Co., 263 Fed. 70 (3d Cir. 1920); Rosenthal v. Rambo, 165 Ind. 584, 76 N.E.
404 (1905).

A counterclaim arising out of the same transaction as that in which the claim of the
assignor was created would also be available against the assignee. See 4 CORBIN, CONTRACTS
596 (1951). Thus, the card holder could counterclaim against the card issuer for damages
arising from the merchant's defective performance (see Feinberg v. Rowan, 111 N.J. Eq. 138,
161 Atl. 673 (Ch. 1932); American Bridge Co. v. City of Boston, 202 Mass. 374, 88 N.E. 1089
(1909)), or from the merchant's breach of warranty (see Rice v. Friend Bros. Co., 179 Iowa
355, 161 N.W. 310 (1917)).

68 Thus, if prior to receiving notice of the assignment the card holder has been discharged
by the merchant through payment, rescission and satisfaction, or other method of dis-
charge, the card holder will be under no obligation to the card issuer. See Ornbaun v. First
claim against the assignor existed prior to notice of the assignment, and the claim is mature at the time of its assertion, it is a good counterclaim against the assignee, although it is not related to the transaction creating the obligation upon which the assignee sues.

The time at which the card holder obtains notice of the assignment will then be the cut-off point, after which both defenses and counterclaims against the merchant not inherent in the sale itself will be unavailable against the card issuer. Notice of the assignment would seem to occur at the time of the card holder's receipt of the bill from the issuer.

1. Estoppel Precluding the Assertion of Any Defense or Counterclaim

Under the assignment theory, since the card holder knows that the merchant's contract claim is going to be assigned to the issuer, his knowledge may estop him from asserting a defense or counterclaim in an action brought by the issuer.

It is difficult to state general rules regarding estoppel since its application is particularly subject to the facts of each individual case. But before an estoppel may be found, it is generally agreed that the obligor by his acts or silence, if there is a duty to speak, must in some way have induced the assignee to accept the assignment. In the credit card transaction, it is unclear whether the card issuer could refuse to purchase the claim from the merchant if a defense or counterclaim were known to exist in favor of the card holder. If the issuer cannot refuse to

Nat'l Bank, 215 Cal. 72, 8 P.2d 470 (1932) (payment); LePorin v. State Exchange Bank, 113 Kan. 76, 213 Pac. 650 (1923) (accord and satisfaction); Parmley v. Buckley, 103 Ill. 115 (1882) (rescission). See generally 4 CORBIN, CONTRACTS § 894 (1951); RESTATEMENT, CONTRACTS §§ 167, 170 (1932). But discharge after notice of the assignment has been received, or after the card holder has reason to know of the assignment, while constituting a good defense against an action by the merchant, will not be available as a defense against the issuer. See 4 CORBIN, CONTRACTS § 590 (1951); First Nat'l Bank v. Perris Irr. Dist., 107 Cal. 55, 40 Pac. 45 (1895).

69 St. Louis Nat. Bank v. Gay, 101 Cal. 286, 35 Pac. 876 (1894); Martin v. Wells, Fargo & Co.'s Exp., 3 Ariz. 355, 28 Pac. 958 (1892); 2 WELLISTON, CONTRACTS § 432 (rev. ed. 1936); RESTATEMENT, CONTRACTS §§ 167, 170 (1932). But in some jurisdictions, the counterclaim is not available unless matured at the time of the assignment. Hartford Nat. Bank & Trust Co. v. Riverside Trust Co., 117 Conn. 276, 167 Atl. 811 (1933); Cosmopolitan Trust Co. v. Rosenbush, 239 Mass. 305, 131 N.E. 858 (1921); Fera v. Wickham, 135 N.Y. 223, 31 N.E. 1028 (1892). In no state is a counterclaim available against an assignee if it is acquired after notice of the assignment. 4 CORBIN, CONTRACTS § 897 (1951).

70 The notice required to be given to an obligor by an assignee to protect the latter's claim is usually considered to be actual notice, but if the obligor has knowledge of such facts as would put a reasonable man upon inquiry, the effect is the same as if actual notice had been given. See 2 WELLISTON, CONTRACTS 1265, 1266 (rev. ed. 1936). In the credit card context, the card holder knows that an assignment is going to take place, but does not know that the assignment has taken place until he receives his monthly bill from the issuer.

71 This knowledge of the card holder should not be regarded as notice of the assignment. The assignment is not executed in some of the entertainment plans until as long as a month after the credit card purchase, while in some of the consumer plans it may be executed on the day of the sale. On the use of estoppel to prevent the assertion of defenses and counterclaims against an assignee, see generally 4 CORBIN, CONTRACTS 899 (1951).

72 "The doctrine of equitable estoppel may prevent an obligor from setting up defenses and counterclaims as against an assignee. To create such an estoppel, the obligor must have so conducted himself as to induce the assignee to believe that the defense or counterclaim that is later asserted did not exist and to change his position materially in reasonable reliance thereon." 4 CORBIN, CONTRACTS 604 (1951). See also C.I.T. Corp. v. Hawley, 34 Cal. App. 2d 65, 93 P.2d 216 (1939); Bank of America v. Pacific Ready-Cut Homes, 122 Cal. App. 554, 10 P.2d 478 (1932); E.V. Harman & Co. v. William Filene's Sons Co., 232 Mass. 52, 121 N.E. 504 (1919).

73 Many of the issuer-merchant contracts provide that the issuer shall purchase all
accept the assignment, it appears there could be no estoppel because there could be no reliance. On the other hand, if the issuer were able to refuse the assignment, he might well allege estoppel. The basis of this estoppel would be the silence of the card holder in the face of a duty to inform the issuer of the existence of a defense or counterclaim. Such a duty has been found where the obligor had full knowledge of a defense or counterclaim existing in his favor, and he remained silent although knowing the obligation was to be assigned and having the opportunity to so advise the prospective assignee.

2. The Use of a Negotiable Instrument in the Credit Card Transaction

Although in most credit card plans the document which is assigned to the card issuer and which evidences the credit card purchase is in the form of an invoice, at least one system transfers the contract right by a document which purports to be a negotiable instrument. This instrument is printed in the form of a bill of exchange drawn by the merchant on the card holder and payable to the issuer or order. The signature of the card holder constitutes his acceptance. If the bill of exchange is negotiable and if the issuer may be deemed a holder in due course, "accounts" owing from credit card purchases. The merchant agrees to indemnify the card issuer for any defenses or counterclaims successfully asserted against it by the card holder, but there is no indication that if a defense or counterclaim exists in favor of the card holder against the merchant the issuer could refuse to purchase the "account" in the first place.


Ibid.

A variation of this credit card system is found in Franklin Nat'l Bank v. Kass, 184 N.Y.S. 2d 783 (Sup. Ct. 1959). In the plan there involved, the draft was drawn by the merchant on the card holder and made payable to the card issuer or order, as in the plan under consideration. But rather than having the card holder sign the draft at the time of the purchase as an acceptor, the terms of the credit card provided, in addition to an agreement to pay for charges incurred, that the card holder agreed to accept all drafts drawn on him for charges incurred through use of the card. In an action brought by the holder of the bill of exchange, to whom the issuer had apparently negotiated the draft, it was held that a promise to accept the draft was equivalent to an acceptance, and the holder of the bill of exchange was therefore allowed to recover the amount of the draft. See Cal. Civ. Code §§ 3208, 3216 (Uniform Negotiable Instruments Law §§ 127, 135).

The comment has been made of this case that a "more satisfactory way of finding liability would have been to hold the card bearer liable on his simple promise to pay which he made in the club regulation . . . ." Hart, Commercial Law, 1959 Survey of N.Y. Law, 34 N.Y.U.L. Rev. 1455 (1959). The juxtaposition of the theory used by the court to find the card holder liable, i.e., as an acceptor of a bill of exchange, and the suggested "more satisfactory" theory of Professor Hart, i.e., as the maker of a simple promise to pay for charges incurred with the card, indicates the failure of courts and writers to recognize that there are two possible interpretations of the nature of the card holder's obligation. If the credit card purchase is viewed as creating an obligation owed from the card holder to the merchant, which is then transferred to the card issuer, it would seem that there could be no collection of the purchase price apart from the draft itself. The Kass case seems to take this approach, i.e., that the obligation was owed to the merchant and was transferred to the card issuer by means of the bill of exchange sued upon. Professor Hart, on the other hand, seems to prefer the view that the provisions printed on the credit card create a direct obligation owing to the card issuer.

Holder in due course holds the instrument free from any defect of title of prior parties, and free from defenses available to prior parties among themselves, and may enforce payment of the instrument for the full amount thereof against all parties liable thereon."
a transfer of the instrument will cut off all the card holder's defenses and counter-
claims against the merchant that would otherwise be available against the issuer,
with the exception of certain "real" defenses.\footnote{79}

The document used in this plan seems to meet all the requirements necessary
for negotiability with the possible exception of being made payable on demand or at a fixed or determinable future time.\footnote{80} The terms on the form are:

Twenty-five days from demand unless otherwise agreed, purchaser-acceptor shall pay
to [issuer] . . . or order, the sum of . . . \footnote{81}.

No cases have been found which clearly decide whether the condition "unless
otherwise agreed" defeats the negotiability of an otherwise negotiable instrument.
But the purpose of requiring a negotiable instrument to have a definite due date
is to enable a person to whom it is negotiated to ascertain from its face whether
it is overdue; for if it is overdue when obtained, he may not be deemed a holder
in due course.\footnote{82} When the due date is conditioned by the phrase "unless otherwise
agreed," the purchaser of the instrument, even knowing the date of demand, will
be unable to determine if the twenty-five day period has been reduced or extended.
Thus, when the purpose of the requirement of a definite due date is considered,
it appears that the above bill of exchange is not negotiable.

