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The Amendments to the Truth in Lending Act 1974

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COMMENT

The 1974 Amendments to the Truth in Lending Act

Congress enacted the Truth in Lending Act in 1968 to provide a mechanism for control of the credit industry by requiring disclosure of information that would allow consumers to "credit shop." Ambiguities and conflicts in the basic application of the Act were soon illustrated. Both the courts in civil liability cases and the Federal Reserve Board in its overall administration of the Act immediately recognized various problems and these difficulties called for remedial legislation. In the fall of 1974, Congress finally amended various provisions of the Act.[1] Although labeled as "minor technical changes"[2] by members of Congress, the amendments will significantly affect substantive rights. This comment will explore these alterations and will attempt to assess their potential impact. In addition, this study will probe key problems to evaluate continuing shortcomings of the Act and to determine possible future developments in consumer credit disclosure legislation.

I. BACKGROUND

The Truth in Lending experiment began with the express purpose of assuring a "meaningful disclosure of credit terms" to enable consumers to compare credit prices and to avoid the uninformed use of credit.[3] Reluctant to insert a vast new bureaucracy into the credit area, Congress opted for "disclosure regulation" rather than rate regulation and established a wide range of enforcement devices including "multi-agency" administrative enforcement, Federal Reserve Board (FRB) rules and regulations, criminal penalties and private civil enforcement.[4] Immediate developments pushed Truth in Lending far beyond its initial purpose. For example, the FRB, rather than "filling in" the statutory framework, adopted a series of complex regulations, many of which conflicted with or clearly exceeded statutory authority. Furthermore,

1. The Truth in Lending Act is Title I of the Consumer Credit Protection Act, 15 U.S.C. §§ 1601 et seq. (1970). The 1974 amendments are Title IV of the Federal Deposit Insurance Corporation Act, 88 Stat. 1500 (codified in scattered sections of 15 U.S.C.A.).

2. 120 CONG. REC. H10,277 (daily ed. Oct. 9, 1974) (remarks of Rep. St. Germain).

3. 15 U.S.C. § 1601 (1970). *See also* Wachtel v. West, 476 F.2d 1062, 1064 (6th Cir.), *cert. denied*, 414 U.S. 874 (1973) (Douglas, J., dissenting).

4. 15 U.S.C. §§ 1604 (Regulations), 1607 (Administrative enforcement), 1611 (Criminal liability), 1640 (Civil penalties), 1635 (Right of rescission) (1970).

various states adopted independent disclosure requirements in the form of truth in lending acts,[5] the Retail Installment Sales Act,[6] the Uniform Consumer Credit Code,[7] and other legislative guidelines.[8] Although the FRB may exempt states with their own disclosure plans from Truth in Lending requirements,[9] exemptions had been given to only five states by the end of 1973.[10] As a result, the precise interaction between the federal regulatory provisions and those of the states is unclear.[11]

In addition to developments on the legislative front, debtors filed Truth in Lending civil actions in a flurry of activity unprecedented in many districts.[12] The attitude of courts that gave a "liberal interpretation" to the obviously remedial enactment often spurred such litigation.[13] In many cases this meant that the court would construe any ambiguity in the statute in favor of the consumer and against the creditor. Also, these cases carried the congressional desire to create "private attorneys general"[14] to a *reductio* as consumers who had never paid a finance charge recovered penalty damages.[15] Courts assessed punitive damages for such conduct as failure to include a one dollar notary fee in the itemized finance charge,[16] and one tribunal imposed liability

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5. ME. REV. STAT. ANN. tit. 9A, §§ 2.201-6.415 (Supp. 1974); MASS. ANN. LAWS ch. 140C (Supp. 1974).

Both states have adopted versions of the Federal Truth in Lending Act. The Massachusetts provisions preceded the Federal Act and formed the basis for many of the federal provisions.

6. *See, e.g.*, OHIO REV. CODE ANN. § 1317.11 (Page 1962) which regulates revolving credit accounts via the Ohio Retail Installment Sales Act.

7. UNIFORM CONSUMER CREDIT CODE (1968). The UCCC has been adopted by five states: COLO. REV. STAT. ANN. §§ 5-1-101 et seq. (1973); IDAHO CODE §§ 28-31-101 et seq. (Supp. 1974); IND. ANN. STAT. §§ 24-4.5-1-101 et seq. (Burns 1974); OKLA. STAT. ANN. tit. 14A, §§ 1-101 et seq. (1972); and WYO. STAT. ANN. §§ 40-1-101 et seq. (Supp. 1973).

