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Commercial Law

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COMMERCIAL LAW

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The area of commercial law was an active one during the Survey year. This article is by no means comprehensive, but highlights many of the major developments of the year.

I. THE NEW USURY LAW

A very important development in the area of commercial law during the survey year was the passage of a number of statutes dealing with usury in New Mexico.[1] This deceptively simple law contains several problems of which New Mexico attorneys should be aware.

A. *Background*

The unrest in the nation's financial markets and the rapid rise in market interest rates has caused problems in jurisdictions with fixed usury interest rate ceilings. Interest rates have risen so fast that rates which were recently considered outrageous are now quite common. States with fixed rate ceilings now run the risk of inhibiting lending within the state unless those rate ceilings are frequently adjusted.

For several years, New Mexico lenders were restricted by unrealistically low rate ceilings—twelve percent on unsecured loans and ten percent on secured loans.[2] In order to obtain reasonable interest rates, lenders had to conform their transactions to one of a number of laws which permitted higher rates to be charged.[3] Each of these laws, however, was limited to certain types of loans.[4] Some of the statutes also regulated ancillary matters, such as late charges and

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1. N.M. Stat. Ann. §§56-8-11.1 to -11.4 (Cum. Supp. 1981) hereinafter referred to as the Usury Act.

2. 1957 N.M. Laws ch. 209, §2 (prior to the 1980 amendment).

3. N.M. Stat. Ann. §§56-1-1 to -15 (1978) (Retail Installment Sales Act); N.M. Stat. Ann. §§56-8-22 to -30 (Cum. Supp. 1981) (Residential Home Loan Act); N.M. Stat. Ann. §56-8-21 (Cum. Supp. 1981) (Exemption for loans to corporations and limited partnerships); N.M. Stat Ann §§58-7-1 to -9 (1978) (Bank Installment Loan Act); N.M. Stat. Ann. §§58-15-1 to -31 (1978) (New Mexico Small Loan Act of 1955); N.M. Stat. Ann. §§58-19-1 to -10.1 (1978) (Motor Vehicle Sales Finance Act).

4. *See* note 3 *supra.*

prepayment penalties,[5] which made it difficult to assess the value of the increased rate ceiling to the creditor. In 1980, the legislature provided lenders with some relief from the low limits of the general usury statutes by allowing the general usury interest rate ceiling to "float" at a level three percent above the federal reserve discount rate.[6] The floating rate allowed the general rate ceiling to be adjusted without legislative action. Because differing rates applied at different times, however, the floating rate further complicated the state's tangled web of interest rate ceilings.

With the new Usury Act, the legislature abandoned the effort to set rate ceilings, but it seems to have done so reluctantly.[7] As if to compensate for the loss of protection enjoyed by borrowers under the old law, the new Act sets up new hurdles for creditors to cross in the form of a "writing" requirement and a disclosure requirement.[8] Both of these new requirements pose problems for New Mexico lawyers.

B. *The "Writing" Requirement*

The first section of the new Usury Act states that the maximum allowable interest rate is the "rate agreed to in writing by the parties."[9] A writing requirement is not a new feature in New Mexico law. Section 56-8-3, which dates back to 1852,[10] applies the statutory rate of ten percent to money due by contract "in the absence of a written contract fixing a different rate,"[11] and the section has been interpreted to mean that in the absence of special circumstances, unwritten agreements for other interest rates are unenforceable.[12]

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5. *See, e.g.,* the comprehensive regulation of ancillary matters contained in the Retail Installment Sales Act, which includes regulation of prepayment penalties, (N.M. Stat. Ann. § 56-1-2(J) (Cum. Supp. 1981)), later charges, (N.M. Stat. Ann. § 56-1-2(K) (Cum. Supp. 1981)), and insurance (N.M. Stat. Ann § 56-1-4 (1978)).

The Act also prohibits the use of various other terms, including the use of provisions for acceleration of payments in the event of buyer default, the assignment of the power of attorney from buyer to seller that could be exercised to confess to a judgment in New Mexico, or provisions through which the buyer agrees not to assert a claim or defense against the seller arising out of the sale. N.M. Stat. Ann. § 56-1-5(A, B, and F) (1978).

6. N.M. Stat. Ann. § 56-8-11 (Cum. Supp. 1981).

7. N.M. Stat. Ann. §§ 56-8-11.1 to -11.4 (Cum. Supp. 1981). This law is in effect on a trial basis. The Act provides for its own repeal and the revival of the former law on July 1, 1982. N.M. Stat. Ann. § 56-8-11.4 (Cum. Supp. 1981).

8. N.M. Stat. Ann. §§ 56-8-11.1, -11.2 (Cum. Supp. 1981).

9. N.M. Stat. Ann. § 56-8-11.1 (Cum. Supp. 1981).

10. 1851-52 N.M. Laws p. 254.

11. N.M. Stat. Ann. § 56-8-3 (Cum. Supp. 1981). The rate was six percent until 1980. *See* N.M. Stat. Ann. § 56-8-3 (1978).

12. *See* Brown & Manzanares Co. v. Gise, 14 N.M. 282, 91 P. 716 (1907). In that case, the court enforced an unwritten interest rate which differed from the statutory rate after finding that the borrower waived the right to object to the lack of a writing.