Since it appears that the simple deletion of the qualifying words would make
the instrument a negotiable bill of exchange, it is important to consider the effect
of such a deletion upon the defense and counterclaim rights of the card holder.
The terms of the instrument under consideration name the card issuer as payee.
Although the rule is not universal, the majority of jurisdictions allow a payee of a
negotiable bill of exchange, who otherwise qualifies, to be a holder in due course.\footnote{83}
However, even in a jurisdiction where a payee may be a holder in due course, a
number of cases indicate that the credit card issuer might well be unable to estab-
lish itself as a holder in due course.\footnote{84} In those cases it appeared that the party
claiming to be a holder in due course was the moving party in the sale, even to the
extent of providing the forms and documents necessary for its conclusion, and it
was held that since the party was so closely connected with the sales transaction
it could not be deemed a holder in due course.\footnote{85} There is no apparent reason why

\footnotetext[79]{See notes 90–92 infra and accompanying text.}
\footnotetext[80]{CAL. CIV. CODE § 3082 (UNIFORM NEGOTIABLE INSTRUMENTS LAW § 1) specifies the
requisites of a negotiable instrument. CAL. CIV. CODE § 3082(3) provides that the instrument,
to be negotiable, "must be payable on demand, or at a fixed or determinable future time."}
\footnotetext[81]{The phrase "unless otherwise agreed" is printed on the form by the issuer because its
plan is a consumer credit card plan under which the card holder is permitted to pay for pur-
chases in installments.}
\footnotetext[82]{CAL. CIV. CODE § 3133 (UNIFORM NEGOTIABLE INSTRUMENTS LAW § 52) provides, "A
holder in due course is a holder who has taken the instrument under the following conditions:
. . . (2) That he became the holder of it before it was overdue . . . ."}
\footnotetext[83]{BEUTEL, BranNon NEGOTIABLE INSTRUMENT LAW 356 (7th ed. 1948); UNIFORM COM-
MERCIAL CODE § 3–302. The difficulty is that under UNIFORM NEGOTIABLE INSTRUMENTS LAW
§ 52 a holder in due course of an order instrument must obtain the instrument by negotiation.
And for a negotiation to take place, there must be an indorsement and a delivery of the instru-
ment. UNIFORM NEGOTIABLE INSTRUMENTS LAW § 30. A payee, however, may claim under an
order instrument although there has been no indorsement. BEUTEL, supra at 591. For an
exhaustive review of the entire question see BEUTEL, supra at 675–90.}
\footnotetext[84]{Mutual Finance Co. v. Martin, 63 So. 2d 649 (Fla. 1953); Commercial Credit Corp. v.
Orange County Machine Works, 34 Cal. 2d 766, 214 P.2d 819 (1950); Commercial Credit Co.
v. Childs, 199 Ark. 1073, 137 S.W.2d 260 (1940).}
\footnotetext[85]{In Commercial Credit Co. v. Childs, supra note 84, the defendant had purchased an auto
and given a note to the seller. This note was sold to the plaintiff who claimed as an innocent
non-
the doctrine of these cases should not be applied to a credit card sale if the issuer claims the status of a holder in due course of a negotiable bill of exchange. The credit card issuer, though not closely connected with the individual credit card sale, is certainly the moving force behind the use of the credit card in that sale and does provide the necessary forms and documents.\footnote{86}

Assuming the card issuer to be a holder not in due course of a negotiable bill of exchange, what defenses and counterclaims would be available to the card holder? The card issuer would be subject to the same "defenses" as if the instrument were non-negotiable.\footnote{87} But in the majority of jurisdictions "defenses" are construed narrowly to mean only those defenses which arise out of or are inherent in the claim itself, and are to be distinguished from counterclaims.\footnote{88} Only in a minority of jurisdictions would the card holder be able to assert a counterclaim against the card issuer, even though it arose out of the credit card sale.\footnote{89}

But even considering the card issuer to be a holder in due course of a negotiable bill of exchange, there are certain "real" defenses which may be available to purchaser for value. It appeared that the plaintiff financed many sales of the seller and, in anticipation of future financing, a previously printed assignment had been placed on the back of the defendant's note. In holding the plaintiff not to be an innocent purchaser for value of the note the court stated: "We think appellant [plaintiff] was so closely connected with the entire transaction or with the deal that it can not be heard to say that it, in good faith, was an innocent purchaser of the instrument for value before maturity. It financed the deal, prepared the instrument, and on the day it was executed took an assignment of it from the [seller] . . . . Even before it was executed it prepared the written assignment thereon to itself. Rather than being a purchaser of the instrument after its execution it was to all intents and purposes a party to the agreement and instrument from the beginning." 199 Ark. at 1077, 137 S.W.2d at 262. Commercial Credit Corp. v. Orange County Machine Works, supra note 84, relying on the doctrine of Childs, is to the same effect. There the plaintiff claimed as a holder in due course of a note given by the defendant to the seller. The defense of failure of consideration was allowed against the plaintiff, although the note was found to be negotiable, because of the proximity of the plaintiff to the sales transaction between the seller and the defendant. The plaintiff had provided the forms necessary to complete the sale, had agreed in advance to finance the sale, and had knowledge of the financial status of the seller. The court concluded: "When a finance company actively participates in a transaction of this type from its inception, counseling and aiding the future vendor-payee, it cannot be regarded as a holder in due course of a note given in the transaction and the defense of failure of consideration may properly be maintained." 34 Cal. 2d at 771, 214 P.2d at 822.

\footnote{86}{The credit card issuer, by virtue of its agreement with the merchant, is bound to provide all the forms necessary for completing the credit card transaction, and the merchant is bound to use these forms. These forms include the "sales drafts" upon which the name of the card issuer appears and which, in the plan under consideration, purport to be negotiable bills of exchange. In addition, the card issuer provides certain promotional material to the merchant which is to be displayed by the merchant to advertise the credit card plan.}

\footnote{87}{The term "defenses" used in Uniform Negotiable Instruments Law § 58 bas, in some jurisdictions, been limited strictly to defenses. Whether a counterclaim, as distinguished from a defense, will be available against a holder not in due course will depend upon the law of counterclaim in the particular jurisdiction. Yokohama Specie Bank, Ltd. v. Milbert Importing Co., 44 N.Y.S.2d 71 (Sup. Ct. 1943).}


\footnote{88}{See cases under "counterclaims allowed," note 88 supra.}
the card holder to defeat payment thereunder. One such defense is referred to as fraud in the factum, which prevents enforcement of a negotiable instrument which the maker or acceptor did not know or have reason to know he was making or accepting. A typical case is where the signature of an illiterate person is obtained on a document that is represented to be a simple contract but is actually a negotiable instrument. Nothing as flagrant appears in the credit card sale, but if the card holder could not reasonably have determined he was signing an acceptance to a bill of exchange it appears that the same principle would apply. It is doubtful that a credit card holder realizes that he may be signing the sales draft as an acceptor of a negotiable instrument, especially since the words of negotiability are in extremely small print. The card holder more likely intends his signature merely to evidence a receipt of the goods.

It is apparent that the use of a negotiable bill of exchange in the credit card transaction constitutes a potential danger to the card holder's ability to assert defenses and counterclaims against the issuer. There are no credit card cases that have passed upon this practice, and there is only a slight possibility that statutes in two states may prevent the use of a negotiable instrument to cut off defenses of the card holder. Even if the card issuer is able to establish itself as a holder in due course of a negotiable instrument, it is doubtful that it would make a regular practice of asserting its position as a holder in due course in the enforcement of claims against which card holders have substantial defenses. Such a practice might prove disastrous to the issuer's credit card plan when the thousands of card holders realized that they might be compelled to pay the issuer for goods that were, for example, never delivered, and then be required to bring an independent action against the merchant. It is probable that the credit card issuer which has introduced the purported negotiable instrument into the credit card transaction had an entirely different purpose in mind; namely, to exempt the issuer from the requirements of the California accounts receivable notice-filing statute, and thus protect itself against claims asserted by the merchant's trustee in bankruptcy.

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80 See Beutel, Brannon Negotiable Instrument Law 753–62 (7th ed. 1948).
81 Beutel, op. cit. supra note 90, at 758–62.
83 Identical statutes adopted in California and New York provide that no retail installation account (termed a retail instalment credit agreement in New York) "shall require or entail the execution of any note or series of notes by the buyer which when separately negotiated will cut off as to third parties any right of action or defense which the buyer may have against the seller." Cal. Civ. Code § 1810.9; N.Y. Pers. Prop. Law § 413(7). Whether the tripartite credit card plans meet the definition of "retail installment account"—a question which requires an affirmative answer if the quoted statute is to have any application to such plans—is considered in Part VII infra. Assuming for the moment that the statute does so apply, it is necessary to construe the word "note" to include a bill of exchange as well as a promissory note if the statute is to have any effect upon the particular credit card plan under consideration. Furthermore, it is not manifest from the wording of the statute what the result will be if it is violated. It leaves room for an interpretation that would allow an issuer to attain the status of a holder in due course, thus forcing the buyer-card holder to resort to the remedies afforded by accompanying statutes. Cal. Civ. Code § 1812.7, for example, would permit the card holder to escape payment of the service charge, hardly an effective remedy when he has a defense against the merchant which would entirely defeat the issuer's action if it were not for the negotiable instrument.
84 California statutes require the assignee of "accounts" to file notice with the county recorder in order to perfect assignments against third parties. Cal. Civ. Code §§ 3017–3029. Exempted from the definition of an account is "any debt evidenced by or arising under a ... bill of exchange . . . ." Cal. Civ. Code § 3017(1)(a). Cal. Civ. Code § 955 provides in part: "The transfer . . . of an obligation to pay money represented by . . . a non-negotiable instru-
THE CARD HOLDER'S RESPONSIBILITY TO PAY FOR PURCHASES MADE WITH HIS CARD

When purchases are made with a credit card by the holder of the card or by an authorized user of the card, the card holder's liability to the card issuer for such purchases has no standing under § 70c, 11 U.S.C. § 110c, e (1958); Costsello v. Taylor, 94 F.2d 782 of the District of Columbia Circuit. Under the direct obligation theory, no debt is ever owed from the card holder to the merchant. Thus, there could be no assignment of accounts from the merchant to the issuer and no need to file notice under Cal. Civ. Code § 3019. Rather, there would be an assignment only of an instrument or piece of paper from the merchant to the issuer, evidencing the fact that an account had arisen directly between the card holder and the issuer. If, on the other hand, the card holder's obligation to pay for goods and services is owed to the merchant who assigns this right to the issuer, it is likely that the transfer of the charge slip would be construed as an assignment of an account subject to the notice-filing statute. See Durkin v. Durkin, 133 Cal. App. 2d 283, 284 P.2d 185 (1955). If the issuer failed to file notice in accordance with the statute, he would lose priority to another assignee of the same account for value and without notice who first filed notice, and the assignment would be invalid as against any creditor of the merchant without actual notice. Cal. Civ. Code § 3018. Furthermore, under § 70e of the Bankruptcy Act, the merchant's trustee in bankruptcy, exercising the right of any actual creditor having a provable claim and protected by the notice-filing statute, would be able to set aside as voidable transfers any assignments made by the bankrupt to the issuer which were not perfected by notice-filing and were uncollected at the time of bankruptcy. And under the doctrine of Moore v. Bay, 284 U.S. 4 (1931), the trustee's recovery would not be limited to the extent of the actual creditor's claim which gave him standing under § 70e. Rather, the unperfected assigned accounts would be voidable in toto for the benefit of the bankrupt's entire estate. See 4 Collier, Bankruptcy ¶ 70.95, at 1798 (14th ed. 1959). The issuer would be reduced to the status of an ordinary unsecured creditor of the bankrupt merchant. Markovitz v. Taylor, 94 F.2d 782 (3d Cir. 1938). Even if there were no actual creditor whom the trustee could represent under § 70e, he could obtain the same result by representing the hypothesized creditor of § 70c. See Constance v. Harvey, 215 F.2d 571 (2d Cir. 1954), cert. denied, 348 U.S. 913 (1955); Marsh, Constance v. Harvey—The "Strong-Arm Clause" Re-Evaluated, 43 Calif. L. Rev. 65 (1955). An alternative holding in Costello v. Bank of America Nat'l Trust & Sav. Ass'n, 246 F.2d 807 (9th Cir. 1957), affirms 141 F. Supp. 225 (N.D. Cal.1955), indicates that in California the merchant's trustee in bankruptcy would have no standing under § 70 to set aside non-filed assigned accounts which had been collected by the issuer prior to bankruptcy. Costello, however, did suggest that the trustee may be able to set aside as voidable preferences under § 60a (64 Stat. 24 (1950), 11 U.S.C. § 96a (1950)) accounts collected by the assignee within four months of bankruptcy; but since the credit card issuer, like the factor, purchases the accounts of the merchant without recourse, it is doubtful that the issuer-merchant relationship is that of creditor and debtor as required for the operation of § 60a. See Treister, Effect of Failure to Record Notice of Assignment of Accounts Receivable, 33 Los Angeles B. Bull. 179, 184-85 (1958); Koessler, Assignment of Accounts Receivable, 33 Calif. L. Rev. 40, 53 n.39 (1945). Since the Costello rule is dependent upon an interpretation of the California notice-filing statute, it could be upset by a different interpretation by the state courts or by a legislative amendment.
purchases seems clear on general contract principles. The only matter that requires articulation is the underlying contractual theory of his liability.