8. KANSAS STAT. ANN. §§ 16a-1-101 et seq. (1974).

9. 15 U.S.C. § 1610 (1970).

10. Maine, Massachusetts, Connecticut, Oklahoma and Wyoming. *See* FRB, ANNUAL REPORT TO CONGRESS ON TRUTH IN LENDING 4-5 (1973) [hereinafter cited as FRB, 1973 ANNUAL REPORT].

11. 15 U.S.C. § 1610 (1970) establishes the basic guidelines but their effect is somewhat confusing. *See* remarks of Sen. Tower in S. REP. No. 278, 93d Cong., 1st Sess. 45-46 (1973).

12. Mullinax v. Willett-Lincoln Mercury, Inc., 381 F. Supp. 422 (N.D. Ga. 1974). The docket in this district is so crowded that Truth in Lending cases are being referred to bankruptcy referees.

13. Ratner v. Chemical Bank New York Trust Co., 329 F. Supp. 270 (S.D.N.Y. 1971).

14. Sosa v. Fite, 498 F.2d 114, 121 (5th Cir. 1974).

15. *See* Ratner v. Chemical Bank New York Trust Co., 329 F. Supp. 270 (S.D. N.Y. 1971).

16. Buford v. American Fin. Co., 333 F. Supp. 1243 (N.D. Ga. 1971).

when the creditor had complied in good faith with an FRB Letter Opinion later found invalid.[17] In addition, the statutory provision that authorized the recovery of attorneys' fees probably spawned many cases.[18]

In the midst of these developments, courts very narrowly construed the statutory defenses given to creditors in the original Act. In the *Ratner* case[19] the court held that the "bona fide error" defense was available only for clerical errors. The case was subsequently followed by a majority of courts[20] despite a paucity of congressional history on the intent of the draftsmen of section 130(c), the conflicting views on the proper scope of the section that can be found in the case law and commentary, and the shortcomings of Judge Frankel's analysis.[21] As

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17. Ratner v. Chemical Bank New York Trust Co., 329 F. Supp. 270, 277-79 (S.D.N.Y. 1971).

18. 15 U.S.C. § 1630(a) (1970).

19. Ratner v. Chemical Bank New York Trust Co., 329 F. Supp. 270, 281-82 (S.D. N.Y. 1971).

20. The finding that the § 130(c) defense applies only to a creditor's clerical errors was followed in Haynes v. Logan Furniture Mart, Inc., 503 F.2d 1161 (7th Cir. 1974); Starks v. Orleans Motors, Inc., 372 F. Supp. 928 (E.D. La. 1974); Ives v. W.T. Grant Co., 4 CCH CONS. CR. GUIDE ¶ 98,526 (D. Conn. 1974); Palmer v. Wilson, 359 F. Supp. 1099 (N.D. Cal. 1973); Owens v. Modern Loan Co., 4 CCH CONS. CR. GUIDE ¶ 99,099 (W.D. Ky. 1972); Douglas v. Beneficial Fin. Co., 334 F. Supp. 1166 (D. Alas. 1971), *rev'd on other grounds*, 469 F.2d 453 (9th Cir. 1972); and Buford v. American Fin. Co., 333 F. Supp. 1243 (N.D. Ga. 1971).

However, a contrary result, that the § 130(c) defense is available for good faith attempts to comply with the Act, was reached in Hamilton v. G.A.C. Fin. Corp., 4 CCH CONS. CR. GUIDE ¶ 98,804 (N.D. Ga. 1974); McTerry v. Household Fin. Corp., 4 CCH CONS. CR. GUIDE ¶ 98,803 (N.D. Ga. 1974); Heard v. G.A.C. Fin. Corp., 4 CCH CONS. CR. GUIDE ¶ 98,802 (N.D. Ga. 1974); Jones v. Community Loan & Inv. Corp., 4 CCH CONS. CR. GUIDE ¶ 98,787 (N.D. Ga. 1974); Chittester v. LC-DF-F Employees, 384 F. Supp. 473 (W.D. Pa. 1974); Welmaker v. W.T. Grant Co., 365 F. Supp. 531 (N.D. Ga. 1972); Richardson v. Time Premium Co., 4 CCH CONS. CR. GUIDE ¶ 99,272 (S.D. Fla. 1971); and Thrift Funds, Inc. v. Jones, 259 So. 2d 587 (La. Ct. App. 1971), *aff'd*, 274 So. 2d 150, *cert. denied*, 414 U.S. 820 (1973).

