Contracts -- Credit Cards -- Liability of Holder for Unauthorized Use -- Issuer's and Merchants's Duty of Due Care in Accepting Charges

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sidered in light of the following statement by Mr. Justice Burton in *Bute v. Illinois*:\(^6\)

While such federal court practice does not establish a constitutional minimum standard of due process which must be observed in each state under the Fourteenth Amendment... [it] does afford an example approved by the courts of the United States. It thus contributes something toward establishing a general standard of due process currently and properly applicable to the states under the Fourteenth Amendment.\(^6\)

Applying this strict standard of impartial selection through the due process clause to criminal proceedings insures to a defendant those procedures that are "so rooted in the traditions and conscience of our people as to be ranked as fundamental."\(^6\) The adoption by all courts of this standard would do much to insure that all people, regardless of class, receive the same treatment under the same laws, an essential requirement of ordered liberty.

Established as the rules against discrimination are, violation of these rules continues with alarming regularity. By adopting a rule such as that applied by the Supreme Court to federal proceedings, all convictions in which there was systematic exclusion of a race or class contrary to statutory provisions would be subject to reversal. Under such circumstances a state would have no choice but to eliminate discrimination or abolish trial by jury, the latter a result which most state constitutions prohibit\(^6\) and which public conscience would not tolerate.

RALPH MALLOY McKEITHEN

Contracts—Credit Cards—Liability of Holder for Unauthorized Use—Issuer’s and Merchants’s Duty of Due Care in Accepting Charges

In *The Diners’ Club, Inc. v. Whited*,\(^1\) a California intermediate appellate court discussed a problem on which there are few re-

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61. *Id.* at 659-60.
63. *E.g.*, *N.C. Const.* art. I, § 13, which provides: "No person shall be convicted of any crime but by the unanimous verdict of a jury of good and lawful persons in open court.” For a compilation of state constitutional requirements as to the necessity of a jury trial in criminal proceedings, see *Judicial Conference of Senior Circuit Judges, Report of the Committee on Selection of Jurors* 33-35 (1942).

ported cases: the liability of the holder of a credit card for the unauthorized use of the card by another person. The usual three-party credit card situation was present in Diners' Club. The issuer furnished the card to the holder, and the merchants were to furnish merchandise to the holder. Two contracts were involved: one between the issuer and the merchant, whereby the issuer agreed to pay the merchant the amount of the holder's charges the merchant accepted; and another between the issuer and the holder, in which the holder agreed to repay the issuer and also to pay a small fee for the privilege of using the card. The holder in Diners' Club agreed to the following liability provision, similar to provisions used by most credit card issuers, printed on the back of his credit card: "If this credit card is lost or stolen, original holder is liable and responsible for all purchases charged through use of this card until . . . written notice [to the issuer] of its loss or theft." The holder's card was stolen while he was on vacation, and charges of 1,622.99 dollars were made by the thief before the holder

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3 There was no question here of acceptance of the terms of the contract by the holder. However, the problem has arisen in some cases as to whether the holder has accepted the terms of his contract. The question is usually one of consent, i.e., whether a reasonable person would have known that the terms were a part of his contract. In the absence of actual consent to the terms, it has been held, for example, that where the terms of an exculpatory clause are on a separate instrument, or where the clause is in cramped style, the contractual terms would not be binding. The Minnetonka, 146 Fed. 509 (2d Cir. 1906) (cramped style); Anaconda Copper Mining Co. v. Houston, 107 Ill. App. 183 (1903) (separate instrument). For a more complete discussion of this problem, see 22 LA. L. REV. 640 (1962).

4 Civil No. A 10872, App. Dep't Cal., Aug. 6, 1964. Other credit cards have similar provisions. The Cities Service credit card provides: "Customer named hereon agrees to pay all . . . charges . . . and notify Company in writing should card be lost or stolen." The customer's name and address is on the card, but no signature is required. The Esso Standard Oil Company credit card has the following clause printed on its back: "The customer assumes full responsibility for all purchases made by any person presenting this credit card. The customer should promptly notify the issuing office in writing if this card is stolen or lost and, if no such notification is received, it shall be conclusively presumed that any holder of this credit card has the customer's permission to use it." Again, the name of the customer is printed on the face of the card, but no signature is necessary.
discovered the theft and notified the issuer. The issuer brought suit under the contract liability provision to require the holder to pay for the unauthorized purchases made before written notice was received by the issuer. The trial court held for the issuer, saying the holder was absolutely bound by the liability provision.\(^5\)