On the other hand, under what circumstances the card holder must pay the issuer for purchases made by an imposter who has found, stolen, or misappropriated his card presents a more difficult problem. Here the card holder's liability depends upon the binding effect of a provision printed by the issuer on the reverse side of the credit card, purporting to make the card holder liable for all purchases made with the card until the issuer receives notice of its loss.

A. Card Holder's Liability for Authorized Purchases

One who applies for and is issued a credit card often expressly agrees to pay for all authorized purchases. In addition, almost all cards contain a printed provision on their reverse sides to this effect, and since the provision is a reasonable one, the card holder should be bound by it. An employee has been held liable for the amount of credit purchases made by himself where his company had taken a card membership in his behalf and he had subscribed, retained, and used the card. The card contained a printed provision on its reverse side stating that the employer and the employee both agreed to pay for the charges incurred by him and to accept all drafts drawn on them for such charges.

One who receives a credit card unsolicited through the mails will also be liable for all authorized purchases. A general principle of contract law is that although an offeror has the power to specify the manner in which his offer is to be accepted, he does not possess the power to make the offeree's silence operate as an accept-

Assuming that the credit card transaction involves the assignment of accounts, in order to determine the remedies of the merchant's trustee in bankruptcy against the issuer in other jurisdictions it is necessary to refer to the statutes or case law of the particular state. In states that follow the American rule by judicial decision (i.e., an assignment is perfected against third parties upon execution) and in states that have enacted this rule by so-called "validation statutes," the trustee would have no rights under § 70 of the Bankruptcy Act. His only possible remedy against the issuer would be to attack assignments made within four months of bankruptcy under § 60a, and the existence of even this remedy, as previously indicated, is doubtful. Of the more than 30 states that have enacted notice-filing statutes, the particular enactments and interpretive decisions must be consulted because of the lack of uniformity from state to state. See generally, 3 COLIER, BANKRUPTCY ¶ 60.48 (14th ed. 1956); 4 COLIER, BANKRUPTCY ¶¶ 70.77[2], 70.83[4] (14th ed. 1959); Koessler, supra; Conwill & Ellis, Much Ado About Nothing: The Real Effect of Amended 60(a) on Accounts Receivable Financing, 64 HARV. L. REV. 62 (1950). See also UNIFORM COMMERCIAL CODE § 9-302(1)(e).

This assumes, of course, that he has no defenses or counterclaims against the merchant which he is able to assert against the issuer. See Part IV supra.

The proposition that the card holder should not be held to unreasonable provisions is developed at note 135 infra.

Franklin Nat'l Bank v. Kass, 19 Misc. 2d 280, 184 N.Y.S.2d 783 (Sup. Ct. 1959). Another aspect of this case is discussed at note 77 supra. The employee was sued because his employer had gone bankrupt. It does not appear from the facts whether the purchases were made for the personal benefit of the employee or were entertainment expenses properly incurred for the benefit of the employer's business. In order to hold an employee liable for purchases that represent legitimate business expenses when the card is given to him by his employer, the card issuer should be required to prove that the employee had fair notice of the issuer's intention to impose such liability upon him. Of course, if an employee applies directly to the issuer for a card, uses it for business expenses, pays the issuer for the charges incurred, and is reimbursed for the expenses by his employer, he should not be heard to complain in the event of his employer's bankruptcy, for he, not the card issuer, clearly accepted the risk of his employer's financial responsibility.

Restatement, Contracts §§ 29, 52 (1932); 1 Corbin, Contracts § 67 (1950).
ance merely because the terms of the offer purport to attach that effect to it.\textsuperscript{90}

Thus, when a card-issuing company mails an unsolicited card accompanied by a letter which asserts that unless the card is returned to the issuer the addressee will be entered on the issuer's records as a card-holding member, no duty is thereby imposed upon the addressee to speak.\textsuperscript{100} But should his silence, which alone would serve as a rejection of the offer, be coupled with behavior inconsistent with a rejection, it will be deemed an acceptance and an implied promise to pay for authorized purchases made with the card.\textsuperscript{101} Certainly if the offeree makes one credit purchase with the card, his behavior would indicate an acceptance.\textsuperscript{102}

It would seem that the first credit purchase not only obligates the offeree to pay for that purchase and all future authorized purchases, but also amounts to an acceptance of all the provisions imprinted on the card which would bind a person who applies for and is granted a credit card. Since one of these provisions purports to make the card holder liable for all purchases, authorized or unauthorized, made before the card holder reports the loss of the card, it may be crucial in certain cases to determine whether any act short of making one credit purchase with the card amounts to an acceptance on the part of the recipient of an unsolicited card.\textsuperscript{103} If so, a person who receives a card unsolicited and never uses it for its intended purpose will nevertheless be liable for unauthorized purchases made before he reports the loss of the card.

\textbf{B. Card Holder's Liability for Unauthorized Purchases}

Commonly, the issue of the card holder's liability for unauthorized purchases arises when his card is lost or stolen, and the card issuer brings suit against him to recover the amount of purchases made by an imposter. Today, nearly all credit cards contain a printed provision on their reverse sides which purports to make the holder of the card liable for all purchases made with it until the issuer receives written notice of the loss or theft of the card.

Of the seven reported imposter cases,\textsuperscript{104} the earliest four dealt with two-party

\begin{footnotes}
\item[90] Albrecht Chem. Co. v. Anderson Trading Corp., 298 N.Y. 437, 84 N.E.2d 625 (1949); Restatement, Contracts § 72 (1932).
\item[100] "[A]nn offeror . . . can not force the offeree to take his pen in hand, or to spend a two-cent stamp, or to open his mouth, under penalty of being bound by a contract if he does not." 1 CORBIN, CONTRACTS § 73 at 231 (1950).
\item[101] Austin v. Burge, 156 Mo. App. 286, 137 S.W. 618 (1911) (receiving and reading unsolicited newspapers when it is known they are not offered as gratuity); Indiana Mfg. Co. v. Hayes, 155 Pa. 160, 26 Atl. 6 (1893) (taking control of unordered goods from carrier); 1 CORBIN, CONTRACTS § 75 (1950).
\item[102] An offeree's silence operates as an acceptance "where the offeree with reasonable opportunity to reject offered services takes the benefit of them under circumstances which would indicate to a reasonable man that they were offered with the expectation of compensation." Restatement, Contracts § 72 (1) (a) (1932).
\item[103] Assuming for the moment that one who has accepted the issuer's offer is bound by the provision making him liable for purchases of an imposter, suppose that upon receiving an unsolicited card, Jones puts it in his billfold intending never to use it for a credit purchase, but for the sole purpose of using it as a credit reference for cashing personal checks. This exercising of dominion over the card might well be construed as constituting an acceptance of the terms of the issuer's offer. Hence, Jones' retention of the card would impose the same duties upon him that are imposed upon the card holder who uses his card for credit purchases: \textit{if} he uses it for purchases (his acceptance of the offer does not obligate him to do so), he must pay the purchase price of the goods and services so obtained, and if he loses the card he is not relieved of liability for subsequent purchases made with it until he reports its loss to the issuer.
\item[104] See Annot. 158 A.L.R. 762 (1945).
\end{footnotes}
situations where there was no such written provision. But these early cases are of more than historical interest because they represent the only judicial guides for deciding a modern tripartite plan imposter case should a court rule as a matter of law that the notice of loss provision is not binding on the card holder, or should a court determine that it is a jury question as to whether the provision constituted a part of the contract.

The first of these cases, *Wanamaker v. Megary*,
 relying upon the equitable rule that as between two innocent parties he who makes the loss possible should bear the consequences, held a credit coin holder liable for purchases made by an imposter before loss of the coin was reported. In *Lit Bros. v. Haines*, the court ruled that in the absence of a contract to the contrary a coin holder is not liable for purchases made by an imposter. *Gulf Refining Co. v. Plotnick* stated the rule that in the absence of an express contract, each party owes the other a duty of due care—the card holder in using the card and the issuer-merchant in honoring it. This approach, which consists of weighing the negligence of the parties, not only seems to resolve the holdings of the two earlier cases on their respective facts, but also provides the most reasonable method of deciding a tripartite plan imposter case where the court or jury decides that a notice of loss provision printed on a credit card is not binding upon the card holder.

It becomes necessary, then, to determine whether the card holder is bound by the "notice of loss" provision printed on the reverse side of most credit cards.

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105 In *Union Oil Co. v. Lull*, 349 P.2d 243 (Ore. 1960), the court said that if the issue had been properly raised it would have presented a jury question under the circumstances of that case, provided there was proof that the card holder was not aware of the provision. The circumstances cited were: the credit card application form did not refer to the holder's liability for unauthorized purchases, and the notice of loss provision was in very small print on the back of the card. *Id.* at 246–47.


107 There was no evidence that the issuer-merchant was negligent, whereas the coin holder was deemed to be at fault for not keeping the coin in a secure place in her purse. For a brief description of a credit coin see note 6 supra.

The court also advanced the bold theory that a credit coin is similar to a negotiable instrument payable to bearer, a notion that has been systematically rejected or ignored in all subsequent credit card cases.

108 98 N.J.L. 658, 121 Atl. 131 (Sup. Ct. 1923).

109 This broad holding must be viewed in the light of the evidence which suggested the plaintiff's negligence. The imposter made a number of purchases, and at his request the plaintiff shipped the goods to the imposter's address, which the plaintiff knew to be different from the defendant's.

The broad rule that a coin holder is not liable for purchases made with his coin by one who wrongfully gained possession of it was also stated in *Jones Store Co. v. Kelly*, 225 Mo. App. 833, 36 S.W.2d 681 (1931), where a verdict for the plaintiff was reversed because the charge to the jury omitted the defendant's theory as to the terms of his oral agreement with the plaintiff.


111 *Id.* at 150. Acknowledging that ordinarily a card holder should not be held liable for unauthorized purchases, the court held that it was a question for the jury where the defendant failed to notify the plaintiff of the loss of the card even after receiving bills from the plaintiff for purchases made by an imposter.