While the 1974 amendments now provide a reliance defense for FRB rules, interpretations and regulations (new § 130(f), *see* discussion at text accompanying notes 115 to 119 *infra*) they have failed to resolve this basic conflict over the meaning of § 130 (c). While indications are that Congress has accepted the clerical error interpretation and that it rejected a general good faith compliance defense (*see* S. REP. No. 278, 93d Cong., 1st Sess. 44-46 (1973) (remarks of Sen. Tower)), the question, so very crucial to the statutory scheme, remains open to interpretation and the conflict continues.

21. Judge Frankel seemed to rest his conclusion (that the § 130(c) defense was available for clerical errors only) on four factors: First, his interpretation of the statutory language. Secondly, the fact that he could not perceive how a creditor could devise procedures to avoid legal errors of statutory interpretation. Thirdly, a letter of concern by banks, who worried about clerical or mathematical errors, and a letter by the Attorney General showing concern about the original liability provisions which required a "knowing violation." (*See Hearings on H.R. 11,602 Before the Subcomm. on Consumer Affairs of the House Comm. on Banking and Currency*, 90th Cong., 1st Sess., pt. 2, at 902-03 (1967)). Lastly, a desire to give a liberal interpretation or a pro consumer outlook to a remedial statute. While his analysis is appealing it fails to take into account at least four additional factors: First, that nowhere in the congressional history of Truth

a result of that decision, a creditor is almost strictly liable for any violation of the Act, no matter how technical; and in addition, he is subject to punitive damages. Perhaps the rationale for this position is that the best way to achieve Truth in Lending compliance is to make creditors "scared to death" of violations.[22] This rationale, however, is not well founded. Little is known about how creditors will respond to fears of liability.[23] It is likely that large creditors will translate their fears into higher interest rates or deny credit to higher risk customers, driving them into the "grey market."[24]

Thus the first major problem that Truth in Lending encountered was a "hodge-podge" random pattern of regulation perhaps inherent in the legislative premise itself: creation of a myriad of enforcement patterns, largely dependent on private rather than public initiative. For

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in Lending is there any direct discussion of the provisions of § 130(c) and the meaning attached to it. The only discussion is general and by inference relates to the good faith provisions of § 130(c). *See*, for example, the remarks of Sen. Moss, 113 CONG. REC. 18,420 (1967). Secondly, the statutory language is capable of two interpretations. "Bona fide error" need not mean "clerical error." A fair reading of it would infer that bona fide might mean REAL and include all kinds of errors so long as they were truly mistakes and not intentional subterfuges to mask genuine disclosures. Thirdly, the mind can easily generate procedures to avoid legal as well as clerical errors. Although not generally accepted in criminal law (the analogy which Judge Frankel used) they could include employment of legal counsel, careful drafting, continual review of disclosure forms, and requests for rulings on questionable matters from the FRB. Fourthly, the true intent of the draftsmen of this section is buried somewhere in the proceedings of the Conference Committee, for the language was altered in this Committee without explanation. The § 130(c) wording was identical in the original House and Senate versions of Truth in Lending. The Compromise Committee changed it, although there was apparently no basis for dispute. The original House version of the Act that became § 130 illustrates what is most likely the true intent of the draftsmen. Section 7(a)(1) of H.R. 11,602 stated:

> . . . [in] any action brought under this subsection [a knowing failure to disclose] in which it is shown that the creditor . . . failed to disclose information so required by the Act or regulations there shall be a rebuttable presumption that such violation was made knowingly. Such presumption shall be rebutted IF THE CREDITOR SHOWS BY A PREPONDERANCE OF THE EVIDENCE THAT THE VIOLATION WAS NOT INTENTIONAL AND RESULTED FROM BONA FIDE ERROR NOTWITHSTANDING THE MAINTENANCE OF PROCEDURES REASONABLY ADAPTED TO AVOID ANY SUCH ERROR.

H.R. 11,602, 90th Cong., 1st Sess. § 7(a)(2) (1967). The "knowing" failure requirement was dropped per request of the Attorney General but the emphasized language remained unchanged. Since it was obvious that it originally was not drawn to apply only to clerical errors, there is adequate evidence that it was meant to apply to failure to disclose any required information, and that Judge Frankel's clerical error limitation is erroneous.

22. 120 CONG. REC. H10,279 (daily ed. Oct. 9, 1974) (remarks of Rep. Sullivan).