On appeal, the appellate court reversed, holding that although the terms of the issuer-holder contract seemed to call for absolute liability for all purchases made with the card before notice, the issuer and the merchants nevertheless owed a duty of reasonable care to see that "irregular charges . . . [were] not unnecessarily incurred."\(^6\) The court found that there had been an actual assignment of the merchants' claims to the issuer and therefore held under general assignment law that the holder could assert any defenses against the issuer-assignee that he could assert against the merchant-assignor.\(^7\) However, the court indicated that the assignment was not essential to the decision and that it would have reached the same result in the absence of the actual assignment.\(^8\) Also, the court indicated that the showing of due care on the part of the issuer and the merchants was part of the issuer's case\(^9\) and said that the issuer had not carried this affirmative burden of proof.\(^10\)

The early cases that dealt with the liability of the holder for unauthorized purchases involved two-party situations in which credit was extended directly from an issuer-merchant to a holder, and no liability clauses were present.\(^11\) In each case, the issuer claimed that the holder should be liable for unauthorized purchases regardless of the absence of a liability provision. A conflict of authority on this question developed. A Pennsylvania case, *Wanamaker v. Megary*,\(^12\) used the novel approach of treating the credit card that the imposter had taken from the holder as a negotiable instrument. Under this theory, the issuer-merchant became a holder in due course when he accepted the charges and could enforce the charges against the credit card holder, who was viewed

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\(^6\) Id. at 3.
\(^7\) Ibid.
\(^8\) Id. at 4.
\(^9\) Ibid.
\(^10\) Ibid.
as an indorser of a note. Cases from other jurisdictions strongly criticized this approach, and a later Pennsylvania case expressly disapproved it. The other view was that because there was no contractual obligation to pay for unauthorized charges, the holder could not be liable. All courts, however, completely ignored the question of negligence and did not discuss whether due care should be required of either party. Rather, the courts were concerned solely with whether an absolute contractual obligation on the part of the holder to pay for unauthorized charges should be implied.

The first three-party case also involved a contract in which there was no liability clause. That case, Gulf Refining Co. v. Plotnik, held for the first time that there was an implied obligation on each party in the credit card arrangement to use due care. But the court said that in the absence of any negligence, the holder would not be liable because there was no liability clause. In Plotnik, however, the holder was held liable because the unauthorized charges had been incurred as a result of his negligence.

In an attempt to shift liability for unauthorized purchases to the holder, the issuers began to include liability provisions, similar to the clause in the Diners' Club contract, in their issuer-holder contracts. These clauses have been present in all reported cases since Plotnik. The courts in these cases have been faced with the problem of whether the clauses, which seemingly called for absolute liability for all purchases made with the card, should be strictly construed against the holder. A conflict of authority has arisen on this question also. One view says that the issuer, after paying the charges to the merchant, becomes an assignee of the merchant and

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13 Id. at 779.
16 Lit Bros. v. Haines, 98 N.J.L. 658, 121 Atl. 131 (Sup. Ct. 1923). Accord, Jones Store Co. v. Kelly, 225 Mo. App. 833, 36 S.W.2d 681 (1931). In Kelly there was an agency question, and the court held that even though the holder would not be liable for unauthorized charges, he would be liable if he had authorized the charges. 36 S.W.2d at 683.
18 Id. at 151.
19 Ibid.
20 The holder received bills for some of the charges incurred after his card was stolen, but he did not pay them, and did not notify the issuer until a few weeks later of the fact that his card had been stolen.
21 See text accompanying note 4 supra.
that under general assignment law the holder can assert any defense against the issuer that he can against the merchant.22 The courts following this view hold that the issuer and the merchant are required to exercise due care in accepting credit charges.23 The same courts have also regarded the holder as a guarantor,24 one court saying that the situation could be classified as one of "suretyship, guaranty, or indemnity"25 and that "it is immaterial which of these terms would most accurately describe the relationship . . . ."26 The imposter who makes the unauthorized purchases is regarded as the principal debtor, the merchants and the issuer are treated as the creditors, and the holder is treated as a gratuitous guarantor, a favorite of the law. Therefore, "it is necessarily implied from this broad guaranty that the person extending credit [the merchant] must do so in good faith . . . ."27 Thus, before Diners' Club, some courts required due care by all parties to the credit card arrangement, saying that an assignment or guaranty situation existed.

