Preserving Consumer Defenses
In Credit Card Transactions

Since the development of the installment sales contract, waiver of defense clauses have been used in consumer finance transactions to provide banks and finance companies with a freedom from contractual defenses equivalent to that enjoyed by the holder in due course of a negotiable instrument. Consumers who finance purchases by means of an agreement containing such a clause waive the right to raise against an assignee of the contract any claim of defense to payment that they might have against the seller-assignor.

The operative consequences of a waiver of defense clause become most apparent to the consumer when he discovers that he has purchased defective merchandise from a merchant who ignores legitimate requests for refund or cure. The most effective self-help weapon a consumer debtor possesses is his refusal to make further payments on the goods until his complaints have been satisfied. In signing a contract containing a waiver of defense clause, the consumer foregoes this leverage. He agrees to make full payment to any subsequent assignee regardless of the merchant's failure to perform his contractual obligations, however willful or outrageous the seller's conduct may be. At this point the only remedy available to the buyer is a lawsuit against the merchant—a remedy which, in the context of consumer transactions, rarely provides effective relief. Not only does the expense of litigation generally exceed the amount which the buyer can hope to recover, but many merchants who regularly engage in fraud and

1. For a general discussion of the development of waiver of defense clauses and the judicial reaction to their use in consumer financing, see Gilmore, The Commercial Doctrine of Good Faith Purchase, 63 YALE L.J. 1057, 1093-1102 (1954).
2. Under the UNIFORM COMMERCIAL CODE § 3-305 [hereinafter cited as U.C.C.], as under prior law, a holder in due course takes a negotiable instrument free from all defenses of any party to the instrument with whom he has not dealt, except "real" defenses such as infancy, duress and fraud in the factum. While the literal terms of most waiver of defense clauses would cover even these defenses, most courts have permitted "real" defenses to be raised in spite of a waiver clause. See, e.g., Anglo-California Trust Co. v. Hall, 61 Utah 223, 211 P. 991 (1922) (dictum) and Gilmore, supra note 1, at 1096. U.C.C. § 9-206(1) continues this rule. See also ILL. REV. STAT. ch. 121/5, § 518 (Supp. 1972).
The one thing certain about the typical consumer's execution of a purchase contract with a waiver of defense clause is that he is unaware of the consequences of signing.
deception may have arranged their affairs so as to be virtually judgment proof.

As a result of mounting pressure\(^6\) for corrective action and more than a few spectacular instances of abuse,\(^6\) the use of waiver of defense clauses in installment sales contracts is now prohibited, or strictly regulated, in a majority of states.\(^7\) The Federal Trade Commission

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5. No single aspect of consumer credit causes more outrage to consumer spokes-
men and insistence on statutory change . . . .


During the 1950's, the drafting of the U.C.C. became the focus of the debate. The earliest drafts of § 9-206 prohibited the use of waiver of defense clauses in all con-
sumer transactions. However, such pro-consumer provisions were successfully repelled by banks and finance companies. See 1 G. GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY 293-94 (1965). A similar battle was also waged over the UNIFORM CONSUMER CREDIT CODE [hereinafter cited as U.C.C.C.]. The earliest drafts of the U.C.C.C. flatly prohibited the use of waiver of defense clauses. An attack by financial interests once again forced the pro-consumer draftsmen to retreat. Compare § 6.102 (First Tent. Draft 1966) with § 2.404 (Official Text 1968). See Murphy, Another "Assault Upon the Citadel": Limiting the Use of Negotiable Notes and Waiver of Defense Clauses in Consumer Sales, 29 OHIO ST. L.J. 667, 680-85 (1968).


7. Legislation or judicial decisions currently prohibit, or greatly restrict, the use of waiver of defense clauses in at least twenty-eight states and the District of Columbia.

They are made wholly unenforceable by statutes in the following sixteen states: ALA.


Judicial decisions prohibit the use of waiver of defense clauses in four additional states: Connecticu

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may soon universalize the prohibition by declaring the use of these clauses an unfair trade practice.8

Nevertheless, over 9,000 banks throughout the United States currently finance consumer purchases by means of credit card agreements containing waiver of defense clauses.9 The effect of these clauses is exactly the same as those which appear in installment sales contracts, yet the credit card agreements have been drafted in a manner which places them beyond the scope of most statutory restrictions.10

Until recently, this discrepancy between the legal restrictions placed on installment sales contracts and the laissez-faire attitude accorded to bank credit cards has not been a matter of great concern.11 Since bank credit cards are rapidly becoming the dominant means of fi-


8. 36 Fed. Reg. 1211-12 (1971). Hearings on the proposed trade regulations were held in 1971 but a decision has yet to be announced. 4 Consumer Credit Guide, Report No. 78 (Oct. 12, 1971).

9. As of June 30, 1971, the Interbank Card Association (Master Charge) and the Bank of America reported that 9365 banks were associated with their respective credit card systems. Both require the use of waiver of defense clauses in contracts drafted by member banks. American Banker, August 19, 1971, at 6, col. 3. This figure represents nearly sixty-seven per cent of the 14,000 commercial banks in the United States and does not include numerous banks which issue credit cards independent of the two major systems.

10. See Bergsten, Credit Cards—A Prelude to the Cashless Society, 8 B.C. Ind. & Com. L. Rev. 485, 511 (1967). Generally, the statutes prohibiting the use of waiver of defense clauses are drafted in language applicable only to instruments in which the waiver clause is made operative by means of assignment. See, e.g., N.Y. Pers. Prop. Law § 403(3)(a) (McKinney 1971 Supp.); No retail installment contract of obligation shall contain any provision by which the buyer agrees not to assert against an assignee a claim or defense arising out of the sale. See also U.C.C.C. § 2-404 (Official Text).

In the vast majority of credit card agreements, the consumer's obligation to make payments to the issuer bank is phrased in terms of a direct obligation rather than an assignment from a merchant. By incorporating the waiver of defense clause in its contract with the cardholder, rather than in a merchant-consumer agreement (where it appears in installment sales contracts), the issuer bank is able to cut off consumer defenses without relying on the device of assignment.

A rare exception to this direct obligation format is the credit card agreement described in Clontz, Bank Credit Cards Under the Uniform Commercial Code, 87 Banking L.J. 888 (1970). It was drafted on an assignment model for use in North Carolina, one of the states which has never placed restrictions upon the use of waiver of defense clauses.