A question arises, however, as to whether the two writing requirements are in conflict. A literal interpretation of the new Usury Act's writing requirement suggests that no interest at all ought to be allowable where no rate has been agreed upon in writing. Because the maximum rate is the rate agreed to in writing, where no rate has been agreed to, the maximum rate is no rate, and no interest may be charged. Section 56-8-3 takes a different position—where no rate has been agreed to in writing, the rate to be assessed is the statutory rate of ten percent.[13]

The rules of statutory construction militate against interpreting the writing requirement of the new Usury Act to mean that no interest should be charged where there is no written agreement. Such an interpretation would entail the implied repeal of the statutory rate section. Statutes should be construed harmoniously if possible, so as to avoid implied repeal of other acts.[14] Where an act specifically enumerates existing laws which it repeals, as does the new Usury Act,[15] the policy of construction against implied repeal is especially strong, because it is presumed that the legislature's enumeration of repealed sections is comprehensive.[16] Additonally, the same legislature which passed the new Usury Act also amended another statutory interest rate section to increase the statutory rate on open accounts to ten percent.[17] Under this principle of harmonious interpretation, statutes which appear to conflict must be interpreted, if possible, to be consistent with one another. This rationale is especially appropriate when the statutes in question were enacted in the same session.[18]

It is likely, then, that the courts will find some reason to conclude that statutory interest rates are not rendered unenforceable by the absence of a writing. If so, the statutory rate of ten percent will continue to be a sort of default rate. The ten percent rate will apply to any loan transaction in which no other rate has been agreed upon in writing by the parties.

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13. N.M. Stat. Ann. § 56-8-3 (Cum. Supp. 1981).

14. C. Sands, Statutes and Statutory Construction § 23.10 (1975) (hereinafter referred to as Statutory Construction).

15. N.M. Stat. Ann. § 56-8-11.4 (Cum. Supp. 1981). This section repeals N.M. Stat. Ann. §§ 56-8-2.1, -3.1, 56-8-11, -25 to -28, 58-7-4, 58-11-17, 58-13-47, 58-15-14, 58-19-8, and 59-8-7.1.

16. *See* Statutory Construction, *supra* note 12, at § 51.02.

17. N.M. Stat. Ann. § 56-8-5 (Cum. Supp. 1981) (the Open Account Law).

18. If the two acts were held to be irreconcilable, the new Usury Act (1981 Laws ch. 263) would prevail over the Open Account Law (1981 Laws ch. 194) because the Usury Act was signed by the governor after the Open Account Law. *See* N.M. Stat. Ann. § 12-1-8(1978). *See also* State v. Monteil, 56 N.M. 181, 241 P.2d 844 (1952); State v. Marcus, 34 N.M. 378, 281 P. 454 (1929).

C. *The Disclosure Requirement*

The most difficult feature of the new Act is its disclosure requirements.[19] The Act provides that compliance with the federal Truth in Lending Act[20] will be deemed to be compliance with the New Mexico disclosure requirements.[21] Most lenders will therefore have little reason to deal with the specific disclosures called for by the state Usury Act[22]. All lenders, however, should be aware of some problems which arise under the disclosure requirement.

The disclosure requirement sets out twelve items which must be disclosed in connection with most loans.[23] Exemptions are allowed only for loans made by persons who are not in the business of lending[24] and for loans made for business or agricultural purposes in a principal amount greater than $50,000.00.[25]

The state disclosure provision is similar to those of the federal Truth in Lending Act in many respects. The two acts, however, are not identical. The state Act requires a disclosure of three items which are not required to be disclosed by federal law. Those items are the purpose of the loan,[26] the interest rate expressed as a percent per month,[27] and a "clear and concise description of the legal and financial consequences" of failure to pay as agreed.[28] Federal law requires the disclosure of many items not required by the state Usury Act,[29] and contains much more detailed directions as to the manner of disclosure.[30]

The most striking difference between state and federal disclosure requirements, however, is the comparative vagueness of the state Act. For example, federal law provides an extremely detailed description of what must be included in the "finance charge,"[31] which

19. N.M. Stat. Ann. §56-8-11.2(A) (Cum. Supp. 1981).

20. 15 U.S.C. §§1601-50, 1665a, 1667 (1976). The federal Truth in Lending Act is supplemented by Regulation Z, 12 C.F.R. §226 (1981).

21. N.M. Stat. Ann. §56-8-11.1(D) (Cum. Supp. 1981). The statute reads: "[A]ny form which is in compliance with federal law regarding disclosure of information by creditors to borrowers, such as the federal Truth in Lending Act shall be deemed to be in compliance with [the disclosure portion] of this section." *Id.*

22. Some lenders may elect to give the specific state disclosures on loans which are covered by the state Act but not by the federal Act. *See* notes 56-61 *infra* and accompanying text for a discussion of this practice.

23. N.M. Stat. Ann. §56-8-11.1(D) (Cum. Supp. 1981).

24. *Id.* -11.2(B).

25. *Id.* -11.2(C).

26. *Id.* -11.2(A)(3).

27. *Id.* -11.2(A)(5).

28. *Id.* -11.2(A)(12).

29. A discussion of all of the differences between the federal Truth in Lending Act and the disclosure requirements of the new Usury Act is beyond the scope of this article.

30. *See, e.g.*, the general rules of disclosure at 12 C.F.R. §226.6 (1981).