The other view is that the holder owes a direct contractual obligation to the issuer to pay for all purchases made with his card. Under this view, the contractual provision is decisive of liability, and negligence on the part of the merchant in accepting charges is unimportant. One case expounding this view is Texaco, Inc. v. Goldstein.28 The holder was held liable for all purchases made with his card because of the terms of the liability clause of the issuer-holder contract,29 which were "that of an original undertaking in which the . . . [holder] made it his own responsibility for any use

22 Gulf Refining Co. v. Williams Roofing Co., 208 Ark. 362, 186 S.W.2d 790 (1945); Union Oil Co. v. Lull, 220 Ore. 412, 349 P.2d 243 (1960). The card in Union Oil provided: "The customer . . . guarantees payment . . . of price of products delivered or services rendered by anyone presenting this card . . . until card is surrendered or written notice is received by the company that it is lost or stolen." Id. at 416, 349 P.2d at 245.

23 See cases cited note 22 supra.

24 See cases cited note 22 supra.


26 Ibid.


28 34 Misc. 2d 751, 229 N.Y.S.2d 51 (1962).

29 The Texaco card provided: "the person . . . whose name is embossed on the reverse side thereof . . . assumes full responsibility for all purchases made hereunder by any one through the use of this credit card prior to surrendering it to the company or to giving the company notice in writing that the card has been lost or stolen." 229 N.Y.S.2d at 53.
The court said that they so held because there would be an impairment of the credit card system if a “high duty of diligence” was required of issuers and merchants. The court in Texaco distinguished the cases in which the holder was treated as a guarantor because the word “guaranty,” present in the issuer-holder contracts in those cases, was absent from the Texaco card. Therefore, said the court, good faith on the part of the issuers and the merchants in accepting charges, implicit in the guaranty situation, was not required under the Texaco contract. The court, however, did not discuss the fact that the courts in the cases it distinguished did not rely on the guaranty theory alone, but rather would have reached the same result on the assignment theory.

Diners’ Club, which rejected the Texaco approach, makes significant additions to the growing body of credit card law. Although the court approved the decisions requiring due care of issuers and merchants on assignment and guaranty theories and found an actual assignment, it indicated that it would have reached the same result in the absence of the assignment. Thus, Diners’ Club implies that the issuer and the merchant have to use due care in accepting credit card charges regardless of the contractual provisions and regardless of whether there is present a guaranty or assignment situation. If due care is used by the issuers and merchants, the holder will be held liable under the contractual liability provision in the issuer-holder contract.

The case is also significant because the court indicated that it followed the rule, announced in Union Oil Co. v. Lull, that the issuer suing a holder on the liability provision has the burden of proving that both it and the merchant involved used due care in

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30 Id. at 54.
31 Id. at 55. Another case which seems to hold the same way is Magnolia Petroleum Co. v. McMillan, 168 S.W.2d 881 (Tex. Civ. App. 1943). The Magnolia credit card provided that the “holder shall be responsible for all purchases made by use of this card . . . whether or not such purchases are made by the named holder . . . .” Ibid. The court seemed to hold that because of the terms of the issuer-holder contract, the holder was absolutely liable for all purchases made with his card. The only defense the holder had set up was that the charges had been made by an unauthorized person, and the court held that this was not a valid defense; however, it was not made clear from the decision whether there were other defenses which the holder could have asserted.
32 229 N.Y.S.2d at 54.
accepting the charges. *Lull* has been criticized by one commentator,\(^4\) who expressed fear that this requirement usually will result in the issuer losing the case. This criticism is based on the fact that it will often be impossible for the merchant to recall all his actions, even if due care was in fact used, and also on the fact that costs in locating the necessary witnesses and taking depositions will often be prohibitive.\(^5\) Granting that this rule may often be harsh on the issuer, it would be even harsher to put this burden of proof on the holder. The holder is not present when the charges are incurred, and unlike the issuer, it would be impossible in most instances for him to prove that due care was not used. The issuer can require the merchants to develop methods of recording the details of each transaction and also require them to develop a uniform system of checking all charges. By following such a system, the issuer can prevent many unauthorized charges and also more easily meet his burden of proof.