11. See Rosenthal, Negotiability—Who Needs It?, 71 Colum. L. Rev. 375, 400-01 (1971). The use of waiver of defense clauses in credit card agreements was first noted in Bergsten, supra note 10, at 509-17, where the author "ruminated" over some of the problems raised, but reached no clear conclusions. See also Navin, supra note 5, at 531, where the author describes his discovery of the clause in his credit card as a "puzzlement," and exclaims "how about that?"
nancing consumer purchases, however, the inconsistency can no longer be ignored.

In view of the widespread efforts to abolish the use of waiver of defense clauses in installment sales contracts and other assignment-type consumer financing, this Note will examine the desirability of their elimination from credit card agreements as well. Rather than add to the painstaking efforts to characterize credit card transactions in terms of existing legal doctrines and definitions, this Note will concentrate on a more functional analysis of credit cards and the practical effect of waiver of defense clauses. The view which the law should take of credit card transactions and merchant-consumer disputes can be best informed by an analysis of underlying economic realities.

12. According to Federal Reserve System statistics, as of August 31, 1971, approximately $3.2 billion of installment credit was outstanding on bank credit card accounts alone. This figure represents thirty-five per cent of the consumer goods installment credit held by commercial banks, other than automobile financing. Federal Reserve System, Consumer Credit, Statistical Release G. 19 (Oct. 4, 1971).

13. In addition to the three statutes described in note 10 supra, bills prohibiting the use of waiver of defense clauses in bank credit cards were introduced in at least one other state legislature and the Congress during 1971. See S. 6483-A, N.Y. Legis., 1971-72 Reg. Sess. (April 22, 1971); S. 652, 92d Cong., 1st Sess. § 169 (1971).


Brandel & Leonard, Bank Credit Cards: New Cash or New Credit, 69 Mich. L. Rev. 1035 (1971) [hereinafter cited as Brandel & Leonard] is the most recent effort. Devoting fully twenty-five pages to such analogies and characterizations, they conclude at one point:

The multiparty bank charge card transaction appears to be a hybrid of the traveler's or "clean" letter of credit and the commercial or documentary letter of credit, although it more closely resembles the latter.

and later:

The premise upon which to proceed by analogy for the convenience card transaction is that of the cash sale. For these transactions, the charge card system . . . replaces cash.

... . . .

As to such transactions, the card holder should be in no better, nor worse, position than if he had paid for his purchase with cash.

Id. at 1046-47, 1051.

U.C.C.C. § 1.301(9) continues this unfortunate trend, analogizing credit card banks to lenders. The most obvious distinction between unsecured loans and credit card purchases is that the latter can be made only from merchants whom the bank has solicited to join its system. Even assuming the usefulness of some past analogies, this Note argues that a functional analysis of bank credit cards is the only coherent way to discuss what is clearly a new phenomenon, and calls for the abolition of waiver of defense clauses.
I. Credit Card Contracts

The operational characteristics of bank credit cards are generally familiar.\textsuperscript{15} The individual bank credit card transaction is a three-sided arrangement which involves a cardholder, a merchant and a bank.\textsuperscript{16}

The contract between the cardholder and the bank primarily contains an authorization for the bank (issuer) to pay money upon the presentation of invoices or "sales slips," and the terms under which the cardholder is to repay the bank for credit so extended. In addition, a typical "cardholder agreement"\textsuperscript{17} also contains a waiver of defense clause and a provision entitling the issuer to recover all costs incurred in collecting an indebtedness owed by the cardholder.\textsuperscript{18}

The contract between the merchant and the bank sets forth the terms under which the bank will accept sales slips presented by the merchant and, in addition, contains a number of general limitations on the merchant's business practices.\textsuperscript{19} Among other typical provisions contained in "merchant agreements" are two which deserve special attention. The first gives the bank the right to inspect the merchant's books and financial records. The second is an agreement which gives

15. The best description of the mechanics of bank credit transactions is Davenport, supra note 14. The characteristics of bank credit card systems, including the role of regional clearing centers, are briefly described in Brandel & Leonard, supra note 14, at 1094-37.
16. Many bank credit card transactions actually involve two separate banks—one called the "issuer bank" with whom the cardholder deals and a second called the "depository bank" from which the merchant receives payment. Because the role of the bank may be split in this manner, it is technically incorrect to speak of bank credit cards as purely "tripartite" devices. However, almost all credit card banks perform both functions. Therefore, it is simpler to analyze credit card transactions in tripartite terms, reserving discussion of the realistic quadripartite model for later. See pp. 280-01 infra.
17. The contract between the cardholder and the issuer bank will be referred to as the "cardholder agreement," and the depository bank/merchant contract as the "sales agreement." In situations where two banks are related in an interchange system, the contract between them shall be called the "interbank agreement."
18. Copies of both a cardholder and a merchant agreement used by a Master Charge bank in the midwest are included in an appendix to Davenport, supra note 14, at 976-85. Virtually all of the clauses referred to in this Note also appear in that appendix.
19. Typical are requirements that the merchant honor all valid credit cards issued by banks within the system; that he display promotional material supplied by the bank advertising his membership in the credit card plan; that he establish a "fair" policy regarding the exchange, return or adjustment of merchandise purchased by credit cardholders.

A very large number of these contracts also contain a clause by which the merchant agrees not to discriminate as to price, service or otherwise against any cardholder desiring to use his credit card in a transaction with merchant. See, e.g., Davenport, supra note 14, at 985, clause 13(a). By thus limiting the merchant's freedom to establish his own prices, such clauses may constitute price-fixing agreements, illegal per se under the antitrust laws. See, e.g., United States v. Socony-Vacuum Oil Co., 310 U.S. 150 (1940).