112 In one case the court declared that the card holder was bound by the provision. *Magnolia Petroleum Co. v. McMillan*, 168 S.W.2d 881 (Tex. Civ. App. 1943). In another, the card holder admitted that the provision formed at least an implied contract to which he was bound. *Gulf Ref. Co. v. Williams Roofing Co.*, 208 Ark. 362, 186 S.W.2d 790 (1945). In a third case the issue was not properly raised by the card holder in the trial court. *Union Oil Co. v. Lull*, 349 P.2d 243 (Ore. 1960). *But see note 105 supra.*
and if the card holder is so bound, to determine the proper interpretation of the provision.

It has often been stated as a general rule of contract law that the acceptance of an instrument or document that purports to be a contract operates as an assent to the terms contained therein, whether or not the one who accepts it actually reads the terms. Of all the documents that have been held to be either within or without the purview of this rule, the bank deposit passbook is the one most similar in function to the credit card.

On the ground that a passbook purports to be a contract, most of the cases follow the rule that a depositor, by accepting and retaining a passbook, is bound by the rules printed therein, even though he did not expressly assent to them and they were never brought to his attention. It is well recognized, however, that a provision purporting to insulate the bank from liability for payment of the depositor’s funds to an imposter will not protect the bank from its own negligence.

This rule resolves many of the cases that have had to determine the binding effect of provisions in small print on various types of instruments. See generally 1 Williston, Contracts §§ 90A, 90B, 90C, 90D (3d ed. 1957); Note, Contract Clauses in Fine Print, 63 Harv. L. Rev. 494 (1950). Most courts hold that a person who accepts a bill of lading, express receipt, or warehouse receipt is bound by its legibly printed provisions which are not contrary to public policy. See e.g., American Ry. Express Co. v. Lindenberg, 260 U.S. 584 (1923) (express receipt); Taussig v. Bode & Haslett, 134 Cal. 260, 66 Pac. 259 (1901) (warehouse receipt). As to whether a person will be bound by provisions printed on passenger tickets, the result may depend upon the appearance and size of the ticket. See Goddard, Passenger Tickets as Contracts, 25 Macq. L. Rev. 1 (1926). As to steamship passenger tickets, compare Fonseca v. Cunard S.S. Co., supra, with The Majestic, 166 U.S. 375 (1896). A provision printed on a carrier baggage check, parcel room ticket, or parking lot ticket purporting to limit the bailee’s liability is usually held not binding in the absence of proof that the bailor read the provision or that it was brought to his attention at the time of the bailment so as to constitute a special contract. See e.g., Klar v. H. & M. Parcel Room, Inc., 270 App. Div. 538, 61 N.Y.S.2d 285 (1946), aff’d mem. 296 N.Y. 1044, 75 N.E.2d 912 (1947) (parcel room); Sandler v. Commonwealth Station Co., 307 Mass. 470, 30 N.E.2d 389 (1940) (parking lot); Ferris v. Minneapolis & St. L. Ry., 143 Minn. 90, 173 N.W. 178 (1919) (baggage check). While the bailee may limit his liability by such a special contract, most courts will not allow him completely to contract away liability for his own negligence. See e.g., Jersey Ins. Co. v. Syndicate Parking, Inc., 78 N.E.2d 692 (Ohio App. 1948). See also 17 U. Cinn. L. Rev. 305 (1948); Jones, The Parking Lot Cases, 27 Geo. L.J. 162 (1938).

In contrast to the ordinary bailment ticket, the passbook and credit card are intended for more or less permanent use. They serve primarily as a means of identification—one enabling its owner to withdraw money from an account, the other enabling him to charge goods and services to an account. They are instruments that are retained by their owners for a long period of time, with considerable opportunity for the owners to read the printed provisions. In the case of bank passbooks, the provisions are usually printed on the inside front cover. The credit card provisions appear either on the reverse side of the card or on the inside front cover of the wallet-sized merchant directory, if the particular credit card plan issues such directories.


These provisions are to the same general effect as the credit card provisions. They usually state that until the depositor gives the bank notice of the loss or theft of his passbook, the bank will not be responsible for any loss sustained by the depositor arising from an unlawful presentation of the passbook and withdrawal of the depositor’s funds.
or bad faith, and accordingly it has been held that if the bank has not exercised reasonable care in paying over the depositor's funds to an imposter, it is liable to the depositor for the amount of the unauthorized withdrawal. 117 It is also the rule that the contributory negligence of the depositor in not discovering or reporting the loss of his passbook will not defeat his recovery. 118

Because the credit card and bank passbook serve equivalent functions in similar transactions and because the contractual provisions involved are basically the same, 119 it is submitted that the rules developed in the passbook cases should govern credit card imposter cases. Thus, the card holder should be held bound by the provision imposing liability upon him for unauthorized purchases made before he reports the loss of his card to the issuer, but the issuer should be able to recover the amount of such purchases only if it has been free from negligence; whether the card holder was negligent in losing the card or in not discovering or reporting its loss should be deemed irrelevant. 120

As stated, these rules leave one important question unanswered. The passbook situation involves two parties only, and of course the bank is vicariously liable for the negligence of its agents. In the tripartite credit card situation, however, the merchant is not an agent of the card issuer, but an independent contractor. Since the negligence in question will usually be that of the merchant who makes the sale to the imposter rather than that of the issuer, it is important to determine whether the merchant's negligence will defeat the issuer's action against the card holder where the card holder failed to notify the issuer of the loss of his card prior to the imposter's purchases.

This issue was first presented in the case of Gulf Refining Co. v. Williams Roofing Co., 121 where the plaintiff, an oil company which issued its own credit


118 Cases cited note 117 supra.

"Even if plaintiff was negligent, as claimed, that did not excuse the bank officers from exercising ordinary care to prevent one who they knew was not a depositor from obtaining money upon a forged order, nor relieve the bank from liability for payments negligently made to the wrong person. The question of contributory negligence is not involved in the case." Chase v. Waterbury Sav. Bank, note 117 supra at 302, 59 Atl. at 40.

119 The passbook provision tells the depositor: "Until you report notice of loss, we will not be responsible for any unauthorized withdrawals." The credit card provision tells the card holder: "Until you report notice of loss, you will be responsible for any unauthorized purchases." In either case, when the provision is strictly construed its effect is to relieve the drafter of the clause from a duty of reasonable care. It would seem to be of no legal significance that in the passbook case the depositor is the plaintiff suing to recover the amount of his account which was negligently paid by the bank to an imposter, whereas in the credit card case the card holder is the defendant denying his liability for unauthorized purchases made with his card because of the card issuer's negligence.

120 As in the passbook cases, evidence of the card holder's negligence would not avail the issuer, because such a showing could not relieve the issuer of his duty to exercise reasonable care to detect an imposter. That the proposed set of rules is not a radical innovation will subsequently appear, for all three of the imposter cases in which the card contained a notice of loss provision are entirely consistent with them. Indeed, the most recent case, Union Oil Co. v. Lull, 349 P.2d 243 (Ore. 1960), discussed the passbook rules with approval.

121 208 Ark. 362, 186 S.W.2d 790 (1945).
cards, brought a suit in equity to recover an amount deducted and withheld by the defendant card holder from its running account with the company. The amount in dispute represented purchases made with the defendant's card by an imposter at retail outlets which distributed the plaintiff's products. There was conflicting evidence on the question of whether the defendant, in accordance with the provision printed on his card, had notified the plaintiff of the loss of his card. But the evidence did show numerous instances of collusion between the imposter and the service station dealers who had honored the card. In affirming the trial court's decree dismissing the plaintiff's suit on the merits, the court stated:

If these dealers were independent contractors and not agents of appellant, it necessarily follows that they were assignors of the forged invoices upon which appellant seeks to recover. [A]ppellant, as assignee, acquired no greater right than his assignors. It is well-settled that the assignment of a non-negotiable instrument passes the rights of the assignor subject to all defenses that would be available if the assignor brought suit direct on the instrument. [Citations].

This reasoning was followed in Union Oil Co. v. Lull, where the defendant had not reported the loss of his card before the unauthorized purchases were made. The jury had returned a verdict for the defendant upon the trial court's instruction that the defendant would be excused from performance of the notice of loss provision if he exercised reasonable care in possessing and using the card and if he reported its loss within a reasonable time. On appeal, the Oregon Supreme Court held that the trial court had erred in its instruction and that the notice of

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122 The facts were not all favorable to the plaintiff. The card was stolen by an employee of an authorized retail distributor of the plaintiff's products after the defendant had inadvertently left the card at the service station after making a purchase with it. In a ninety-day period the employee forged 223 invoices amounting to $975. There was evidence that some of the dealers who honored the card used by the imposter were acquaintances of his. Most of the invoices showed that the dealers had written down fictitious license numbers. Some invoices were made out for fictitious merchandise, others evidenced sales of complete sets of tires which were not the size required for the imposter's automobile.

Furthermore, the defendant had typed across the face of his card the words, "Good for Truck only." The imposter did not drive a truck. The court said that the defendant had a right to put these words on his card, and that anyone honoring the card must do so only in accordance with this limitation. One writer has criticized this reasoning of the court on the ground that it allows one party to bind another with a unilateral act. Claflin, The Credit Card—A New Instrument, 33 Conn. B.J. 1 (1959). This criticism is not justified if the provision typed on the card by the card holder is not considered in the light of contract law, but as only one element in determining whether or not the merchant made a reasonable inquiry into the authority of the imposter to use the card.

123 208 Ark. at 367, 186 S.W.2d at 793, 794. This language is not inconsistent with the case of Magnolia Petroleum Co. v. McMillan, 168 S.W.2d 881 (Tex. Civ. App. 1943), which held the defendant liable for an imposter's purchases. There the card provision required the card holder to surrender his card to the issuer before being relieved of liability for any purchases made with the card. The court indicated that this provision would have been fulfilled had the card holder notified the issuer of the misappropriation of the card. But no notification was given, and the negligence of the issuer or retail dealers was not in issue.


125 The printed term on the credit card provided: "The customer to whom this card is issued guarantees payment within 10 days of receipt of statement, of price of products delivered or services rendered to anyone presenting this card, guarantee to continue until card is surrendered or written notice is received by the company that it is lost or stolen." The reference in this provision to guarantee led the court to couch much of its decision in the language of guaranty and indemnity. This semantic barrier could have been avoided by simply considering the card holder's "guarantee" to be nothing more than a promise to pay for all purchases until reporting loss of his card.
loss provision could not be interpreted so as to absolve the card holder from liability if he exercised due care. The court stated that this provision must be construed as subjecting the card holder to liability for unauthorized purchases made before the loss of his card was reported, but only if the plaintiff and its privies exercised due care to ascertain the authority of the person using the card.\textsuperscript{128} The court, quoting the \textit{Williams} case, instructed the trial court that the plaintiff’s rights could not transcend those of the independent dealers who assigned the invoices to the plaintiff. The court also stated that the burden of proving that the dealers had made reasonable inquiry was upon the plaintiff.\textsuperscript{127} Thus, upon retrial, the issuer’s recovery would be barred if it could not prove that the independent dealers had been free from negligence.\textsuperscript{128}

The rule established by \textit{Williams} and \textit{Lull} is that the merchant’s\textsuperscript{129} in not detecting an imposter will bar the issuer’s recovery

\textsuperscript{128} In support of this point, the court drew an analogy to the bank passbook cases where the bank must exercise reasonable care in making inquiry into the authority of the withdrawer; it also relied upon cases holding that a person receiving a forged check owes a duty of reasonable inquiry to the drawee bank. 349 P.2d at 250, 251.