31. *Id.* at §226.4

must be disclosed to the consumer.[32] The state Act does not even require the finance charge to be disclosed. It seems, however, to require something like a finance charge to be calculated by requiring "all charges and costs" to be taken into account in calculating the interest rate.[33] What will constitute compliance with the state disclosure requirements is a matter fraught with uncertainty. For example, §56-8-11.2(12) requires that the lender disclose a "clear and concise description of the legal and financial consequences of failure . . . to make repayment according to the agreement. . . ."[34] An almost limitless number of "legal and financial consequences" could take place upon a borrower's default.[35] There are so many possible legal consequences of a default that it would be virtually impossible to disclose them all. The disclosure requirement gives no indication as to where to draw the line.

The Usury Act itself seems to recognize that lenders are bound to be uncertain of their compliance with the Act. The Act authorizes the Financial Institutions Division of New Mexico's Department of Commerce and Industry to approve or promulgate specific disclosure forms, use of which will then be deemed to be compliance with the disclosure provisions of the Act.[36] Thus, even though the Act itself is hopelessly unclear, lenders, theoretically at least, can protect themselves to some extent by having their forms approved by the Division. As discussed below, however, the Division has decided not to approve such forms.

It is important to note the penalty portion of the disclosure provision. Any lender not in compliance with the disclosure provision "shall forfeit all interest, charges or other advantage for the loan . . ."[37] This penalty is extremely severe with respect to loans on which a large amount of interest is to be paid—much more severe in many instances than are the penalties for violations of the Truth in Lending Act, where the penalty is more or less limited to $1,000.00.[38] The most worrisome aspect of the penalty under the

32. Federal regulations require the disclosure of the finance charge. *See* 12 C.F.R. §§226.7(3), 226.8(b)(2), 226.8(c)(8)(i), and 226.8(d)(3) (1981).

33. N.M. Stat. Ann. §56-8-11.2(A)(5) (Cum. Supp. 1981).

34. N.M. Stat. Ann. §56-8-11.2(A)(12) (Cum. Supp. 1981).

35. The lender might have the right to accelerate the indebtedness. The borrower might be liable for a late charge. The lender might foreclose upon the collateral for the loan. The borrower might have redemption rights. The borrower might forfeit prepaid insurance premiums. The lender might be entitled to a deficiency judgment. The borrower might be entitled to an accounting of the surplus from a foreclosure sale. The borrower's credit might be impaired. The borrower might have the right to declare bankruptcy.

36. N.M. Stat. Ann. §56-8-11.2 (Cum. Supp. 1981).

37. N.M. Stat. Ann. §56-8-11.3 (Cum. Supp. 1981).

38. 15 U.S.C. §1640 (1976).

state law, from the lender's point of view, is that the penalty is virtually unlimited in class actions. Class action recoveries under the Truth in Lending Act are limited to $500,000.00, or one percent of the lender's net worth, whichever is less.[39] The New Mexico Usury Act makes it possible for a systematic disclosure violation[40] by a commercial lender to result in a class award equal to the interest portion of its entire loan portfolio.

New Mexico lenders who plan to rely on their federal Truth in Lending disclosures, then, should be aware that the stakes are now much higher than they were before passage of the new Usury Act. A systematic disclosure violation of the Truth in Lending Act could mean financial ruin for a lender, because of the availability of the class action brought pursuant to the state Act. It is, therefore, almost impossible to be too cautious in drafting disclosure documents and in insuring that they are properly used.

Compliance with the Truth in Lending Act is no easy matter. Regulation Z,[41] with the body of interpretation which has grown up around it,[42] is infamous for its puntiliousness,[43] its obscurity,[44] and its sheer bulk.[45] While much progress toward the remedy of these difficulties has been made by the adoption of the Truth in Lending Simplification Act[46] and the revised Regulation Z promulgated under the Simplification Act,[47] many lenders may still seek a way to comply with the state Act, on the theory that compliance with the

39. *Id.* at § 1640(a)(2)(B).

40. "Systematic disclosure violations," as used in this article, refers to an error in the form used, or an error in the algorithm for calculating a numerical disclosure.

41. Regulation Z is the body of regulations promulgated under the Truth in Lending Act which defines and prescribes the disclosure requirements of the Truth in Lending Act. *See* note 20 *supra.*

42. Primary interpretive material for federal Truth in Lending includes over 150 Official Staff Interpretations and about twice as many Unofficial Staff Interpetations issued by the Federal Reserve Board. Also important are some 1,000 Public Information Letters adopted by the Board. These materials are collected and indexed in R. Clontz, Truth-in-Lending Manual (4th ed. 1976, with 1981 Cum. Supp.).

43. *See, e.g.,* 12 C.F.R. § 226.6(a) (1981), which specifies the size of type to be used for numerical disclosures.

44. *See, e.g., id.,* which also states that disclosures must be made in "meaningful sequence," and § 226.7(k)(2)(i), which requires certain symbols to be "reasonably unique."

45. Consider, for example, that R. Clontz, Truth in Lending Manual (4th Ed. 1976), a standard and invaluable reference tool in the area, runs well over one thousand pages in two volumes, and its 1981 cumulative supplement is almost as large as the parent work.

46. Enacted as Title VI to the Depository Institutions and Monetary Control Act of 1980, Pub. L. No. 96-221 (March 30, 1980) (to be codified with the existing Truth in Lending Act, 15 U.S.C. §§ 1601 to 1665a, 1667 (1976)).