While both the Federal Trade Commission and the Justice Department are aware of the existence and widespread use of such agreements, they have, as yet, failed to take any action. See Hearings Pursuant to H. Res. 66 Before the Subcomm. on Special Small Business Problems of the Select House Comm. on Small Business, 91st Cong., 2d Sess., at 132, 158, 173 (1970) [hereinafter cited as Credit Card Hearings].
the bank broad chargeback privileges, including the right to recourse against the merchant in the event a cardholder refuses payment because of a sale-related defense or claim.\textsuperscript{20}

The relationship between the cardholder and merchant arises from an exchange of goods or services in return for a sales slip which the cardholder signs at the time of sale. The sales slip itself is primarily an evidentiary device, recording the date, nature and amount of the purchase and identifying the buyer and seller.\textsuperscript{21} It does not incorporate any of the terms of the agreement between the cardholder and merchant, which are either set out in a separate document or left to be "implied at law."\textsuperscript{22}

II. \textit{Filter Queen}

One major objection to the use of waiver of defense clauses or negotiable instruments in consumer transactions has been that by insulating banks and finance companies from responsibility for the

\textsuperscript{20} A typical recourse clause provides: BANK may refuse to accept any sales slip or revoke its prior acceptance thereof in any one or more of the following circumstances: . . . (b) the cardholder in such sale disputes his liability to BANK on any one or more of the following grounds: (1) that the merchandise or services covered by such sales slip were returned, rejected, or defective in some respect, or MERCHANT agrees to repay BANK the amount theretofore paid by it or credited to the MERCHANT's account. This clause is taken from a Master Charge merchant agreement currently used in Connecticut. Similar clauses appear in virtually all merchant agreements. \textit{See}, e.g., Davenport, supra note 14, at 983, clause 14; Rosenthal, supra note 11, at 400-01 nn.116.

\textsuperscript{21} Except for those few credit cards designed as assignment devices (\textit{see} Clontz, supra note 10), execution of a sales slip does not create any express obligation from the cardholder to the merchant. Under almost all bank credit cards, the consumer's payment obligation runs solely to the bank. The language used on the face of sales slips has changed considerably in recent years. Older sales slips were apt to be drafted as quasi-negotiable instruments depicting the consumer/buyer as the "acceptor" of a draft drawn by the seller and made payable to the issuer bank, or order. It is clear that none of the participants in credit card sales ever viewed themselves in the manner suggested by the early sales slips. Most sales slips used today exhibit more candor, merely restating the cardholder's general obligation as set forth in the cardholder agreement. The operative language of a current Master Charge sales slip provides:

The issuer of the card identified on the sales slip is authorized to pay the amount shown as TOTAL upon proper presentation. I [cardholder] promise to pay such TOTAL (together with any other charges due thereupon) subject to and in accordance with the agreement governing the use of such card.

The current Uni-Card sales slip contains a complete "Retail Instalment [sic] Credit Agreement" on its rear side. The Agreement contains, \textit{inter alia}, a waiver of defense clause:

Uni-Card is not responsible . . . for disputes regarding goods and services, and such disputes will be settled by me directly with Member [merchant] without affecting any indebtedness owing to Uni-Card.

\textsuperscript{22} Aside from the different nature of the buyer's payment obligation in a credit card sale, the merchant-cardholder relationship is the same as would exist if it had been a cash sale. The absence of a written agreement does not change the relationship which the law implies, concerning warranties made by the seller, or the buyer's or seller's rights and remedies set forth by the Uniform Commercial Code.
practices of the merchants with whom they deal, these devices have permitted financiers to relax, or even discard, standards of merchant conduct and solvency. Any belief that credit card financing was immune from similar abuses has been called into question by a case being litigated in California. *Payne v. Filter Queen of Hayward, Inc.* involves a major credit card bank which financed the sales of an allegedly undercapitalized corporation which employed door-to-door salesmen to sell vacuum cleaners.

A list of the techniques allegedly employed by Filter Queen's salesmen reads like a handbook on consumer fraud. Plaintiffs have claimed that prospective purchasers were solicited by telephone and told that they had “won” the right to participate in a drawing for a new automobile; if they called a certain telephone number, they would receive an additional $5 cash prize. Persons who called in response to these representations learned that they would receive the $5 only if they consented to a home demonstration of the Filter Queen vacuum cleaner. Among the alleged representations made during the subsequent home demonstrations were claims that the vacuum cleaner would function as an air conditioner and that if the consumer agreed to purchase the vacuum cleaner, he would receive an “Owner's Dividend Certificate” which would entitle him to a $10 dividend for each one of his friends who would agree to a home demonstration. Plaintiffs claim that none of these promises was fulfilled.

Filter Queen originally financed its vacuum cleaner sales by means of installment sales contracts, which were routinely assigned to a finance company. This arrangement was discarded when Filter Queen was solicited and approved by a bank as a member of its credit card

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23. Empirical investigations have suggested that the single most important factor in retail merchant fraud is the ability of banks and finance companies to purchase sales contracts from merchants without any incentive to inquire into the merchant’s practices, reputation or financial stability. See Comment, *supra* note 4, at 395, 414. See also *Federal Trade Commission, Report on the District of Columbia Consumer Protection Program* 17-18 (1968).

24. Civil No. 384418 (Alameda County Super. Ct. Calif., June 16, 1959), *appeal filed*, Civil No. 27751 (Calif. Ct. App. 1st Dist., May 13, 1970). The case is a class action by defrauded consumers seeking rescission and damages against Filter Queen and the bank and finance company which had financed its sales. At present the case is on appeal from a decision granting the bank's motion to dismiss the complaint without leave to amend because of failure to establish a proper class. The “facts” of the case as set forth in the text are largely taken from the plaintiff-appellant's brief. However, most of the allegations concerning Filter Queen's practices and its involvement with the bank are uncontested.

The change in financial arrangements allegedly did nothing to alter Filter Queen's practices. If a prospective purchaser did not have a bank credit card at the time of the home demonstration, the session was extended to allow the salesman to take out an application on his behalf. Shortly after the bank accepted Filter Queen as a merchant it allegedly began to receive complaints from its cardholders; within a month and a half, it terminated its relationship with the merchant, having already discounted $28,000 worth of vacuum cleaner sales slips.

After the bank terminated its credit card relationship with Filter Queen, the company ceased operations and its principals disappeared. At this juncture, the critical question was one that lies at the heart of the debate over the use of waiver of defense clauses: who should bear the loss, the consumer or the bank? Because the use of waiver of defense clauses in installment sales contracts is illegal in California, those consumers who bought under installment contracts have retained their ability to assert the defenses of fraud and breach of contract against the finance company to which their obligations had been assigned. Those who used credit cards, however, have no such protection against their issuing bank. They find themselves in the unenviable position of being potentially liable to the bank for the full purchase price of the defective vacuum cleaners.