\textsuperscript{127} 349 P.2d at 254. Although the court acknowledged that there was scant authority for this proposition, it evidently felt that public policy justified placing the burden of proof on the card issuer.

\textsuperscript{129} The court said the fact that the imposter’s auto had an Idaho license plate while the credit card showed the defendant’s state of residence to be Oregon was sufficient to raise a jury question as to whether a duty of reasonable care required the retail dealers to inquire further into the authority of the imposter to use the card. 349 P.2d at 253, 254.

\textsuperscript{127} The most obvious example of negligence on the part of a merchant would be his honoring an expired card when the expiration date is printed on the face of the card. In the bank passbook cases negligence has often been found in situations where the bank clerk failed to make further inquiry when a comparison of the signature on the withdrawal slip and the signature of the passbook holder would have made a reasonable man suspicious. See cases cited note 117 supra. Many of the all-purpose credit card issuers, however, do not require card holders to sign their cards before using them. Even when the card holder signs his card, many merchants do not question a variance in the signatures, apparently because of the fact that card holders sometimes allow relatives or friends to use their cards. Perhaps in the case of a small purchase the convenience of not making inquiry outweighs the risk that an unauthorized person is using the card. But a point is reached, perhaps a $10 or $25 sale, depending on the circumstances, where a reasonable man would require the card user to offer further identification if the signatures on the charge slip and card were manifestly unlike or if there were no signature on the card with which to compare the one on the charge slip. At a minimum, due care in such cases would seem to require that the merchant elicit reasonable proof that the card user bears the same surname as the person whose name appears on the card. Even where the signatures on visual inspection appear to be drawn by the same hand, the merchant, in the case of particularly large sales, should be required to obtain further proof of the card user’s identity. If the merchant fails to adhere to a standard of reasonable care in verifying the identity of the card user and an imposter is thereby enriched, the issuer should not be heard to complain to the card holder, since the issuer can and sometimes does retain by contract a right of recourse against the merchant in such situations.

\textsuperscript{130} There would seem to be negligence on the part of the issuer if it became aware that the card holder’s charge balance had exceeded any prearranged credit limit and it failed to make an inquiry of him within a reasonable time.

In the consumer card plans the issuer requires the merchant to telephone the issuer’s credit department to obtain prior authorization for any sale about to be concluded when the amount of the sale will exceed the card holder’s one-purchase credit limit. This “floor limit” may vary from $15 to $100, depending on the plan and the particular card holder, and is indicated by a symbol printed on the face of the card. The sanction for the merchant’s not obtaining prior authorization would seem to be effective: in event of noncollection for the sale, the issuer has recourse to the merchant for the full amount of the sales slip.

This built-in protection is no doubt installed for the selfish interests of the issuer, \textit{i.e.},
against the card holder, even though the unauthorized purchases are made before the card holder notifies the issuer of the loss of his card. But in both of these cases the rule was based upon what this Comment has termed the "assignment" theory. The card holder was permitted to assert the merchant's negligence as a defense to the action brought by the issuer because the issuer was treated as an assignee of the right to collect the purchase price of the goods obtained with the card holder's card. In neither case did the court recognize the "direct obligation" theory, under which the issuer's right to receive payments from the card holder is interpreted as being derived not from an assignment, but from the card holder's promise to make payments to the issuer. Thus, it is important to determine whether the rule of Williams and Lull has any vitality if the assignment theory is rejected in favor of the direct obligation theory.

Earlier in this Comment, it was submitted that if the legal incidents of the credit card transaction are to be controlled by the direct obligation theory, the card holder's promise should be construed as being conditional upon the merchant's fulfillment of his obligations under the contract of sale. It was concluded to enable it to detect sudden, extravagant spending by one of its card holders or by an imposter. But this checking system also works to the benefit of the card holder whose card has fallen into the hands of an imposter, for once an imposter has made a series of purchases, each in excess of the card holder's floor limit, which together exceed the card holder's total credit limit, the issuer is in a position to contact the card holder or have the merchant confiscate the card. The clever imposter who makes a series of purchases, each within the floor limit of the card holder, will not be detected so quickly; but even this scheme should be disclosed in a matter of one to three days after the total credit limit is exceeded, particularly where the geographical proximity of merchant and issuer permits a rapid assignment of sales slips to the issuer.

The entertainment card plans have very ineffective means of detecting imposters, both because merchants transmit sales slips to the issuer at less frequent intervals and because merchants are often authorized to permit a card user to accumulate a bill of as much as $500 before getting telegraphic credit clearance from the issuer. The Hilton company, however, has lowered this amount from $500 to $100 in a move evidently intended to decrease bad debt losses (see note 17 supra) and to prevent a recurrence of the Miraglia incident (see text accompanying notes 1-2 supra). Jones, Errant Chargers, Wall Street Journal, April 26, 1960, p. 1, col. 1.

It is to be noted that Williams and Lull involved oil company credit cards which can be the basis of a two or three-party transaction, depending on whether the card is used at a company-owned or independently-owned service station. Since the Williams court assumed that the dealers were independent contractors, and the Lull facts showed that many of the dealers had this status, the decisions of both courts are directly applicable to the tripartite all-purpose credit card plans.

But it was also acknowledged that it would be possible, under the direct obligation theory, to construe the card holder's promise to pay the issuer as obligating him to pay regardless of any defenses he may have against the merchant. See text accompanying notes 64-65 supra. It is submitted that if the card holder's promise "to pay for all purchases made with this card until reporting its loss," which appears in fine print on the reverse side of credit cards, is so construed, it should be held an unreasonable provision and therefore not binding upon him, in the absence of proof that he expressly assented to it. See Los Angeles Inv. Co. v. Home Sav. Bank, 180 Cal. 601, 182 Pac. 293 (1919), where it was held that a depositor was not bound by a printed provision in a commercial account passbook that purported to allow him a period of only ten days from the receipt of each monthly statement to dispute the genuineness of checks. The court remarked that the provision "very materially changed the usual obligations of a bank to its depositors" and that to enter such an unreasonable agreement a depositor must do so deliberately. The court distinguished the cases holding a depositor to provisions printed in his passbook (see note 115 supra and accompanying text) on the ground that the provision
that this interpretation would allow the card holder to assert against the issuer any defense he may have against the merchant arising from the credit card transaction. The merchant's negligence in failing to exert due care in an attempt to detect an imposter would certainly constitute such a defense. Thus, it would appear that the rule of *Williams* and *Lull* is a correct statement of the law whether the assignment theory or the direct obligation theory is used to explain the legal relationships of the three parties to the credit card transaction.

A few jurisdictions, however, may hold that the card holder is not bound by the notice of loss provision which appears in small print on the reverse side of his card in the absence of his knowledge of or assent to the provision. Such jurisdictions might well resort to a balancing process, suggested by the early credit card cases, consisting of weighing the negligence of the issuer and merchant against that of the card holder.

VI

THE CREDIT CARD AND CRIMINAL LIABILITY

Because of the lack of direct statutory and judicial authority, it is important to determine whether existing criminal law can be invoked to impose adequate criminal sanctions upon card holders and unauthorized card users for both the fraudulent procurement and use of credit cards. The little authority that does exist is contained in seven recently enacted statutes which specifically define some of involved in those cases was a reasonable and customary one.

Of the many cases holding that a person is not bound to a provision printed in small print, it is often difficult to determine whether the basis of the decision is that a reasonable man would not recognize the instrument as a proposed contract, that the person did not expressly assent to the provision, or that the court considers it unjust to hold a person to an unfavorable term of which he was not given fair notice. For three cases that rest in part upon the latter ground, see *French v. Bekins Moving & Storage Co.*, 118 Colo. 424, 195 P.2d 968 (1948) (storage receipt); *Ferris v. Minneapolis & St. L. Ry.*, 143 Minn. 90, 173 N.W. 178 (1919) (baggage check); *The Majestic*, 166 U.S. 375 (1897) (steamship passenger ticket).

Legal writers have increasingly criticized the courts for not recognizing the reality that there is no freedom of contract in situations where a large organization employs experts to draft standard provisions which individuals contracting with the organization have no choice but to accept. See Kessler, *Contracts of Adhesion—Some Thoughts About Freedom of Contract*, 43 COLUM. L. REV. 629 (1943); Ehrenzweig, *Adhesion Contracts in the Conflict of Laws*, 53 COLUM. L. REV. 1072, 1088–90 (1953). It has been suggested that to compensate for the inequality manifested by disparity of economic power or by one party's employing an expert drafter the courts should exercise a systematic veto power over all unreasonable and customary fine print provisions. *Note*, 63 HARV. L. REV. 494, 504 (1949). *Cf. Uniform Commercial Code* § 2–302. It is unnecessary, however, to go this far in deciding that the credit card provision does not preclude the card holder, in a suit brought by the issuer, from setting up any defenses he has against the merchant arising out of the sale, including the negligence of the merchant in an imposter case. It need only be said that the provision itself is not amenable to such an unreasonable interpretation. It is more reasonable to construe the card holder's promise of payment as conditional upon the merchant's non-negligent and satisfactory completion of the sale.

A few cases have held that a person who accepts a document, normally considered as one of those that purports on its face to be a contract, is not bound by its printed provisions unless he reads or assents to them. See, e.g., *Highfield v. First Nat. Bank*, 45 Ga. App. 431, 165 S.E. 135 (1932) (bank passbook); *Colgin v. Security Storage & Van Co.*, 208 La. 173, 23 So. 2d 36 (1945) (warehouse receipt). Such cases are not in accord with the weight of authority. See note 113 *supra*.

*See text accompanying notes 110–12 supra.*
the criminal liabilities that may be incurred by persons using credit cards and in the few reported cases where credit card users have been prosecuted under criminal statutes of more general applicability.