The court in *Diners' Club* did not decide the question, raised in the holder's brief,\(^6\) of whether the holder would ever be liable in the case of a forgery. A forgery occurs under the Diners' Club contract when someone other than the authorized holder uses the card. This is because the person making purchases must sign his name to a sales slip, and a contractual provision in the issuer-holder contract (incorporated by reference) provides: “The Credit Card is not transferable and *will be honored only* when properly signed and presented by the *authorized holder*.\(^7\) The reason the possibility existed that the holder would never be liable in the case of a forgery was because of an ambiguity between this clause and the issuer-holder provision which seemingly called for absolute liability for all unauthorized purchases. Obviously, when an imposter presents the card he is not an “authorized holder,” and under this provision the card should not be honored. Thus, the two contractual provisions present the anomalous situation in which unauthorized charges are not to be accepted, but if they are, the holder is absolutely responsible for them. The holder urged that because of the

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\(^5\) Ibid.
\(^7\) Civil No. A 10872, App. Dept Cal., Aug. 6, 1964, at 2. (Emphasis added.)
uncertainty of these contradictory provisions, the ambiguity should be resolved against the issuer and the holder should never be liable for unauthorized purchases. The court did not reach this problem because there were other grounds on which to base the decision, but it was indicated that “there is much merit to this argument . . . .” However, it was also pointed out that this problem is not one of general interest because “it can be avoided easily by properly drafting the contract,” as has been done in some oil company contracts where the card is not signed by the holder and is not restricted to the holder’s use.

If the court had been faced only with the liability question in Diners’ Club, the case would have been reversed and remanded so as to give the issuer an opportunity to allege and prove the use of due care in accepting the unauthorized charges. However, the court found that because of the terms of the issuer-merchant contract, the issuer could never prove damages. The court pointed out that the difficulty arose because the issuer-merchant contract was not worded the same as the issuer-holder contract. The issuer-holder contract provided that the holder was to pay the issuer for any charges incurred with the holder’s card. The issuer-merchant contract, however, provided that the issuer undertook “to purchase . . . all valid charges . . .” and that in order to be a valid charge “the signature of the cardholder . . . must be the same as that appearing on the face of the card.” It is obvious that the charges accepted by the merchants from the thief, whose signature was not the same as the one appearing on the card, were not valid charges. Therefore, when the issuer purchased the charges which were the basis of this suit, it made the payments voluntarily “to promote its own good will among merchants.” The court said that such a “voluntary payment is not damage.” This decision will obviously result in more careful draftsmanship of the issuer-merchants contracts in the future, with the issuers being careful to provide that their payments to the merchants are not “voluntary.”

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8 Id. at 4.
9 Id. at 4-5.
10 Id. at 5.
11 Ibid.
12 Ibid.
13 Id. at 2. (Emphasis added.)
14 Ibid.
15 Id. at 6.
16 Ibid.
Because of the great amount of business done with credit cards, it is vital that there be some definitive solution to the problem of which of the two parties, the issuer or the holder, should be held responsible for unauthorized purchases made with credit cards. It appears that the result reached in Diners' Club is the fairest. If neither the issuer, holder, nor merchant has been negligent, and if the parties have used due care in carrying out their various duties, or if only the holder has been negligent, the contractual liability clause between the issuer and the holder should be given full force and the holder should be liable for the unauthorized purchases. However, as between the holder and the issuer, the issuer is better in a position to prevent unauthorized charges. Therefore, if the issuer or merchant has been negligent in accepting charges, the issuer and not the holder should be the one to suffer. To hold otherwise would be to encourage lax practices among the merchants, for the merchants' examination of credit cards would become even more perfunctory than at present if they knew they would be repaid regardless of whether the charges were authorized. Requiring due care by all parties in the three-party credit card situation is the most equitable solution to the problem.

HOWARD S. IRVIN

Criminal Law—Statutory Rape—Mistake of Age—Mens Rea

Prior to People v. Hernandez, all American jurisdictions faced with an ignorance or mistake of age plea in statutory rape cases have held it not to be a valid defense. Upon facts showing that the defendant and the prosecutrix were not married, that the prosecutrix was under the statutory age of eighteen, and that the prosecutrix

1 39 Cal. Rptr. 361, 393 P.2d 673 (Cal. 1964).

2 Ignorance of age is no defense even though based on a good faith belief that the female was above the prohibited age. Commonwealth v. Murphy, 165 Mass. 66, 42 N.E. 504 (1895); State v. Houx, 109 Mo. 654, 19 S.W. 35 (1892). This is true even where there has been an exercise of reasonable care to ascertain her age. Manning v. State, 43 Tex. Crim. 302, 65 S.W. 920 (1901). It is also true where the defendant was misled by her appearance or her misrepresentations. Brown v. State, 23 Del. 159, 74 Atl. 836 (7 Penn. 1909); Heath v. State, 173 Ind. 296, 90 N.E. 310 (1910); Harris v. State, 115 Tex. Crim. 227, 28 S.W.2d 813 (1930). See generally 1 WHARTON, CRIMINAL LAW AND PROCEDURE § 241 (12th ed. 1952).

3 CAL. PENAL CODE § 261.