III. The Nature of the Problem: Unremedied Losses

A. Sources of Unremedied Loss for Consumers

When a consumer is defrauded in a credit card-financed retail sale, when he purchases merchandise which proves to be defective, or fails to receive the goods purchased, he incurs a "loss." The ultimate

26. Among the attractions of credit card financing was that the bank would finance Filter Queen's sales at a discount rate of only 3 per cent. While the record does not show the rate Filter Queen had been forced to pay finance companies to discount its installment sales contracts, it was undoubtedly much higher. For example, the discount rate charged for similar financing in Star Credit Corp. v. Molina, 59 Misc.2d 290, 298 N.Y.S.2d 570, 574 (Civ. Ct. 1969) was 20 per cent.
27. CAL. CIV. CODE § 1804.2 (West 1970). California is now one of the three states which have enacted statutory prohibitions against the use of waiver of defense clauses in credit card transactions. See note 10 supra.
28. The purchase price was an astonishing $320-345.
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consequence of this loss, however, depends on whether the consumer can obtain relief from the merchant involved, or from the issuer bank. If the merchant is willing to refund the buyer's money or provide some other satisfactory cure, the effects of the loss will be minor and temporary. The difficult cases are those where the consumer and merchant are unable to resolve their disagreement. While the right to institute legal action against the merchant is theoretically available, it rarely provides effective relief. The merchant, for example, may be insolvent or otherwise unavailable for suit. Even if he can be reached by a lawsuit, the expense of litigation often exceeds the amount of the consumer's claim.

In this context, the self-help remedy of refusing to pay the money still owed on the goods in question has the advantage of limiting the consumer's loss to the amounts already paid. This device is not only unaffected by the merchant's insolvency, but, since it can be invoked by the consumer himself, also avoids non-recoverable attorney's fees. The effect of such a refusal to pay, of course, shifts the loss to the bank which financed the sale, and this is the institution which is left with the task of seeking recovery from the offending merchant. It is precisely this sequence of events which banks seek to avoid by placing waiver of defense clauses in cardholder agreements.

30. The threat of a call to the "Better Business Bureau" is virtually a waste of breath. See Comment, supra note 4, at 401. Since merchants who engage in this kind of unsavory conduct hardly expect defrauded customers to return for more of the same, the threat of taking one's patronage elsewhere is equally unavailing.


32. The average amount of an individual credit card sale is approximately $20. Credit Card Hearings, supra note 19, at 104. See also Brandel & Leonard, supra note 14, at 1060. The cost of hiring an attorney for even the most limited purposes far exceeds this amount.

33. As used here and throughout this Note, "insolvency" is generally meant to include all instances in which a party is judgment proof or otherwise unavailable for suit. 

34. If the merchant himself had financed the sale, the consumer's refusal to pay would have the effect of extinguishing the loss. However, self-financing is generally limited to large retail chains which have large amounts of capital. Since these large stores rarely make a practice of engaging in fraud or refusal to satisfy legitimate consumer complaints, discussion of such bilateral transactions is not undertaken here.

35. The bank or finance company would be free to sue the consumer rather than the merchant. Absent waiver of defense clauses, however, the bank would be subject to any defenses that could be raised against the merchant, and a suit against the consumer would be unlikely unless the merchant was insolvent or otherwise unavailable.
B. Allocating Unremedied Losses

Obviously, the elimination of waiver of defense clauses would greatly benefit the consumer, but what about the bank? Shifting a loss from one innocent party to another is socially beneficial in at least two general situations: (1) where the party upon whom the loss is placed is better able to bear its consequences through spreading\(^\text{36}\) and (2) where the party upon whom the loss is placed is better able to deter such costs from arising in the future.\(^\text{37}\) In the context of consumer transactions, banks and other financiers are invariably better able than individual consumers to spread losses among a large number of people.\(^\text{38}\) Of equal importance is the fact that banks also fit the second criterion of cost allocation. They enjoy a comparative advantage both in obtaining effective relief from losses, and, in many instances, in preventing their occurrence in the future.

When a credit card merchant presents a sales slip to the bank, its account is credited with the face value of the instrument less a small discount to cover administrative costs. If the cardholder later refuses to pay the bank because of some defect in the merchant’s performance, the bank can either absorb the loss or recover the money credited to the merchant. Banks and consumers differ substantially, however, in the amount of leverage they can exercise against merchants. Among the devices available to the banks are the recourse agreement, the right to set off losses against a merchant’s account, control over a merchant’s credit rating, and the ability to screen insolvent and dishonest merchants out of the credit card system.

Merchant agreements used by credit card banks invariably include recourse provisions, under which the merchant is obligated to repurchase any credit card sales slip the payment of which is disputed by a cardholder on the basis of defects in the underlying sale.\(^\text{39}\) By itself,

\(^{36}\) Such interpersonal loss spreading has two advantages: (1) the taking of a large sum of money from one person is more likely to lead to costly economic dislocations than the taking of a series of small sums from many people, and (2) even if total dislocations are not reduced by spreading, many small losses are preferable to one large one because people may feel less pain if many lose one dollar instead of one losing many dollars. G. CALABRESI, THE COST OF ACCIDENTS \(39\) (1970). In the case under discussion, the losses imposed on the bank could be spread among the many users of credit cards; many small losses would replace relatively fewer larger losses.

\(^{37}\) In Calabresi’s terminology, this is the search for the cheapest cost avoider. Id. at 136-73.

\(^{38}\) In addition to interpersonal loss spreading, banks are better able to obtain intertemporal spreading by means of insurance. While insurance is theoretically available to individual consumers, it is reasonable to assume that it would be more expensive to consumers, if for no other reason than that their loss experience is more limited. Id. at 251-53.

\(^{39}\) See p. 292 and note 20 supra.
a recourse agreement is not substantially more effective against a recalcitrant merchant than a consumer's cause of action for breach of contract or fraud. If banks were compelled to sue merchants to obtain compliance with the terms of a recourse agreement, litigation costs would present a real barrier to effective relief. Banks, however, are rarely forced to sue.

First, the ongoing relationship between a credit card bank and its merchants permits the bank to quickly and easily remedy losses by setting off disputed amounts against any balance the merchant has in his checking account or against sales slips which the merchant presents. Credit card merchants are required to maintain an account with their bank, into which they deposit sales slips. Any balances retained in such accounts are subject to set-off.

Even if the merchant maintains an insufficient balance in his account, credit card merchants usually hold one or two days' worth of sales slips that they have not yet presented to the bank for payment. These represent a debt owed to the merchant by the bank. Should a merchant balk at repurchasing a contested sales slip, the bank can obtain immediate relief by setting off the disputed amount against any sales slips the merchant may attempt to present.