47. 46 Fed. Reg. 20,848 (April 7, 1981) (to be codified as 12 C.F.R. § 226). Lenders may elect to comply with either the old regulations or the new revised regulation until April 1, 1982, at which time the new regulation becomes mandatory. Pub. L. No. 96-221, Title VI, § 625.

state Act does not stand or fail on their ability to satisfy the requirements of the federal Truth in Lending Act.

One such approach would be to comply with the specific disclosure provisions of the state Act in addition to those of the Truth in Lending Act. The theory behind doing so is that even if the lender is found to have erred under the federal Act, the state disclosures might still insulate the lender from the harsh state penalties. As discussed above, however, the state Act is itself far from clear, and compliance with state disclosure requirements might be even more difficult than compliance with the federal requirements. In addition, Regulation Z expressly forbids disclosure in accordance with inconsistent state disclosure requirements.[48] Therefore, any attempt to cover all bases would be a violation of federal law. Another complication is that the New Mexico Financial Institutions Division has, by regulation, expressly disapproved the use of the state disclosure requirements.[49]

Another approach would be to use forms approved by the Financial Institutions Division, because such forms are deemed to be in compliance with the Act.[50] The Division, however, has not issued any forms, and has no intention of reviewing all the Truth in Lending disclosure forms in use in New Mexico.[51] Instead, it has simply directed that all New Mexico lenders write their own truth in lending forms.[52] The Division is reviewing forms only for a very few lenders in New Mexico who have no experience in disclosing information under the Truth in Lending Act.[53]

Compliance with the disclosure provision in cases which are covered by the state Act but not by the federal Truth in Lending Act[54] present a special problem. The Division's regulation provides that "[i]f a credit rate on a loan is exempt from the Federal Truth in Lending Act and Regulation Z, the disclosure of information by a creditor which would otherwise comply with the federal Truth in Lending Act and Regulation Z shall be deemed to comply with the disclosures required by [the new Usury Act]."[55]

The Division has statutory authority to approve forms "as con-

48. 12 C.F.R. §§226.6(b) and 226.28 (1981). Revised Regulation Z has a similar provision at §226.6(b).

49. Regulation 81-1, June 24, 1981.

50. N.M. Stat. Ann. §56-8-11.2(D)(A)(2) (Cum. Supp. 1981).

51. Telephone conversation with E. St. Peter, Chief Examiner, Financial Institutions Division, October 27, 1981.

52. Regulation 81-1, June 24, 1981.

53. *See* note 51 *supra.*

54. These loans are mostly non-consumer loans of $50,000.00 or less.

55. Regulation 81-1, June 24, 1981.

forming with the provisions of [the disclosure section of the Act]."[56] It is not clear, however, that the Division's regulation is within this statutory authority.[57] Federal Truth in Lending disclosures do not satisfy the state disclosure requirements directly, because they do not contain the three items which are unique to the state Act.[58] It may be that the Division's authority to approve forms does not extend to making a categorical approval of that class of forms which clearly do not otherwise comply with the Act. Thus, the Division's regulation presents the practitioner with a dilemma.

Any lender which relies upon the regulation might be found to be in violation of the state Usury Act on such loans because it failed to disclose the three items which state law requires but federal law does not. A lender taking any other action, however, could be in for equal trouble. If only the New Mexico disclosures are given, the lender is faced with the unappealing task of interpreting the vague requirements of the New Mexico law. That course would also be in violation of the Division's regulation. Such a violation could be of little or great significance, depending upon the extent of the Division's regulatory authority over the lender involved. Making both disclosures would probably be futile because the making of the state disclosure would invalidate the federal disclosure, even if it is otherwise correct.[59]

D. *Recommendations*

What the New Mexico lawyer should do about this confusing new statute depends upon the position he is in. Counsel for lenders should review the disclosure documents being used by their clients for compliance with the Truth in Lending Act. Lenders should, if they have not already done so, immediately convert to the use of the Simplification Act forms.[60] The use of the standard forms offers lenders unprecedented protection against shifting interpretations of the requirements of Regulation Z.[61] Accepting such protection should not be put off until compliance with the revised federal Act becomes mandatory on April 1, 1982. The standard forms should be copied as exactly as possible, and should not be modified except for compelling reasons.

Lenders' counsel should also take care to impress upon their cli-

56. *See* text accompanying notes 51-53, *supra.*
57. *See* N.M. Stat. Ann. § 56-8-11.2(D) (Cum. Supp. 1981).
58. *See* text accompanying notes 26-28, *supra.*
59. *See* note 48 *supra.*
60. These forms are found at Revised Regulation Z. 12 C.F.R. § 226, Appendices G and H.
61. 15 U.S.C. § 1614(b) & (d) (revised act).

ents the need for strict compliance with the Truth in Lending Act, and should make the lenders aware of their possible exposure to increased liability under New Mexico's new Usury Act. Where the lenders rely on the business or agricultural exemption, lenders should obtain a certificate from the borrower stating that the loan is to be used for business or agricultural purposes and that it exceeds $50,000.00.[62] Finally, lenders' counsel should exercise utmost care in drafting opinion letters regarding a client's forms and procedures.