A. Theft of the Credit Card Itself

In instances where the card holder applies to the issuer for a credit card, he must fill out an application form which usually requests the name, occupation, places of business and residence, and credit references of the applicant. If the issuer materially relies upon the representations made in the application form and subsequently issues a credit card to the applicant, the applicant's submission of false information with an intent to defraud may result in a prosecution for obtaining property (the credit card) by false pretenses.\footnote{This crime requires proof that the victim parted with property in material reliance on a false pretense or representation made with intent to defraud. See authorities cited in notes 153-56 infra.}

Similarly, once a credit card has been issued to a card holder, the card may be the subject of larceny and its wrongful taking may result in a conviction of theft.\footnote{At common law written documents were not subject to larceny, nor could it be alleged that the paper itself was subject to larceny because by a fiction the paper was merged into the document. But it is now generally accepted that written documents are subject to larceny. See Hall, Theft, Law and Society 81-97 (2d ed. 1952). N.Y. Pen. Law § 1290 refers to "articles of value of any kind" in describing property that is subject to larceny. Cal. Pen. Code § 484 refers to "money, labor or real or personal property" as the subject matter of theft. These statutes seem sufficiently broad to include the credit card.}

Larceny, for example, will occur where a person appropriates to his own use a lost or misplaced credit card without making a reasonable effort to establish the identity of the owner and return the card to him.\footnote{Cal. Pen. Code § 485 deals with this situation, providing: "One who finds lost property under circumstances which give him knowledge of or means of inquiry as to the true owner, and who appropriates such property to his own use . . . without first making reasonable . . . efforts to find the owner and restore the property to him, is guilty of theft."} In most cases, the finder should have no difficulty in ascertaining the identity of its owner since a credit card displays the name of the issuer and the name and address of the card holder.

Although a card holder's fraudulent acquisition of a credit card from the issuer will constitute the crime of obtaining property by false pretenses and although a person's wrongful taking or appropriation of a previously issued credit card will constitute larceny, it remains to be determined whether such acts amount to grand or petit theft. The resolution of this problem depends upon the value attached to the credit card.\footnote{Cal. Pen. Code § 487 provides: "Grand theft is theft committed in any of the following cases: 1. When the money, labor or real or personal property taken is of a value exceeding two hundred dollars ($200) . . . ."}

Although it might be argued that the value of a credit card is to be determined by the value of the goods which might be obtained with it, thus subjecting the defendant to a conviction of grand theft, it would seem that the value of the card is no greater than the cost of its manufacture when it is obtained from the issuer by false pretenses. But when a card is stolen from a card holder, its value would also include any fees which the card holder may have paid to obtain the card.\footnote{Annual fees for entertainment cards range from $5 to $6. See text at note 18 supra. Consequently, it seems that a theft of a credit card would constitute not grand, but petit theft.}

The California Penal Code provides that if the thing stolen is a written instrument, its value is to be determined by the amount of money which in any continu-
gency might be collected with it.\textsuperscript{143} Whether a credit card is a written instrument within the meaning of the statute is doubtful,\textsuperscript{144} but even if it were so considered, no \textit{money} may be collected through its use, although it may be used to obtain property and services of considerable value. Thus, it appears that the theft of a credit card would not fall within the terms of the statute. As previously stated, however, a credit card has sufficient value to support a petit theft conviction.\textsuperscript{146}

\textbf{B. Submission of False Information on a Credit Card Application Form}

In California, a person who knowingly submits false information with respect to his financial condition or ability to pay in a written application for credit commits a misdemeanor.\textsuperscript{146} Thus, a credit card applicant who submits this type of false information may be prosecuted even though a credit card was not issued to him in reliance upon the false statements contained in the application form.

\textbf{C. Special Statutes Imposing Criminal Sanctions on the Card User}

Statutes in Florida,\textsuperscript{147} Minnesota,\textsuperscript{148} and Texas\textsuperscript{149} make it unlawful to use knowingly an expired or revoked credit card. The statutes in the former two states also make it unlawful to use a credit card without the authorization of its owner. While the coverage of the Texas statute is restricted to making use of a credit card to obtain gasoline service station products and services, the statutes in Florida and Minnesota apply regardless of the type of goods obtained.

In Minnesota\textsuperscript{150} one who obtains or attempts to obtain services by using a counterfeit credit card is guilty of a misdemeanor, and in Arkansas\textsuperscript{151} one who obtains goods or services with a counterfeit card is guilty of larceny.

In 1960, statutes have also been enacted in Georgia, Kentucky, and Mississippi which impose criminal penalties upon persons who fraudulently use credit cards.\textsuperscript{152}

\begin{footnotes}
\item[143] "If the thing stolen consists of any evidence of debt, or other written instrument, the amount of money due thereupon, or secured to be paid thereby, and remaining unsatisfied, or which in any contingency might be collected thereon, or the value of the property the title to which is shown thereby, or the sum which might be recovered in the absence thereof, is the value of the thing stolen." \textit{CAL. PEN. CODE} \textsection 492.
\item[144] The cases decided under \textsection 492 have involved the theft of documents evidencing title to property or calling for the payment of money. People v. Quiel, 68 Cal. App. 2d 674, 157 P.2d 446 (1945); People v. Jones, 61 Cal. App. 2d 608, 143 P.2d 726, \textit{appeal dismissed}, 323 U.S. 665 (1944); Stubbs v. Abercrombie, 42 Cal. App. 170, 183 Pac. 458 (1919); People v. Charidis, 29 Cal. App. 166, 154 Pac. 1061 (1915); People v. Rial, 23 Cal. App. 713, 139 Pac. 661 (1914); People v. Dadmun, 23 Cal. App. 290, 137 Pac. 1071 (1913). The credit card fits into neither of these categories.
\item[145] See People v. Charidis, \textit{supra} note 144; People v. Dadmun, \textit{supra} note 144.
\item[146] \textit{CAL. PEN. CODE} \textsection 532a provides in part: "Any person (1) who shall knowingly make ... any false statement in writing, with intent that it shall be relied upon, respecting the financial condition, or means or ability to pay, of himself, or any other person ... for the purpose of procuring in any form whatsoever ... the making of a loan or credit, the extension of credit ... for the benefit of ... himself ... shall be guilty of a misdemeanor ... ."
\item[147] \textit{Fla. Laws} 1959, ch. 59-331 \textsection 1-3.
\item[148] \textit{MINN. STAT. ANN.} \textsection 622.28 (Supp. 1959).
\item[149] \textit{TEX. PEN. CODE ANN.} art. 1555b (1959).
\item[150] \textit{MINN. STAT. ANN.} \textsection 620.501 (Supp. 1959).
\item[151] \textit{ARK. STAT. ANN.} \textsection 41-1901 (Supp. 1959).
\item[152] The authors have not had access to these statutes which are briefly summarized in 14 \textit{PENS. F.L.Q. REP.} 87 (1960).
\end{footnotes}
D. Obtaining Property by False Pretenses

1. The Card Holder

When the card holder obtains goods or services from a merchant with no intention of paying for them, the possibility of a subsequent prosecution for obtaining property by false pretenses will depend, in a majority of jurisdictions, upon whether or not the card holder obtained his credit card from the issuer in a fraudulent manner.

It would seem that when the card holder uses his card he represents to the merchant that the card was validly obtained. Thus, if the card were issued to the card holder on the basis of false information submitted on his application form and the merchant parts with goods or services materially relying upon the representation that the card was validly obtained, the card holder, if acting with fraudulent intent, would seem to be obtaining the goods or services by false pretenses. In the case of People v. Robertson, the California District Court of Appeal affirmed a conviction of grand theft where the defendant, with intent to defraud, acquired goods through the use of a credit card issued on the basis of false information submitted on his credit card application form. The Robertson case involved a simple two-party credit card transaction since the credit card and goods were received from the same party. In the tripartite transaction, however, the card holder acquires his card from one party and the goods or services from another. But since the crime of false pretenses can be established when the pretense is relied upon by the person from whom the property is obtained, even though the intent to defraud is directed at another and the ultimate loss falls on another, it is submitted that the Robertson rule is applicable to three-party as well as two-party transactions.

153 It has generally been held that the crime of obtaining property by false pretenses extends only to property which can be the subject matter of larceny. Perkins, Criminal Law 251 (1957). The subject matter of larceny has been expanded by statute in many jurisdictions to include labor and services as well as the traditional moveable personal property. Cal. Pen. Code § 532; N.Y. Penal Law § 1290.

154 The representation need not be in writing nor in words but may be inferred from the acts of the card holder. See People v. Carpenter, 141 Cal. App. 2d 884, 297 P.2d 498 (1956); State v. Hastings, 77 N.D. 146, 41 N.W.2d 305 (1950); Dixon v. State, 152 Tex. Crim. 504, 215 S.W.2d 181 (1948).

155 It is not necessary that the false representation be the sole factor inducing the merchant to part with his goods or services; it need only be a material factor. See People v. Ashley, 42 Cal. 2d 246, 267 P.2d 271 (1954).

156 The intent to defraud need not be shown by statements of the accused, but may be inferred from all the circumstances. The inability of the accused to pay for the goods received (People v. Robertson, 167 Cal. App. 2d 571, 334 P.2d 938 (1959)) and the signing of the name of another (People v. Platt, 124 Cal. App. 2d 123, 268 P.2d 529 (1954)) have been held sufficient to show an intent to defraud. For a general discussion of the intent necessary to establish the crime of obtaining property by false pretenses see Clark & Marshall, Crimes § 12.24 (6th ed. 1958).


158 It was alleged that the defendant filled out an application for a credit card from complainant store and falsely stated that he was a doctor of osteopathy. On the basis of this information, a temporary credit card was issued to him. See also People v. Keller, 165 Cal. App. 2d 419, 332 P.2d 174 (1958).

159 Commonwealth v. Johnson, 167 Ky. 727, 181 S.W. 368 (1916); State v. Hargrave, 103 N.C. 328, 9 S.E. 406 (1889). In Johnson the defendant had assigned his future wages. He then told his employer that no assignment had been made and in reliance on this statement the employer paid wages to the defendant. A conviction of obtaining property by false pretenses was affirmed, although the loss fell on the assignee and although the intent to defraud...
When a card holder acquires his card without submitting false information on the application form, it would seem that the only misrepresentation he could make to the merchant is that he will pay for the goods or services purchased. The common law rule and the present rule in the majority of American jurisdictions is that a fraudulent promise to pay is not a representation of an existing fact and therefore cannot form the basis of the crime of obtaining property by false pretenses. California, however, in the case of People v. Ashley joined the minority of states following the contrary rule on the ground that "a promise made without intention to perform is a misrepresentation of a state of mind, and thus a misrepresentation of existing fact, and is a false pretense within the meaning of section 484 of the Penal Code [California theft statute] ..." Thus, in California, the use of a credit card by the card holder without the intention of paying for the charges incurred would be a sufficient pretense to constitute the crime of obtaining property by false pretenses.

2. The Unauthorized Card User

When a person who is unauthorized to use a credit card obtains goods or services through its use with intent to defraud, his unauthorized purchases may subject him to prosecution for obtaining property by false pretenses. The only element was apparently directed at the assignee. Yet the false pretense was made to and relied on by the employer. Hargrave was a similar case in which the defendant had made an assignment of a right to collect money from the state. The defendant falsely told a state official that no assignment had been made and he then received payment on the basis of that false statement. A conviction of obtaining property by false pretenses was affirmed, although the assignee was the party actually defrauded.