While the ability to set off disputed amounts is an extremely simple and effective remedy, it is not the only weapon available to the bank. Unlike consumers, banks enjoy considerable leverage over merchants through their ability to affect adversely a merchant's credit rating. Rather than risk impairment of his access to continued financing, a merchant who expects to remain in business very long will rarely refuse to repurchase a disputed obligation.

The bank's leverage may fail to provide relief in the event of merchant insolvency. While banks can use their debtor position to set off sales slips which cardholders refuse to pay prior to the time the merchant goes out of business, losses which arise from consumer defenses raised subsequent to insolvency are bound to go unremedied.

Even here, however, banks can minimize unremedied loss resulting from insolvency by refusing to deal with high-risk merchants. And,

40. Of course the barrier might not be as high as that faced by consumers if banks retain house counsel and hence have smaller costs in pursuing particular claims. Since this seems probable, even a system which allocated the initial loss on banks and forced them to sue merchants would be somewhat superior to one which left to consumers the burden of commencing a lawsuit. See note 49 infra.

41. While the discussion in the text assumes a single bank, tripartite model, it would be equally applicable to two bank, quadripartite transactions.

unlike consumers, banks need not rely on external appearances as the sole indicia of a merchant's financial stability. They not only have access to a merchant's financial records, but they possess expertise and experience in evaluating them. Banks continually use credit information, balance sheets and other financial data to make solvency predictions in connection with direct loans. Placing the risk of merchant insolvency on banks by a prohibition of waiver of defense clauses would encourage them to use the same care in screening merchants for credit card plans as they now use in selecting borrowers.

While banks are generally not in the business of evaluating merchant conduct, they are not completely helpless in screening dishonest merchants out of their credit card systems. Each credit card bank has many local cardholders who deal with its merchants on a daily basis. As a result, knowledge of a merchant's fraudulent or irresponsible practices will quickly be brought to the bank's attention by cardholder complaints.

By employing their potential leverage, banks possess the ability to minimize the two primary sources of unremedied losses in consumer transactions: litigation costs and merchant insolvency. For this reason, shifting the risk of loss to banks should serve to substantially reduce the extent of unremedied loss. The undesirable effects of any unremedied losses that did arise would be minimized because losses would be imposed on the party best able to spread their effects.

IV. The Problem of Overreaching by Consumers

The elimination of waiver of defense clauses clearly would minimize the incidence and effect of litigation costs and merchant insolvency as sources of unremedied consumer losses. It remains to be seen, however, whether abolition would also permit unscrupulous cardholders

43. See p. 291 supra.
44. For example, it is inconceivable that the United California Bank would have given Filter Queen an unsecured loan of $23,000 in view of the merchant's undercapitalized financial structure. But the bank evidently did not have the same qualms about signing up Filter Queen as a member of its credit card plan and, in effect, loaning Filter Queen $23,000 of its cardholders' funds. Credit card banks assert that they carefully evaluate merchants for purposes of determining their honesty and reputation in the community. Credit Card Hearings, supra note 19, at 184. Thus, there would be little additional cost involved in assessing the merchant's financial condition as well.
45. In spite of their access to information regarding merchant practices, the present allocation of the risk of loss gives banks little incentive, other than cardholder goodwill, to make use of it. For an example of an issuer's failure to get rid of even notoriously fraudulent merchants because they were "good customers," see Credit Card Hearings, supra note 19, at 209.
to raise so many unfounded claims that a significant new source of unremedied losses would enter into the system.

If a bank exercises recourse against a merchant on the basis of an unjustified cardholder claim, a loss will be imposed on the merchant analogous to that incurred by a defrauded consumer. Like the defrauded consumer, the innocent merchant may be confronted with two barriers to effective relief—consumer insolvency and litigation costs. Unlike the situation imposed on consumers by waiver of defense clauses, however, these barriers to relief for the merchant are relatively slight.

Consumer insolvency may present less of an obstacle to recovery by a merchant against whom recourse was unjustly exercised. Banks already engage in some screening of potential cardholders to insure that they represent good credit risks. Because a system which abolished waiver of defense clauses in credit card transactions would create an incentive for banks to conduct this screening with care, merchants would be largely protected by the banks' self-interest in avoiding judgment-proof defendants.

Merchants are similarly protected against litigation costs as a source of unremedied loss by the costs of collection clauses that are incorporated in credit card agreements. Besides protecting the merchant, these clauses serve as an important check on the assertion of fictitious claims by consumers. By compelling a bank to exercise recourse on the basis of an unfounded claim, a cardholder runs a very real risk that the merchant will sue him and collect the purchase price along with damages and attorney's fees as well. A further deterrent to frivolous claims is the power of an issuer bank to revoke a litigious cardholder's credit card.

Threats of revocation and the prospect of having to pay collection costs may not completely eliminate unmeritorious refusals to pay on

46. See, e.g., Credit Card Hearings, supra note 19, at 53.
47. Under the present system, it is not in a bank's self-interest to so police merchants. Since payment to the bank by the consumer is virtually guaranteed by waiver of defense clauses, banks can collect on credit card sales even when the merchant goes bankrupt.
48. See note 21 supra.
49. The system proposed would thus put the burden of commencing litigation on the party for whom that course of action is cheapest. For a description of merchant efficiency in the collection process, see Leff, Injury, Ignorance and Spite—The Dynamics of Coercive Collection, 80 YALE L.J. 1, 22-24 (1970). The strictly economic analysis here necessarily overlooks Leff's identification of malevolence as an operative factor in any collection system.
50. Frivolous claims could also be deterred if banks required the payment of a service charge by cardholders who assert defenses. See p. 303 infra.
the part of consumers. And, since courts are not infallible, some merchants will be faced with a source of unremedied loss which they did not face under the waiver of defense system. But slippage of this kind is inevitable in any remedial scheme. Unless consumers are more apt to raise unmeritorious defenses than merchants are to reject legitimate claims, abolition of waiver of defense clauses will not increase the frequency with which this kind of loss occurs.51

V. The Four-Party Model

The majority of bank credit card transactions involve two banks, one which issued the credit card and another with whom the merchant deposits sales slips from credit card sales. The presence of the additional bank somewhat alters the operational model outlined above,52 but the superior ability of banks to avoid and remedy losses in the credit card system remains. In quadripartite transactions the exercise of recourse involves one additional step, as the issuer bank must first charge the disputed amount against the depository bank, which, in turn, looks to the merchant for its remedy. In both the tripartite and quadripartite models, the bank which has dealt with a merchant would bear the risk of loss in the event of his insolvency.53 Thus, a credit card bank need only be concerned about the solvency of the merchants with whom it has directly dealt, not with those who have another depository bank.