Counsel for borrowers should routinely review the disclosure documents supporting any loan for compliance with Truth in Lending. The experience of this author is that clear violations of the federal law are quite common, and that arguable violations are sometimes present even in the disclosures of the largest financial institutions. Borrowers' lawyers should check the mathematics of the disclosure statement. Many otherwise unobjectionable disclosures are rendered inadequate by faulty figuring. Lawyers who are not familiar with Truth in Lending should learn that law. A clear understanding of Truth in Lending provides a powerful weapon to wield on behalf of borrower clients. Truth in Lending violations may soon mushroom, because there will be some lenders who fail to convert to the new Act when it becomes mandatory in April of 1982.

II. UNIFORM COMMERCIAL CODE

A. *Secured Transactions*

1. Consumer's Deficiency Liability

The key development in New Mexico law in the area of secured transactions during the survey year was the repeal of the statutory provision which insulated consumers from deficiency liability.[63] This change allows secured parties to obtain deficiency judgments where the disposition of collateral consisting of consumer goods does not yield enough money to discharge the secured indebtedness. With that change, New Mexico came into line with other jurisdictions which have adopted the Uniform Commercial Code.

As a result of this development, New Mexico consumer lenders are no longer forced to choose between repossession and action on the note against defaulting debtors. A lender is free to obtain a deficiency judgment if a foreclosure sale does not raise enough money to cover the indebtedness. As a practical matter, then, except in ex-

62. N.M. Stat. Ann. § 56-8-11.2(C) (Cum. Supp. 1981).

63. The clause which read "except, a debtor is not liable for any deficiency where the collateral involved is consumer goods," was deleted from N.M. Stat. Ann. § 55-9-504(2) (1978).

traordinary cases,[64] repossession and foreclosure should be the remedy of first resort for consumer lenders.

2. Retained Collateral—Accounting to Debtor

In another development touching secured transactions, the New Mexico Supreme Court considered whether a secured party who elects to retain collateral in satisfaction of an obligation must account to the debtor for a surplus in the sale of the goods if he intends to sell the retained collateral in the ordinary course of business. The court ruled that such an accounting must be given.

Begay v. Foutz & Tanner, Inc.[65] was a hard case involving the sharp practice of a pawnbroker. Two Indians, who were not astute in commercial matters, pawned some Indian jewelry to secure loans of much less than the value of the jewelry. The Indians defaulted, and the pawnbroker notified the Indians of its intent to retain the collateral in satisfaction of the debt.[66] When the Indians did not object to the proposed retention within the thirty days required by the statute,[67] the pawnbroker (which was a corporation) transferred the jewelry to its sale inventory and promptly sold the jewelry either to Joe Tanner, the president of the corporation, or to another corporation owned by Tanner.

The issue in *Begay* was an apparent conflict between §§ 504 and 505(2). Section 505(2) provides that if the secured party gives written notice of his intent to retain the collateral in satisfaction of the debt, and the debtor does not object within 30 days, the property may be retained by the secured party.[68] Section 504, however, provides that a secured party may sell the collateral, but he must account to the debtor for any surplus he realizes over the amount owed by the debtor.[69] The pawnbroker in *Begay* argued that an accounting was not required after the sale, because it had complied with the require-

64. It is possible to imagine a case where it would be better to sue on the note, even under the new law. The procedure required for foreclosure and sale takes some time, and it is only after the sale that the lender knows if the collateral was sufficient or if he must then file for a deficiency judgment. In a case where there is reason to believe that these delays would prejudice the creditor's ability to collect, the speedier remedy of bringing suit on the note might be preferable.

65. 94 N.M. 760, 617 P.2d 149 (1980).

66. 94 N.M. at 761, 617 P.2d at 150. This action was taken in compliance with N.M. Stat. Ann. § 55-9-505(2) (1978), which requires that the secured party give written notice to the borrower of intent to retain collateral. If written objection to the retention of collateral is not made within 30 days, the secured party may retain the collateral in satisfaction of the borrower's obligations. *Id.*

67. *See* note 66 *supra.*

68. *Id.*

69. *See* N.M. Stat. Ann. § 55-9-504 (Cum. Supp. 1981).

ments of § 505(2). The plaintiffs argued that the intention of the secured party should control. Where the secured party intends to sell the collateral, he must comply with the accounting provision of §504.

The court held that the pawnbroker should account to the Indians for the surplus value of the jewelry. It reasoned that the provision for retention of collateral was not intended as a means of escaping the secured party's obligation to account for a surplus.[70] The court considered the purpose of the accounting provision, and noted that the drafters of the 1972 revisions of the Uniform Commercial Code contemplated that retention of collateral is appropriate in *lieu* of sale.[71] Therefore, when the secured party intends to sell the collateral, § 505 must give way to § 504. The court required an accounting where, at the time the collateral was retained, the secured party contemplated reselling the collatteral in the ordinary course of business.

B. *Revocation of Acceptance*

The Uniform Commercial Code remedy of revocation of acceptance[72] was strengthened by the decision of the New Mexico Supreme Court in *Ybarra v. Modern Trailer Sales.*[73] Ybarra purchased a mobile home from Modern, and soon discovered that the floor of the home rose and bubbled. For the next four years, Ybarra periodically complained about the defect. Modern repeatedly assured Ybarra that the defect would be cured, and made several unsuccessful attempts to cure. Finally, Ybarra brought suit against Modern, seeking to revoke his acceptance of the mobile home. The trial court found for Ybarra. Modern appealed, claiming that the revocation was not made within a reasonable time.