23. However, the FRB has conducted some studies and has made a partial analysis. *See* notes 30-32 *infra*.

24. *See generally* Shay, *A Portrait of the Consumer Credit Market*, 26 BUS. LAW. 761, 766-70 (1971).

example, courts developed a very liberal and almost strict liability approach in individual actions while completely denying class actions. At a time when many public regulatory agencies are being criticized for lack of a unified direction, it is easy to see how "privately" controlled regulation can develop even greater inconsistencies.

In addition to the capricious pattern that developed through private litigation under the original Act, Congress itself occasionally altered the statutory scheme. The basic theory of the original Act was disclosure rather than rate regulation, at least for consumer credit. Proponents believed that consumers could effectively regulate the credit industry through supply and demand if they had a mechanism to evaluate real credit costs. Later amendments to the Act seemed to emphasize creditor conduct control rather than disclosure. In 1970 Congress passed the Fair Credit Reporting Act[25] to direct information-gathering activities, and amended Truth in Lending to regulate credit card practices. The current legislation continues this trend toward conduct regulation. It provides two more weapons for consumers: The Fair Credit Billing Act[26] and the Equal Credit Opportunity Act.[27] This legislation prevents specific abuses and is laudible. However, it continues a theory of governmental "non-regulation regulation"[28] despite the problems created by that theory.

II. TRUTH IN LENDING ACT CHANGES

A. Technical Changes

The 1974 amendments made minor changes in the "multi-agency" enforcement mechanism of the Act. Under this concept the Comptroller of the Currency, the Federal Reserve Board, the Federal Deposit Insurance System, the Federal Home Loan Bank Board (directly or through the Federal Savings and Loan Insurance Corporation), the Di-

25. 15 U.S.C. § 1681a-t (1970).

26. 15 U.S.C.A. § 1666 (Supp. I, 1975).

27. *Id.* § 1691.

28. The credit card provisions added to Truth in Lending in 1970 are examples of the development away from mere disclosure and toward regulation of conduct and redistribution of rights in the credit area. 15 U.S.C. §§ 132-34 (1974). Two proposals made by Sen. Proxmire in 1971 would have taken the last step in the evolutionary context by outlawing both minimum finance charges and certain methods of computing finance charges. This would have effectively imposed a federal usury statute upon credit retailers. *See* S. 652, 92d Cong., 1st Sess. (1971). The evolution from disclosure to rate regulation would have been complete. However, this suggestion was rejected in committee and a subsequent proposal to accomplish the same objectives was also rejected. *See* S. 914, 93d Cong., 1st Sess. (1973).

rector of the Bureau of Federal Credit Unions, the Interstate Commerce Commission, the Civil Aeronautics Board and the Secretary of Agriculture each supervise implementation of the Act in given areas, and the Federal Trade Commission assumes enforcement responsibility in all other areas. The Federal Reserve Board is responsible for development of a statutory scheme including issuance of regulations, formation of an advisory board and reports to Congress.[29] Originally the FRB was skeptical about the interrelation of so many diverse agencies, feeling that enforcement might suffer, but eventually concluded that the concept was working fairly well.[30] However, minor changes in the Act's structure were contemplated. Through an oversight, the Act initially failed to give the Farm Credit Administration the authority to compel compliance in federal land bank programs and one of the earliest proposals to amend the Truth in Lending Act favored extending enforcement power to this agency.[31] In addition, after promulgation of ICC regulations for contract carriers, it was discovered that there were no members subject to the Act and it was suggested that ICC enforcement be deleted.[32] Enactment presented little problem since each agency concurred and the proposals were included in the 1974 amendments.[33]

The second technical change made relates to exemptions from the disclosure requirements. Initially, the Act exempted four kinds of transactions: transactions for business, commercial, organizational, or governmental purposes; transactions by broker-dealers registered with the SEC; extensions of credit other than for real property, in which amounts involved exceeded 25,000 dollars; and purchases under state regulated public utility tariffs.[34] A proposal to repeal the public utility exemption failed to clear committee in both the Senate and the House.[35] However, an FRB recommendation to add agricultural credit to the list of exempt activity was adopted. The basic rationale for the

29. 15 U.S.C. § 1607 (1970) establishes the "multi-agency" concept of administrative responsibility under the Act. FRB basic responsibilities are outlined in this section as well as *id.* § 1604.

30. FRB, 1973 ANNUAL REPORT.

31. FRB, ANNUAL REPORT TO CONGRESS ON TRUTH IN LENDING 19 (1969).

32. FRB, ANNUAL REPORT TO CONGRESS ON TRUTH IN LENDING 20 (1972) [hereinafter cited as FRB, 1972 ANNUAL REPORT].

33. 15 U.S.C.A. § 1607(a)(4)-(6) (Supp. I, 1975), *amending* 15 U.S.C. § 1607 (a)(4)-(6) (1970).