In the absence of waiver of defense clauses, merchant-consumer disputes in the four-party situation would most likely be resolved in something like the following manner. Upon discovery of a defect or other non-conformity in the goods he had purchased, a cardholder would first turn to the merchant and seek a refund or cure. Aware of the consumer's leverage inherent in the right to refuse to pay the bank, the merchant will have a considerable incentive to settle all

51. In this context, see Credit Card Hearings, supra note 19, at 209-10, where the general counsel of Diners' Club replied to the question, "As between the cardholder and your customer merchant, who would get the benefit of the doubt?" by stating:

I would always lean to the cardholder. And that is based on experience, because I find that most cardholders are honest. It is very rare that I can recall in the 20 years or so where I have found that a cardholder concocted a story or did not tell the truth ....

52. The operational characteristics of the four-party model are set out in Brandel & Leonard, supra note 14, at 1035-36.

53. There has been a good deal of confusion on the part of commentators with regard to this point. See Bergsten, supra note 10, at 516, and Brandel & Leonard, supra note 14, at 1052-53. In both of these articles, much is made about the impossibility of an issuer bank evaluating the solvency or business practices of a merchant located three thousand miles away.
legitimate complaints. If the cardholder is unable to obtain satisfaction from the merchant, however, and if the cardholder remains convinced of the validity of his claims, he will bring the dispute to the attention of his bank, the issuer.\footnote{54}

Depending on the issuer's geographic proximity to the merchant and the amount involved, it may attempt to mediate the dispute in the interest of preserving the good will of both parties. While the depository bank may also become involved in the effort to mediate, the role that either bank can play is not without limits. Beyond a phone call or two, there is not much the banks can do to compel a settlement.\footnote{55} If the effort at mediation is unsuccessful and the cardholder remains adamant in his refusal to pay, the banks will have little choice but to exercise recourse against the merchant.\footnote{56}

If the merchant is, in fact, guilty of refusal to correct a legitimate consumer grievance, the system will have simply and quickly extinguished what would otherwise have been an unremedied loss. In those situations where the merchant believes that the cardholder's refusal to pay was unjustified, he is free to sue the cardholder, protected by a costs of collection clause.

VI. Limitation on the Right to Assert Claims or Defenses

Credit card transactions typically differ from installment sales in at least two respects. First, credit cards are often used to finance relatively small sales. Second, they frequently are used in geographic locations far from the consumer's home. Both of these differences have been noted by commentators, either to support the continued enforcement of waiver of defense clauses or to argue that limitations on a cardholder's right to assert defenses would have to be imposed, should waiver clauses be abolished.\footnote{57} Some of these limitations have already begun to appear in statutes.\footnote{58}

\footnote{54} Some credit card issuers find involvement in the messy details of merchant-consumer disputes an anathema. See Credit Card Hearings, supra note 19, at 162-83. Others explicitly recognize that they are involved in the business of selling services, and that settling disputes is part of that business. Id. at 109-10, 141-42.

\footnote{55} In this situation the only real leverage possessed by the banks is their power to cut off their relationship with an intransigent cardholder or merchant.

\footnote{56} If the merchant and cardholder are both customers of the same bank, the bank may decide to absorb the loss, itself, in order to preserve the good will of both parties. See Credit Card Hearings, supra note 19, at 110, 185, 203. Of course, suit could be brought against the consumer, but banks would then be subject to normal defenses.

\footnote{57} See, e.g., Brandel & Leonard, supra note 14, at 1059-71.

\footnote{58} See, e.g., ch. 1019, § 4 [1971] Cal. Acts 2152, 2154 (adding Cal. Civ. Code § 1747.90(a)), which contains most of the restrictions sought by bankers:

(a) The right of a card issuer to recover any credit extended through use by the cardholder of a credit card in making purchases from a retailer shall be subject to
A. Monetary Limitations

The success of credit cards has been due in part to their ability to process a large volume of transactions at an extremely low cost through the use of automatic data processing equipment. Credit card issuers are able to spread the expense of a credit investigation and of maintaining a repayment schedule over a large number of consumer purchases. As a result of such reduced transaction costs, it has been possible for credit card issuers to extend credit on very small sales.

In view of this, it has been argued that, absent a monetary limitation on the right of cardholders to assert defenses, the administrative expense which banks would incur as a result of controversies over minor amounts would destroy the utility of credit cards. It has been proposed that the right of cardholders to assert defenses against payment to credit card issuers should be limited to transactions involving amounts greater than $50.

Even assuming that the transactions costs associated with the operation of the recourse mechanism would impose some financial burden on credit card banks, imposition of a $50 minimum would be an irrational response. Since the average amount charged on credit card sales is approximately $20, limiting the right to assert defenses to claims of $50 or more would arbitrarily deny relief from consumer losses in the overwhelming majority of credit card transactions. One of the primary reasons for eliminating the use of waiver of defense clauses in the first place was to provide an effective remedy for smaller claims, which invariably go unremedied under the present system because of the expense of hiring an attorney.

the defenses which the cardholder has as a buyer against the retailer from whom the cardholder made the purchases if:

1. The purchase price of the item as to which a defense is asserted exceeds fifty dollars ($50).
2. The purchase was made within this state.
3. The cardholder shall have made a written demand on the retailer with respect to the purchase and attempted in good faith to obtain reasonable satisfaction from the retailer.
4. The cardholder gives written notice to the card issuer specifying the retailer, date of purchase, amount thereof, the goods or services purchased, the nature of the cardholder's defense with respect thereto, and those acts, if any, that the cardholder has taken in attempting to obtain satisfaction from the retailer.

Other portions of the statute are set out at note 80 infra.

61. See Brandel & Leonard, supra note 14, at 1062. The California statute adopts such a restriction, limiting claims to those of $50 or more. See note 58 supra.
62. See note 32 supra.
63. Brandel and Leonard assert that small credit card transactions are analogous to cash purchases and that denying cardholders the right to assert defenses arising out of
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A more rational response would be for banks to charge those cardholders who raise defenses a fee or service charge to cover the operational costs of processing their claims. This charge, which could hardly exceed a few dollars, would be analogous to that imposed by banks when payment is stopped on a check. It would avoid any transactions cost effect which might impair the general efficiency of credit cards, without arbitrarily restricting the vindication of relatively small claims.