In both of these cases money only was involved and therefore money was the property stolen. In the credit card transaction, however, merchandise is involved and the question arises as to whether the merchant is defrauded of his goods or whether the card issuer is defrauded of the purchase price of the goods. This question was important in the case of United States v. Golden, 166 F. Supp. 799 (S.D.N.Y. 1958), where the defendant was prosecuted under the Dyer Act, 18 U.S.C. § 2312 (1958), which makes illegal the interstate transportation of stolen motor vehicles. The defendant had used his all-purpose credit card to obtain possession of an automobile from an automobile renting firm, never intending to pay the charges incurred thereby. He subsequently transported the car across a state line and apparently abandoned it. The court concluded that the car was not "stolen" within the meaning of the act, likening the defendant's fraudulent use of his credit card to the fraudulent acquisition of a loan and the subsequent use of that loan to obtain merchandise from a merchant. Thus, the court could find no intent to deprive the rental company of the rights and benefits of ownership, although it expressly reserved comment on the possible criminal liability of the defendant in a state court prosecution.

The possibility of a contrary decision upon facts similar to those of the Golden case was recognized by the court when it stated: "Had the defendant used a card which he had reason to believe had been cancelled, or after notice to him that his credit had been revoked, this together with other factors, might well alter the result." 166 F. Supp. at 802. Apparently the court felt that if the defendant could not expect the card issuer to pay the merchant, then it would have been the merchant who was defrauded and the property received from the merchant would have been the property stolen.

As previously indicated, use of the card creates an obligation to pay for the goods and services purchased, but that obligation may be owed either to the card issuer or to the merchant. See Part III C supra. Where the defendant obtains goods by false pretenses, it would not seem important to determine to whom the card holder's obligation is owed. The important fact is that there is a promise to pay and that this promise is relied upon by the merchant in parting with goods and services.


42 Cal. 2d at 246, 267 P.2d at 271 (1954).

42 Cal. 2d at 262, 267 P.2d at 281.
of the crime that requires examination is the nature of the representations made by the unauthorized card user to the merchant.\textsuperscript{164}

Although the unauthorized user would seem to represent that he will pay for the goods or services purchased, as previously indicated only a minority of jurisdictions would hold that this representation can constitute the crime of false pretenses. But the unauthorized user would appear to make at least two additional representations to the merchant. First, the mere presentation of the card of another would be a misrepresentation of identity. This misrepresentation would appear to be conclusively established if the imposter signs the sales slip in the name of the card holder. Second, the imposter represents impliedly, if not expressly, that he is authorized to make purchases with the card. It seems clear that a misrepresentation of identity\textsuperscript{165} or authorization is sufficient to support a conviction of obtaining property by false pretenses. One, if not both, of these false representations appears to underlie the decision in \textit{People v. Von Hecht},\textsuperscript{166} where the California District Court of Appeal affirmed the conviction of an unauthorized user of a credit card for attempted grand theft.\textsuperscript{167}

\textbf{E. False Personation}

In some jurisdictions, the false personation of another is made a crime distinct

\textsuperscript{164}For a general discussion of false pretenses which may form the basis of the crime see CLARK & MARSHALL, \textit{CRIMES} 821–22 (6th ed. 1958).

\textsuperscript{165}See State v. Goble, 60 Iowa 447, 15 N.W. 272 (1883); People v. Le Grande, 309 N.Y. 420, 131 N.E.2d 712 (1956). See also \textit{CAL. PEN. CODE} § 530.


\textsuperscript{167}The defendant, using the credit card of another without authorization, contracted to buy new wheels for his car. The card was presented to the seller and the defendant was told to return later to pick up the car with the wheels installed. On his return, the defendant was apprehended, the merchant having discovered the credit card belonged to another. A conviction of attempted grand theft was affirmed. Although it is implicit in the affirmation of the conviction that had the defendant been successful in his scheme to obtain merchandise through the unauthorized use of the credit card he would have been guilty of grand theft, the court gave no indication of whether the theft would have been considered obtaining property by false pretenses or larceny by trick and device.

Under the California theft statute, Penal Code § 484, the indictment need not indicate whether the defendant is accused of larceny by trick and device or obtaining property by false pretenses. California, however, has retained a special statute, Penal Code § 1110, which defines the nature of proof required to support a conviction of obtaining property by false pretenses. When a credit card is used to rent merchandise, as in \textit{Golden} (see note 159 \textit{supra}), the card user will obtain only possession of the goods and the crime will be larceny by trick and device. But when a card is used to purchase goods or services, as in \textit{Von Hecht}, both title and possession will pass to the card user and the crime will be obtaining property by false pretenses. Only in the latter situation will the special proof requirements of § 1110 have to be satisfied in order to support the defendant's conviction. Section 1110 provides in part: "[T]he defendant cannot be convicted if the false pretense was expressed in language unaccompanied by a \textit{false token or writing}, unless the pretense or some \textit{note or memorandum} thereof is in writing, subscribed by . . . the defendant, or unless the pretense is proven by the testimony of two witnesses, or that of one witness and corroborating circumstances; but this section does not apply to a prosecution for \textit{falsely representing or personating another}, and, in such assumed character . . . receiving any . . . property." (Emphasis added.) A credit card would not be a "false token or writing," although its use was unauthorized, since a writing that is genuine and contains no false statements of fact cannot be false within the meaning of the statute. People v. Beilfuss, 59 Cal. App. 2d 83, 138 P.2d 332 (1943), \textit{cert. denied}, 321 U.S. 746 (1944). But it appears that the sales slip would be a "note or memorandum" of the false pretense which is in writing and subscribed by the defendant. The sales slip contains all the information that appears on the credit card and is signed by the user of the card. Since it is only the pretense itself which needs corroboration, People v. Andrews, 165 Cal. App. 2d 626, 332 P.2d 408 (1958), it would seem that the sales slip would be a sufficient "note or memorandum thereof." Furthermore, § 1110
from obtaining property by false pretenses. The California Penal Code, for example, makes it a crime for a person falsely to personate another if to do so might render the one personated liable in any suit or if the personator might derive a benefit from the masquerade. This statute is clearly applicable to an unauthorized user of a credit card who pretends to be the named card holder, since the card holder may well be held liable for the charges incurred and since the imposter realizes a benefit from his purchases.

F. Forgery

It appears that an unauthorized credit card user will be guilty of forgery if he signs the name of the card holder to the sales slip evidencing his purchase and if he possesses an intent to defraud. The only significant question is whether a sales slip constitutes proper subject matter for the crime of forgery, and this question has been answered affirmatively in California.

VII

THE APPLICABILITY OF REVOLVING CREDIT STATUTES TO THE TRIPARTITE CREDIT CARD TRANSACTION

Since 1957 states have been vigorously enacting retail installment sales legislation which is primarily designed to prevent oppressive practices by retail sell-
ers, finance companies, and other assignees of retail installment sales contracts. Such legislation usually protects the consumer by establishing maximum finance charges, by requiring the seller to include specified provisions in installment contracts, and by prohibiting certain unfair contractual provisions. Although most retail installment sales acts do not specifically provide for revolving credit agreements, both the New York and California retail installment sales acts do contain provisions which apply exclusively to these agreements. Furthermore, special statutes regulating revolving credit agreements have been enacted in Florida, Nebraska, North Dakota, and Ohio.

There can be no doubt that the revolving credit statutes in all six states are applicable to two-party credit card arrangements that permit the card holder to pay for purchases in monthly installments; it is equally clear that tripartite plans that do not permit card holders to make installment payments are not affected by these statutes. The important question is whether or not they extend to the tripartite plans that permit installment payments and exact monthly service charges. In attempting to answer this question it is convenient to consider the California and New York statutes apart from those of the other four states.

The California and New York revolving credit statutes establish a maximum, all-inclusive service charge of one and one-half percent per month computed on the retail buyer's outstanding balances from month to month, prohibit the execution and negotiation of notes which might be used to enable third parties to cut off the buyer's defenses against the seller, require the monthly statement to show the figures used in arriving at the service charge, require the inclusion of specified provisions (in print of designated type sizes) in revolving credit agreements.
agreements in order to notify the buyer of his rights under the agreement,\textsuperscript{1,2} and establish criminal and civil penalties for violations of any of the statutory provisions.\textsuperscript{3}

Both the New York and California statutes define a revolving credit agreement as one entered between a buyer and a seller. The California statute, for example, defines a revolving credit agreement as follows:

"Retail installment account" or "installment account" or "revolving account" means an account established by an agreement entered into in this State, pursuant to which the buyer promises to pay in installments, to a retail seller, his outstanding balance incurred in retail installment sales, whether or not a security interest in the goods sold is retained by the seller, and which provides for a service charge which is expressed as a percent of the periodic balances to accrue thereafter . . . . (Emphasis added.)\textsuperscript{4}

Other statutory language in both states\textsuperscript{5} is consistent with the notion that the California and New York legislatures considered a revolving credit agreement to be one entered into by a buyer and a seller. Unless this language is to be ignored, tripartite credit card plans do not fall within the California and New York definitions of revolving credit agreements, because in tripartite plans the buyer enters into an agreement with the card issuer and promises to make payments to the issuer, not to the seller.

The revolving credit statutes in Florida, Nebraska, North Dakota, and Ohio\textsuperscript{6} contain the same type of protective provisions as the California and New York statutes, but in none of the four states is the buyer protected from the threat of a negotiable instrument being used to cut off his defenses. These four states do, however, establish maximum service charges ranging from one and one-half to two percent per month, calculated from month to month on the buyer's unpaid balance.\textsuperscript{7} Unlike the California and New York acts, these states define a revolving credit agreement from the standpoint of the buyer and make no mention of the seller as the other party to the agreement. North Dakota, for example, defines a revolving credit agreement as:

... a written instrument, defining the terms of retail installment sales made from time to time pursuant thereto, pursuant to which the buyer's total unpaid balance thereunder, whenever incurred, is payable in installments over a period of time and under the terms of which a credit service charge is to be computed in relation to the buyer's unpaid balance from time to time.\textsuperscript{8}

\textsuperscript{1} CAL. CIV. CODE §§ 1810.1-2; N.Y. PERS. PROP. LAW §§ 413.1-2.
\textsuperscript{2} CAL. CIV. CODE §§ 1812.6-9; N.Y. PERS. PROP. LAW § 414. In both states a willful violation of a statutory provision is a misdemeanor. Also, when a statute is violated, the buyer is excused from paying the service charge unless the failure to comply with the statute is corrected within ten days from the time the guilty party is notified of his violation.
\textsuperscript{3} CAL. CIV. CODE § 1802.7. The corresponding statute in New York is to the same effect. N.Y. PERS. PROP. LAW § 401.8.
\textsuperscript{4} "A retail installment account [revolving credit agreement] may be established by the seller upon the request of a buyer or prospective buyer." CAL. CIV. CODE § 1810.1. "At the time a seller accepts the credit of the buyer and establishes a retail installment account for his use, the seller shall confirm this fact to the buyer in writing." CAL. CIV. CODE § 1810.2. See also N.Y. PERS. PROP. LAW §§ 413.1-3.
\textsuperscript{5} These statutes are cited in notes 183-86 supra.
\textsuperscript{6} The permissible service charge in Florida, Nebraska, and North Dakota is \textsuperscript{1\frac{1}{2}-2\%}. Fla. Laws 1959, ch. 59-414, § 6(3); Neb. Laws 1959, ch. 217, § 2(3); N.D. Laws 1959, ch. 350, § 3. But in Nebraska no service charge is permitted on balances in excess of $500. Neb. Laws 1959, ch. 217, § 1(1). In Ohio, the service charge may vary from \textsuperscript{1\frac{1}{2}-2\%} in accordance with a sliding scale based upon the buyer's outstanding monthly balance. OHIO REV. CODE ANN. § 1317.11(B) (1-3) (Baldwin 1959).
\textsuperscript{7} N.D. Laws 1959, ch. 350, § 1(4).
Other provisions of the North Dakota act, however, state that a copy of a revolving credit agreement "shall be delivered or mailed to the retail buyer by the retail seller" and that the retail seller shall supply the buyer with a monthly statement. Similar language in the Florida, Nebraska, and Ohio statutes indicates that the legislatures of these states felt that a seller would be one of the two parties to a revolving credit agreement. Although all but one of these states expressly recognize the possibility that the seller may assign his rights under such an agreement to a third party, none of them seems to contemplate a situation in which a third party and not the seller enters into a revolving credit agreement with the buyer. Thus, it is arguable that these states did not intend to regulate tripartite credit card transactions.