The Uniform Commercial Code provides that a buyer may revoke acceptance of defective goods if: 1) the goods were accepted on the reasonable assumption that the defect would be cured and the defect has not been seasonably cured; or 2) the defect was difficult to discover or was not discovered because of the seller's assurances.[74] Such a defect must substantially impair the value of the goods to the buyer.[75] Further, the buyer must notify the seller of the revocation of acceptance within a "reasonable time" after the defect is, or should

70. 94 N.M. at 762, 617 P.2d at 151. *See* N.M. Stat. Ann. §55-9-504 (Cum. Sup. 1981).
71. 95 N.M. at 761, 617 P.2d at 150.
72. *See* N.M. Stat. Ann. §55-2-608(1) (1978).
73. 94 N.M. 249, 609 P.2d 331 (1980).
74. N.M. Stat. Ann. §55-2-608(1) (1978).
75. *Id.*

have been, discovered.[76] Revocation is not effective until such notice is given.[77]

In applying these rules to the facts of the *Ybarra* case, the supreme court took a lenient position with respect to the "reasonable time" requirement. The court decided that four years was a reasonable time for the buyer's revocation of acceptance when he continued to rely on the seller's assurances that the defect would be cured.

The buyer must give notice of revocation to the seller, and notice in the form of a lawsuit is not ordinarily sufficient.[78] The *Ybarra* court decided, however, that the notice need not recite any particular "magic words." The court noted that Modern was aware that Ybarra considered the goods unacceptable, and that Modern made several attempts to cure. The court decided that Modern was already familiar with the substance of Ybarra's complaint, and the formal notice afforded by the process server was sufficient in this case.[79]

The fact pattern of *Ybarra* is fairly typical of consumer "lemon" sales cases. The *Ybarra* decision opens the way to more frequent use of the powerful remedy of revocation of acceptance. Lawyers for purchasers should be alert to the possibility of revocation of acceptance of defective goods.

C. *Commercial Paper*

Three New Mexico cases decided during the Survey year dealt with commercial paper matters. These cases do not represent any far-reaching change or expansion of the law of commercial paper, but they do elucidate several undecided points relevant to commercial paper.

Farmington National Bank v. Basin Plastics, Inc.[80] involved a dispute between two persons who had helped a corporation obtain a loan. One of the parties had mortgaged property to secure the note. The other person had lent his credit to the corporation by signing the

76. *Id.* at § 55-2-608(2).

77. *Id.*

78. *See* Kohlenberger, Inc. v. Tyson's Food, Inc., 256 Ark. 584, 510 S.W.2d 555 (1974); Lynx, Inc. v. Ordnance Products, Inc., 273 Md. 1, 327 A.2d 502 (1974). (Cited by the *Ybarra* court for this proposition).

79. Modern argued that while it did have notice of the defect, it did not have notice of the intent to revoke acceptance. Therefore, the statute requiring notice, *see* note 56, *supra*, had not been complied with. The court answered this argument by considering the realities of such cases. The court stated that a buyer is generally not aware of the possibility of revoking acceptance until he consults a lawyer, and a lawsuit is imminent. This analysis implies that notice of the injury and dissatisfaction, rather than notice of intention to invoke a specific statutory remedy, is what the statute requires.

80. 94 N.M. 668, 615 P.2d 985 (1980).

note as an accommodation co-maker.[81] The corporation defaulted on the loan. Farmington National Bank sued the corporation, the mortgagor, and the co-maker for the balance due on the note. The bank also sought to foreclose on the mortgage. The mortgagor paid the balance due on the note to avoid the foreclosure. The claims against all defendants were dismissed with prejudice. The mortgagor then demanded contribution from the co-maker.

The co-maker argued that the payment by the mortgagor was voluntary, and that a voluntary payment did not give rise to a right of action for contribution. The New Mexico courts had never before addressed the question of whether a voluntary payment would bar the person who made the payment from recovering from a co-maker. The court conceded that a voluntary payment does not give a right of action against the co-obligor for contribution.[82] Relying on *Zontelli Brothers v. Northern Pacific Railway Co.*,[83] the court held that a right of action did accrue for contribution against a co-maker when the payment was compulsory. The court noted that "the payment must be compulsory only in the sense that the party paying was under legal obligation to do so . . . [i]t is not necessary that the claim be reduced to judgment before the party paying is entitled to contribution. . . ."[84] The court reasoned that the mortgagor in *Farmington National Bank* had not paid the note voluntarily, but was compelled to do so because of the mortgage. Accordingly, she was entitled to contribution because she had discharged an obligation shared by the co-maker.

In *Ward v. First National Bank in Albuquerque*[85] the bank negligently failed to stop payment on a check after being properly requested to do so. The corporation which wrote the check went into bankruptcy shortly after the check had been negligently paid. The debt for which the check was written would have been discharged in the bankruptcy proceedings. By honoring the check, the bank caused the assets of the bankrupt corporation to be diminished. Liquidation of the corporation thus provided less money for payment to the corporation's creditors, among which was the negligent bank. When the bank sued a guarantor of the corporation's indebtedness to the

81. An accommodation co-maker is one who signs his name, for the purpose of lending his credit to a transaction. *See* N.M. Stat. Ann. § 55-3-415(1) (1978).

82. The court relied on McLocklin v. Miller, 139 Ind. App. 443, 217 N.E.2d 50 (1966), for this proposition.

83. 263 F.2d 194 (8th Cir. 1959).