B. Geographic Limitations

Credit cards issued by banks associated with one of the major interchange systems are honored by merchants throughout the country. As a result, many credit card transactions involve merchants and cardholders who are separated by hundreds or thousands of miles. In transactions in which such geographic dispersion exists, special problems may arise. Most significant is that merchant-consumer discussion and settlement of disputes becomes very difficult.

In the eyes of merchants, the utility of credit cards may be diminished by the prospect of distant cardholders compelling banks to exercise recourse on the basis of unmeritorious claims. If a New York cardholder unjustly forces recourse against a California merchant, for example, the latter faces the burden of collecting money from a buyer 3,000 miles away. While the merchant would enjoy the financial protection of a costs of collection agreement, he would still be required to invest a good deal of time and money in the effort. In the case of small purchases, such considerations might dissuade merchants from honoring out-of-state credit cards.

In response to this problem, a variety of geographic limitations on the right of cardholders to assert defenses have been suggested. One would limit the right to pure tripartite transactions, those in which such transactions is justified because a consumer would not have been able to assert a defense if he had paid for the goods in cash. Brandel & Leonard, supra note 14, at 1050-51. The same writers advance a similar argument based on an analogy to personal checks. Id. at 1050-51.

Each of these arguments is a throwback to the "pigeonhole" analysis which has plagued the legal literature on this subject for so long. See note 14 supra. Analysis should focus instead on the practical issue of whether permitting cardholders to assert defenses arising out of small claims would reduce the incidence and extent of unremedied loss.

To avoid reform because of "administrative cost" is economically irrational here. Under the present system, the total unremedied loss, a real cost in itself, is borne by the consumer. Even if the proposed system involved added administrative costs, it would be preferable to allow the cardholder to pay those costs directly, rather than allowing such "transactions costs" to bar relief altogether.

Cf. U.C.C. § 4-403 and Official Comment 2.
both the merchant and the cardholder had dealt with the same bank.\textsuperscript{66} The Arizona and California credit card statutes limit the right to raise defenses to transactions made within the state.\textsuperscript{67} Other proposals would allow defenses to be raised only when the merchant and cardholder's residence are within a specified distance of one another.\textsuperscript{68}

Each of these suggested limitations is both arbitrary and unresponsive to the underlying problem. Limiting the right to assert defenses to cases in which only a single bank is involved would deny relief for losses arising from the majority of credit card transactions which occur in metropolitan areas. Almost every large city has at least two credit card banks which are associated with the same interchange system. It would be irrational to condition effective relief for consumer losses on the fortuity of a particular merchant and a particular cardholder banking at the same place.

The use of state boundaries as a limitation on the right to assert defenses could be equally arbitrary. In California, where such a limitation has been adopted,\textsuperscript{69} a cardholder living in Crescent City, California, is now permitted to assert defenses based on purchases made in Los Angeles or San Diego, 800-900 miles away, but is denied the right for those made across the border in Oregon, less than fifty miles away.

Limitations based on specific distances would not produce quite such anomalous results. If a reasonably large radius were selected, consumers would enjoy, for most of their purchases, the protection afforded by the right to assert defenses against the issuer bank. But administration of such a rule would be far from simple, especially

\textsuperscript{66} See Bergsten, supra note 10, at 516. The Massachusetts statute preserving the right to assert defenses arising out of credit card transactions apparently imposes such a limitation. It states that a credit card issuer will be subject to consumer defenses where "the creditor was the issuer of a credit card which may be used by the consumer in the sale or lease transaction as a result of a prior agreement between the issuer and the seller or lessor." \textsc{Mass. Ann. Laws} ch. \textsc{255}, \textsection\textsc{12F} (Supp. 1971). Literally interpreted, such a situation exists only in pure tripartite transactions. The only time the "issuer," in any given transaction, has a prior agreement with the merchant is where the "issuer" also happens to be the "depository bank."

Aside from the other objections mentioned in the text, limiting the right to assert defenses to tripartite transactions would arbitrarily discriminate against travel and entertainment credit card issuers, such as Diners' Club and American Express, which operate solely on a tripartite model. It would subject them to defenses arising out of international transactions, while in some cases, insulating banks from defenses based on sales made across the street.

\textsuperscript{67} \textsc{Ariz. Rev. Stat. Ann.} \textsection\textsc{44-145(B)(2)} (Supp. 1971); \textsc{ch. 1019, \textsection\textsc{4}} [1971] \textsc{Cal. Acts 2152, 2154} (adding \textsc{Cal. Civ. Code} \textsection\textsc{1747.90(a)(2)}).

\textsuperscript{68} See Brandel & Leonard, supra note 14, at 1063-68.

\textsuperscript{69} See note 67 supra.
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with respect to purchases made at the margin of the circle surrounding a cardholder's residence.\textsuperscript{70}

Rather than condition a cardholder's right to assert defenses on arbitrary boundaries such as these, it might be more rational to require that the cardholder show that he had returned the disputed goods to the merchant, where possible,\textsuperscript{71} and had made a good faith effort at settlement.\textsuperscript{72} Such a rule would ensure merchant-consumer discussion and preserve the possibility of compromise,\textsuperscript{73} without unnecessarily limiting the availability of relief for consumer losses. In effect, the requirement that cardholders return unsatisfactory merchandise and communicate regarding alleged defects would constitute a geographic limitation on a sliding scale. Consumers' willingness to incur shipping costs and other expenses entailed by a good faith effort at settlement would be proportional to the size of the loss that would otherwise go unremedied. This solution would tend to cut off relief in cases where the costs of negotiation are high and where the consumer does not anticipate success. But these factors already operate to cut off relief. Since the costs which arise as a result of geography are virtually irreducible except by reducing the number of transactions between remote parties, the consumer becomes the party best able to reduce the extent of unremedied losses. Those consumers who do not wish to incur the risk of loss arising from such transactions could simply refrain from using their cards when far from home. To place these losses on merchants or banks would probably result

\textsuperscript{70} Because the purpose of a geographic limitation is to assure the possibility of merchant-consumer discussion the distance should ideally be calculated from the cardholder's residence rather than the location of the issuer bank. However, since cardholders often reside at some distance from their credit card bank, the administrative problems associated with a fixed distance limitation are staggering. For example, an issuer with 1000 cardholders would have to contend with 1000 separate radii which would change every time a cardholder moved.

\textsuperscript{71} Of course, a geographic limit centered on the bank's location would avoid such dilemmas. But because of the typical dispersal of cardholders, this limitation might prove as arbitrary as those discussed above.