Perhaps the comparative youth of tripartite credit card plans accounts for the language in the California and New York statutes which apparently precludes an interpretation of the statutory provisions that would include tripartite credit card transactions. And perhaps the ambiguities of the statutes in the other four states can be attributed to the same reason. Since all six states have clearly authorized service charges ranging from one and one-half to two percent in two-party revolving credit agreements, it would seem that they should amend their statutes to grant the same privilege to tripartite credit card plans. Without such legislation, courts may be tempted to hold that the tripartite transaction is not a time price sale but a cash sale coupled with an extension of credit, thus subjecting the amount of the service charge to the limitations of the usury laws. Furthermore,

200 See, e.g., Fla. Laws 1959, ch. 59-414, § 6(2).
201 See, e.g., Neb. Laws 1959, ch. 350, § 2(1-3).
202 See, e.g., Ohio Rev. Code Ann. § 1317.11(A) (Baldwin 1959). Although this section states that a "holder" of a revolving credit agreement as well as a seller may deliver a copy of the agreement to the buyer, a "holder" is defined as a successor in interest of the seller. This definition of "holder" seems to indicate that the holder itself could not have entered into a revolving credit agreement with the buyer.
204 The traditional view that time price sales are not subject to usury laws has been summarized as follows: "It has often been pointed out that from the standpoint of the buyer and in economic effect there is little or no difference between a loan of money with which to purchase goods or services and the sale of the same goods or services on credit. In either transaction the buyer may be obligated to pay either in instalments or in one lump sum and there may be an additional charge for what is, in economic terms, the buyer's anticipated exercise of his future purchasing power. In the case of a loan, this additional charge is 'interest' in the legal sense, subject to the usury limitations or to the special provisions of small loan laws. In the sales transaction, however, the difference between the 'time sale price' and the 'cash sale price' is generally considered without the scope of the usury laws, the common law rationale being that the vendor and purchaser may agree upon a time sale price without considering what the cash sale price would be." Note, Retail Instalment Sales Legislation, 58 Colum. L. Rev. 854, 858-59 (1958).
205 "[O]nce view is that transactions under revolving credit plans are essentially sales negotiated on the basis of a cash price plus a general agreement for the extension of credit (forbearance) contemplating payment of the cash price over an indefinite period of time. Under this view the credit agreement, in terms of older terminology, is merely an open, running account, for which a percentage charge is made, the charge being measured by the amount owed and the time that it is owed. The issue is whether revolving credit belongs in the category of loans and forbearances or that of time price sale transactions." Britton & Ulrich, The Illinois Retail Instalment Sales Act—Historical Background and Comparative Legislation, 53 Nw. U. L. Rev. 137, 175 n.143 (1958). The Illinois act which these authors discussed applied only to
since it is uncertain whether usury laws are applicable to revolving credit service charges,\textsuperscript{206} it would be desirable for states having no revolving credit legislation to consider enacting statutes regulating both two-party and three-party revolving credit agreements.\textsuperscript{207}

**CONCLUSION**

The advent of tripartite credit plans has launched the credit card into a new era. The day appears near at hand when the businessman and housewife will be able to satisfy all of their entertainment and shopping needs by simply displaying their all-purpose credit cards to employees stationed at outmoded cash registers. The volume of sales made with credit cards has greatly increased in the past few years and is likely to continue increasing in the future due to the spirited competition among the card issuers to acquire more card-holding and merchant members.

As the number of credit card sales grows larger, it can be expected that there will be a greater number of legal disputes arising from credit card transactions. Thus far, the few courts that have been confronted with cases arising from tripartite credit card transactions have failed to recognize that there are two conflicting interpretations of the legal nature of the transaction, and that the rights and duties of the parties may vary substantially depending upon which interpretation is adopted. In this Comment, the two possible interpretations have been labelled the “assignment” theory and the “direct obligation” theory.\textsuperscript{208} If “a law of credit cards” is to develop, it would seem that a choice between the theories will have to be made. This choice may well determine the applicability of accounts receivable notice-filing statutes to the tripartite transaction and the extent to which the card holder may set up defenses and counterclaims existing against the merchant in a suit brought by the issuer.

In choosing a theory, the courts must determine the source from which the credit card issuer derives the card holder’s obligation to pay for credit card purchases. As previously discussed,\textsuperscript{209} it may be argued that the right to collect the obligation is assigned by the merchant to the issuer, the issuer being similar to a company that factors accounts receivable, or that the obligation is owed directly to the issuer, which stands in a position comparable to that of the writer of a letter of credit. Although the assignment theory is a tenable one, it is submitted that

\textsuperscript{206} See Boyle, Charges for Revolving Credit and Charge Accounts, 12 Pers. F.L.Q. Rep. 33 (1958), where it was argued that revolving credit arrangements are not time price sales and should be subject to usury laws. The proclivity of courts to hold service charges within some regulated limit is shown by the case of Master Charge v. Daugherty, 123 Cal. App. 2d 700, 267 P.2d 821 (1954), where it was held that a proposed tripartite credit card plan was subject to the provisions of the California Small Loan Act. Two subsequent legislative amendments have exempted credit card plans fulfilling certain qualifications from the operation of the Small Loan Act. Cal. Fin. Code § 24051.1.

\textsuperscript{207} “[S]ound business practice, the interests of charge-account customers, and the symmetry of the law all require that the legal status of such financing [revolving credit] should be clearly defined by statute. If public policy requires that this kind of consumer financing as well as installment sales financing should not be subject to the state's usury limitations, such exemption should be clearly stated and defined by statute.” Britton & Ulrich, supra note 205, at 175.

\textsuperscript{208} See Part III C supra.

\textsuperscript{209} Ibid.
the direct obligation theory offers a more accurate description of the transaction and thus should be considered the basis for determining the rights and duties of the parties.

The fallacy of the assignment theory is that it focuses attention upon the sale and treats it as giving rise to an account between the seller and buyer which is thereafter assigned to a third party. This approach overlooks the fact that before the sale has taken place two previous contracts have been entered into, one between the issuer and card holder and the other between the issuer and merchant. Since the merchant promises to transmit all sales slips to the issuer and the issuer promises to pay the merchant their face amount less discount, and since the card holder promises to make payments directly to the issuer, it appears that the merchant parts with goods and services not in reliance upon the buyer's, but upon the issuer's promise to pay for them. The issuer, in turn, makes payments to the merchant in reliance upon the card holder's obligation of reimbursement, as in the letter of credit transaction. Although in merchant-issuer contracts the merchant agrees to "assign" or "endorse" sales drafts to the issuer, it would seem that in fact there is no assignment of the right to enforce the card holder's obligation to pay, but only an assignment or transmittal of a document that is necessary for the practical operation of the plan; the sales draft merely informs the issuer that an obligation has arisen in its favor from the card holder and that it, in turn, is obligated to pay the merchant. Thus, the sales draft in the credit card transaction appears to perform a similar function to the documents which the seller must send the writer in the letter of credit transaction, i.e., it notifies the recipient that payment must be made to the seller.

An acceptance of the direct obligation theory requires the conclusion that tripartite credit card transactions are not subject to notice-filing statutes governing assignments of accounts receivable. Hence, the card issuer would be immune from claims made by the merchant's creditors or trustee in bankruptcy should they seek the protection of these statutes.210

Whether, in a suit brought by the issuer, the card holder will be able to assert defenses which he has against the merchant depends upon whether or not the card holder's obligation to pay the issuer is independent of the merchant's obligations under the contract of sale. It has been previously suggested211 that the card holder's promise of payment should be interpreted as conditioned upon the merchant's fulfillment of his contractual obligations, thus allowing the card holder to assert against the issuer any defenses arising out of the sale that he would have been able to assert against the merchant. The card holder, however, would be unable to assert against the issuer any defenses or counterclaims unrelated to the credit card purchase and such disputes between the card holder and merchant would be left to independent determination. This approach seems to represent the fairest way of balancing the card holder's interest in not being left without a remedy and the issuer's interest in not being burdened with disputes between the card holder and merchant.

The suggested rule would be broad enough to allow the card holder to assert in an imposter case the defense that the merchant's negligence made possible the unauthorized purchase. The two most recent imposter cases212 did allow the card holder to assert such a defense although those courts reached their decisions on

210 See discussion in note 94 supra.
211 See text at notes 61-65 supra.
212 See text at notes 121-32 supra.
the basis of the assignment theory without recognizing the existence of the direct obligation theory.

Legislatures should recognize the card holder's lack of real bargaining power and codify the rule that the card holder may assert against the issuer any defenses arising from the sale. This codification should be supplemented by statutes (1) protecting the card holder against a waiver of this right, (2) prohibiting the alteration of the rule by the introduction into the transaction of a document purporting to be a negotiable instrument, and (3) requiring the issuer to print on all issued credit cards a statement that the card holder will not be required to pay the issuer for a purchase to the extent that he has a bona fide defense against the merchant arising from the sale.

There are other aspects of the credit card transaction which are also susceptible of legislative treatment and which should be so treated for reasons of certainty and uniformity. Simple logic would seem to require that the six states that now regulate revolving credit agreements amend their statutes to include clearly within their terms the tripartite credit card plans which permit the card holder to pay for credit card purchases in installments. So amended, these statutes would authorize a maximum and all-inclusive service charge, protect the issuer against claims of usury, and require the issuer to use forms calculated to notify the card holder of his rights and to disclose to him the amount of the service charge and manner in which it is computed.

Present laws of theft, false personation, and forgery appear adequate to impose criminal sanctions upon the unauthorized user of a credit card and upon the card holder who obtains goods or services with a credit card that was acquired from the issuer on the basis of false information submitted on a credit card application form. At least seven states have recently enacted statutes which usually provide that it is a crime to use an expired, revoked, or counterfeited credit card or to use a credit card without the authorization of its owner. But the rule followed in the majority of jurisdictions that a fraudulent promise to pay for goods obtained on credit is not sufficient to support a conviction of obtaining property by false pretenses renders most of the states helpless to cope with the card holder who honestly obtains a credit card but subsequently uses it with fraudulent intent.

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