84. 94 N.M. at 672, 615 P.2d at 989, *quoting Zontelli Bros.*, 263 F.2d at 199.

85. 94 N.M. 701, 616 P.2d 414 (1980).

bank, the guarantor raised the bank's negligence in paying the stopped check as an offset.

The supreme court responded to this curious situation in a curious manner. The guaranty agreement was tightly written and included a recitation that the guarantor *unconditionally* guaranteed the corporation's debt to the bank. The court decided that the term "unconditionally" made the guaranty stand, even against the bank's own negligence, and upheld the bank's position. The supreme court was unwilling, however, to allow the bank to escape unscathed from its negligence, and taxed attorneys' fees and costs against the bank.

The First National Bank in Albuquerque did not fare so well, however, in connection with another technical mistake. *Rutherford v. Darwin*[86] involved an embezzlement scheme perpetrated by Darwin. Darwin drew $300,000.00 on a construction account belonging to a venture of which he was a general partner. He received the money in the form of a check, and, for reasons known only to himself, endorsed the check with a restrictive endorsement, directing that it be deposited to the account of the venture from which he was embezzling the money. He presented the check to a teller at the bank along with a deposit slip from another account over which he had control. The teller ignored the restrictive endorsement and deposited the check to the account shown on the deposit slip. By the time Darwin's chicancery came to light, the money was gone. The victim of the scheme sued Darwin, the owner of the account into which the money was deposited, and the bank. The trial court entered summary judgment against the bank.

On appeal, the bank argued that the court should recognize a doctrine of waiver with respect to restrictive endorsements. The court of appeals did not agree. The court ruled that the common law doctrine of waiver of restrictive endorsements which had been observed under the old Negotiable Instruments Law[87] was entirely precluded by the codification of the law of restrictive endorsements contained in the Uniform Commercial Code.[88] The court thus held that the bank was liable for depositing the check to the wrong account.

While this case involved a very unusual fact situation and an obscure legal issue, it may have a general effect on the application of common law principles to Uniform Commercial Code cases. Section 55-1-103 of the Code[89] specifically adopts the common law "[u]nless

86. 95 N.M. 340, 622 P.2d 134 (Ct. App. 1980).
87. *See* 1907 N.M. Laws ch. 83.
88. *See* N.M. Stat. Ann. § 55-3-205, -06 (1978).
89. N.M. Stat. Ann. § 55-1-103 (1978).

displaced by the particular provisions of [the Code]." The lesson of *Rutherford* is that a common law provision may be "displaced by . . . particular provisions" by implication. No particular provision in the Uniform Commercial Code *expressly* abrogates the doctrine of waiver of restrictive endorsements, but the *Rutherford* court held that the absence of the doctrine from particular provisions governing restrictive endorsements *impliedly* abrogated the doctrine.

III. MISCELLANEOUS DEVELOPMENTS

A. *Insurance Matters*

1. "Time-to-Sue" Provisions

A development of major significance which took place during the Survey year in the area of insurance law was the supreme court's upholding of "time-to-sue" provisions in insurance policies. In *Sanchez v. Kemper Insurance Companies,*[90] the insured sued upon a claim for damages to personal property which the insurance company had refused to pay. Suit was brought over a year after the alleged loss to the insured's property. The insurance company defended on the ground that the claim was barred by the one-year "time-to-sue" provision in the policy.[91] The insured urged the court to require the insurer to show both a substantial breach and that it had suffered prejudice as a result of the insured's tardiness before allowing the company to deny coverage on a time-to-sue provision. In support of this argument, the insured relied upon *Foundation Reserve Insurance Company v. Esquibel,*[92] where it was held that an insurer must show a substantial breach and prejudice as a result of the insured's lack of cooperation before asserting violation of a cooperation clause in order to deny coverage.

The supreme court rejected the insured's contention that the *Foundation Reserve* requirement of substantial breach and prejudice be extended to time-to-sue provisions. The court distinguished *Foundation Reserve* by noting that the public policy which supports the use of cooperation clauses is different from that which supports the use of time-to-sue provisions. Cooperation clauses, the court noted, are designed to prevent collusion between the insured and the injured, and thus avoid prejudice to the insurer. Time-to-sue provisions, by contrast, are chiefly designed to avoid stale claims and un-

90. 20 N.M. St. B. Bull. 323, 632 P.2d 343 (1981).

91. A "time-to-sue" provision is a provision in an insurance policy which limits the time within which suit against the insurance company can be commenced.

92. 94 N.M. 132, 607 P.2d 1150 (1980).

certainty of liability.[93] These policies of avoiding stale claims and uncertainty of liability are not concerned simply with protecting the insurer from prejudice.[94]

The decision in *Sanchez* restricts the use of the holding in *Federal Reserve.* Insurers and their counsel need no longer worry that *Federal Reserve* will lead to the elimination of technical policy defenses. Comparison of these two cases should be a great help to counsel on both sides of insurance cases in assessing the value of such defenses.

2. Simple Language Insurance Policies

Insurance policies are the first targets in New Mexico of the trend toward simpler language in consumer legal documents. The new Insurance Policy Language Simplification Act[95] requires that insurance policies achieve a minimum score of forty on the Flesch Reading Ease Test. The mechanics of the test are described in detail in the statute,[96] but the general effect will be to require policies to be expressed in short sentences which use short words. The passage of this act should put lawyers on notice that simple language requirements for other consumer documents may be imminent.