\textsuperscript{72} A cardholder himself ought not to be required to return items such as stoves or refrigerators, at least in cases where the merchant had originally delivered the appliance to the cardholder's home. In such cases, the requirement of returning the goods would be satisfied by the cardholder giving notice to the merchant and permitting the latter to inspect the defective goods.

\textsuperscript{73} While both the Arizona and California credit card statutes require that written notice of alleged defects be sent to both the merchant and the issuer, the California statute expressly requires that the cardholder attempt "in good faith to obtain reasonable satisfaction from the retailer." Ch. 1019, § 4 [1971] Cal. Acts 2152, 2154 (adding Cal. Civ. Code § 1747.90(e)(3)).

\textsuperscript{73} From the merchant's point of view this is an important protection because it gives him notice of disputes at a time when he can still do something about settling them. See Credit Card Hearings, supra note 19, at 86-87.
in a severe restriction on the utility of credit cards to out of state residents. This would disadvantage those cardholders who might use their credit cards out of state without incident, and those who would prefer to assume the risk of unremedied loss.

C. Limitations on the Extent of Recovery

The Uniform Consumer Credit Code and many of the recently enacted state statutes prohibiting the use of waiver of defense clauses in installment sales contracts limit the right to assert defenses to the amount owed on the purchase in question at the time the defense is raised. This limitation has been incorporated into both the Arizona and California credit card statutes.

Such a rule serves an important objective: it provides a measure of finality in transactions, and reasonably limits a bank's potential liability at any particular point in time. Even assuming the propriety of abolishing waiver of defense clauses, some limit to a bank's exposure is needed. Moreover, the rule puts the credit cardholder in a position analogous to that of other customers exercising a right of set-off, by approximating their ability to withhold only amounts equal to the amount owing on the defective goods.

Limiting the ability to raise defenses to the amount still owed on a particular purchase penalizes those who promptly pay their bills, a category that includes many cardholders. Moreover, such a rule may involve administrative difficulties. Most credit card plans give cardholders a thirty to sixty day period after billing in which to make payments without incurring interest charges. Obligations not met

74. U.C.C.C. § 2.404 (Official Text).
75. See, e.g., N.Y. PERS. PROP. LAW § 408(6) (McKinney Supp. 1971);
   The assignee of a retail installment contract or obligation shall be subject to all claims and defenses of the buyer against the seller arising from the sale notwithstanding any agreement to the contrary, but the assignee's liability under this subdivision shall not exceed the amount owing to the assignee at the time the claim or defense is asserted against the assignee.
   See also CAL. CIV. CODE § 1804.2 (West Supp. 1971).
76. ARIZ. REV. STAT. ANN. § 44-145(A) (Supp. 1971); ch. 1019, § 4 [1971] Cal. Acts 2152, 2154 (adding CAL. CIV. CODE § 1747.90(0)).
77. A bank's potential loss on any credit card transaction is already limited to the amount of the original purchase price plus service or interest charges. See, e.g., First Acceptance Corp. v. Kennedy, 95 F. Supp. 861 (N.D. Iowa 1951), rev'd on other grounds, 194 F.2d 819 (8th Cir. 1952); McGraw Edison Co. v. Haverluk, 130 N.W.2d 616 (N.D. 1964). Absent collusion between a bank and merchant, this limitation is both just and necessary. If banks were liable for personal injuries caused by defective products, they would be forced to abandon the field of consumer financing.
79. Strictly speaking, the "grace period" itself is generally twenty-five days after billing. But the effective period for interest free payment must also include the interval

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within this grace period are consolidated into a single revolving loan. If consumer defenses are to be limited to amounts owed at the time the defenses are raised, it becomes necessary to allocate later installment payments and merchandise credits among a series of purchases and interest charges.80

Another method of achieving a similar limitation on claims would be to place an explicit time limit on the cardholder's ability to raise defenses.81 Such a limit could take a number of forms. One possibility would be to have a pure period of limitation for raising consumer claims—for example, thirty or sixty days after the purchase. A second alternative would be to entertain only those claims raised at the first payment date after the defect is discovered. The pure time limit has the advantage of providing certainty as to liability on the part of the bank, while the second alternative would be a superior protection of consumer claims. Although it is difficult to recommend either of these varieties of time limitation without further study, this approach to limiting the extent of recovery might well entail lower administrative costs than a rule geared to the amounts still owed on the purchase giving rise to the consumer complaint.

VII. Conclusion

The abolition of waiver of defense clauses in bank credit card transactions is desirable on several counts. Not only would abolition decrease the incidence of unremedied consumer loss, but those losses that

between the date of purchase and the billing, which, with monthly billing, should average fifteen days. C.f. Credit Card Hearings, supra note 19, at 50-51.


The amount with respect to which a defense may be asserted under this section shall not exceed the amount outstanding with respect to the purchase involved, and any late charges or finance charges on such amount, determined as of the time the retailer receives the written demand required from the cardholder pursuant to paragraph (3) of subdivision (a) or the card issuer receives the written notice from the cardholder pursuant to paragraph (4) of subdivision (a), whichever is received first. For the purpose of determining the amount outstanding, the payments and credits to the cardholder's account are deemed to have been applied, in the order indicated, to the payment of:

(1) Late charges in the order of their entry to the account.
(2) Finance charges in order of their entry to the account.
(3) Debits to the account other than those set forth above, in the order in which each debit entry to the account was made.


The analogous time limit in the Uniform Consumer Credit Code is three months, U.C.C.C. § 2.404 (Alt.B.), although some of the states which have adopted the code have substituted shorter periods. See, e.g., Ind. Stat. Ann. § 19-22-13-1 (Burns Supp. 1971) (60 days).
did occur would be placed on the institutions best able to spread them. This Note suggests that these results could be achieved at little real cost to credit card banks.

This Note has suggested only tentatively how credit card systems would operate in the absence of waiver of defense clauses. Much remains to be further explored, particularly with respect to geographic and monetary limitations on the right of recovery. Because both factual and policy questions exist, legislative study of the problem is clearly needed. While abolition of waiver of defense clauses has heretofore been limited to state statutes, the nationwide use of bank credit cards suggests that federal legislation may be preferable. In the absence of legislative reform, courts can, as was done in the installment contract area, declare waiver of defense clauses invalid as contrary to public policy. By whatever means, however, abolition of waiver of defense clauses in bank credit card transactions seems clearly warranted.