B. *Tortious Interference with Contractual Relations*

In *M & M Rental Tools, Inc. v. Milchem, Inc.*[97] the court of appeals clarified the law of tortious interference with prospective contractual relations. The court's ruling is not likely to encourage such actions in the future.

The plaintiff and defendant in *M & M* were competing pump rental businesses. An employee of the defendant happened to be visiting plaintiff's office when a prospective pump renter called. While plaintiff's employees were trying to determine whether plaintiff had a suitable pump available, defendant's employee asked to talk to the caller. Defendant's employee made arrangements for defendant to rent the caller a pump. Plaintiff sued for tortious interference with

93. 20 N.M. St. B. Bull. at 324, 632 P.2d at 345.

94. The court also suggested a contrast between the party who was most likely to be injured upon the breach of either of the clauses. The court noted that, where coverage is denied on the basis of a cooperation clause, the loser is most likely to be the innocent injured paty. Where coverage is denied on the basis of a time-to-sue provision, the loser is more likely to be the insured than his victim. *Id.*

95. N.M. Stat. Ann. §59-16A-1, -7 (Cum. Supp. 1981).

96. By calculation of this author, the Flesch score of the first 200 words of the Act is approximately 21. The Flesch score of the first 200 words of this article is approximately 47.

97. 94 N.M. 449, 612 P.2d 241 (Ct. App. 1980). For another view of this case, *see* Scales, *Torts,* 12 N.M. L. Rev. 481 (1982).

contractual relations. The trial court found no such interference, and the plaintiff appealed.

The court of appeals agreed with the trial court and adopted the description of the tort of interference with prospective contractual relations set out in the Second Restatement of Torts.[98] The court decided that the dispositive question was whether the defendant's interference was "improper." [99] In discussing whether the interference was improper, the court focused on the motive for the interference and the means by which the interference was accomplished.

The court held that an improper motive is present only when the sole motive is to harm another.[100] The court found that the defendant's motive in *M & M* was not improper, because the defendant was at least minimally concerned with getting business for himself, not exclusively hurting the plaintiff.

The court then discussed the issue of improper means. The court stated that "improper means refers to actions like misrepresentation, bribery, unfounded litigation, and defamation."[101] The court implied that the defendant's behavior was more on the order of bad manners or audacity, and held that the defendant did not use improper means.

Finally, the court dealt with the question of who has the burden of proof to show that an interference is improper. The court held that the burden rests on the plaintiff.[102] The court's requirement that the plaintiff show intent to harm, or use of means which are almost criminal in nature, ensures that this tort theory will not be much used in New Mexico.

C. *State Antitrust Law*

In *Rogers v. Consolidated Distributors, Inc.*,[103] a person wanting to sell Quasar television sets sued another retailer. Plaintiff alleged that the local distributor of Quasar television sets refused to sell to him because the other retailer in the area had threatened to discontinue his sale of the brand unless he was the exclusive retailer. Plaintiff alleged that this was a violation of state antitrust law. The trial

98. Restatement (Second) of Torts § 766B (1979).
99. 94 N.M. at 453, 612 P.2d at 245.
100. 94 N.M. at 494, 612 P.2d at 246.
101. *Id.*, *quoting* Prosser, Law of Torts (4th ed. 1971); Top Service Body Shop, Inc. v. Allstate Ins. Co., 283 Or. 201, 582 P.2d 1365 (1978).
102. 94 N.M. at 455, 612 P.2d at 247.
103. 95 N.M. at 467, 623 P.2d 587 (Ct. App. 1981).

court granted summary judgment for the defendant, and the plaintiff appealed.

Borrowing from the federal antitrust law,[104] the court of appeals ruled that a mere unilateral refusal to deal on the part of the distributor was not enough to establish an antitrust violation. The court required that a plaintiff must also show that the refusal to deal tended to restrain such trade or fix prices for the goods involved.

In affirming the summary judgment, the court examined the effects of the distributor's alleged refusal to sell on both intrabrand competition and interbrand competition. The court found that, while the distributor's refusal to sell to the plaintiff lessened intrabrand competition with respect to Quasar, the refusal could also enhance the competitive position of Quasar with respect to other brands, by allowing the manufacturer to achieve efficient distribution of its products. The court evaluated such a trade-off by a "rule of reason."[105] This evaluation involved a balancing of the reason for the refusal to deal against the harm it caused. The *Rogers* court found that the distributor's desire to maintain the strength in the marketplace of the existing retailer, and the desire to prevent the plaintiff from taking advantage of the other seller's advertising, more than balanced any harm suffered by the plaintiff. The only harm cited by the plaintiff was that he could not profit from selling the sets. The court ruled that the harm to the plaintiff was insufficient to raise a question of fact as to the lawfulness of the defendant's actions and affirmed the summary judgment.

104. 15 U.S.C. § 1 (1976). *See* Aviation Specialties, Inc. v. United Technologies Corp., 568 F.2d 1186 (5th Cir. 1978), cited by the *Rogers* court.

105. 95 N.M. at 469, 623 F.2d at 589, quoting Orec Corp. v. Whirlpool Corp., 579 F.2d 126, 131 (2d Cir. 1978). *See also* Wilson v. Albuquerque Bd. of Realtors, 82 N.M. 717, 487 P.2d 145 (Ct. App. 1971).