34. 15 U.S.C. § 1603 (1970).

35. *See* S. 1406, 92d Cong., 1st Sess. (1971). This was largely because of various abuses attributable to certain states. *See* S. REP. No. 750, 92d Cong., 2d Sess. 30-31 (1972).

new exemption is that agriculture is considered to be a business rather than a consumer activity and that a need for this exemption was created by the uncertainty inherent in advances for agricultural credit. With a few exceptions, this amendment engendered little controversy.[36]

B. Disclosure Requirements

Changes that created more controversy than the technical requirements discussed above, and that impose a greater burden on individual creditors, deal with specific disclosure requirements. The first of these additions concerns the problem of spreading payment for a single sale of goods or services over a period of time. In theory, maintaining an inventory or credit accounts involves increased costs to sellers. Thus when a customer is given a period of time in which to repay sums owed to a seller, the use of money is deemed to include a finance charge. Whether the finance charge is added to an outstanding balance, or contained in the purchase price, the debtor has had the use of a value that belongs to the creditor. Therefore, to prevent evasion of Truth in Lending by creditors who might claim that they imposed no finance charges when in fact they included them in the purchase price of goods, the FRB promulgated its "four installment rule."[37] Any creditor who allows payment for goods or services in more than four installments is presumed to have charged a finance charge and is subject to the disclosure provisions of the Act. When a circuit court decision imperiled the validity of the rule,[38] the FRB requested congressional approval. However, in *Mourning v. Family Publications*[39] the validity of the rule was upheld and the recommendation was dropped.[40] Congress passed an amendment including the FRB recommendations despite the Su-

36. 15 U.S.C.A. § 1607(a)(4)-(6) (Supp. I, 1975), *amending* 15 U.S.C. § 1607 (a)(4)-(6) (1970).

37. 12 C.F.R. § 226.2(k) (1972) promulgated under authority of 15 U.S.C. § 1604 (1970).

> 12 C.F.R. § 226.2(k) "Consumer credit" means credit offered or extended to a natural person, in which the money, property, or service which is the subject of the transaction is primarily for personal, family, household, or agricultural purposes and for which either a finance charge is or may be imposed or which pursuant to an agreement, is or may be payable in more than four installments. "Consumer loan" is one type of "consumer credit."

38. Mourning v. Family Publications, 449 F.2d 235 (D.C. Cir. 1971).

39. 411 U.S. 356 (1973).

40. *See* S. 652, 92d Cong., 1st Sess. (1971) (including the four installment rule) and subsequent S. 2101, 93d Cong., 1st Sess. (1973) which included the four installment rule in the revised definition of "creditor." Note that S. 2101 formed the basis for amendment to H.R. 11,211, 93d Cong., 2d Sess. (1974) which was enacted as Pub. L. No. 93-495.

preme Court decision and the four installment rule is now codified.[41]

A second proposed disclosure requirement relates to the four installment rule and its relation to credit advertising. Initially, the Act, on the theory that advertisement of credit terms should be subject to similar disclosure requirements as actual extensions of credit, imposed disclosure requirements on merchants who offered credit plans in their advertisements. The four installment rule was not used in this area, however, and creditors who included finance charges in the price of goods were not required to comply with the advertising provisions of the Act. Various consumer groups believed that the rationale underlying the four installment rule should be extended to advertising,[42] and the National Commission on Consumer Finance recommended disdisclosure provisions for such advertising.[43] The FRB disagreed to some extent, stating that it doubted that customers were really concerned about it,[44] and this position was reflected in congressional consideration.[45] Despite doubts, the Act as amended requires that any advertisement in conjunction with an extension of credit that can be paid in more than four installments must disclose that a finance charge increment is included in the cost of goods. New section 146 specifically requires a legend in the advertisement: "THE COST OF CREDIT IS INCLUDED IN THE PRICE QUOTED FOR THE GOODS AND AND SERVICES."[46] It is indeed ironic that the FRB opposed this requirement, for it is a logical extension of its four installment rule. Little justification can logically be made for its use in sales transactions but not in credit advertising.[47] Ultimately, as in the basic rule, new section 146 will most likely serve as a trap for unwary creditors who

41. 15 U.S.C.A. § 1602(f) (Supp. I, 1975).

42. Already regulated by Chapter 3 of the Act.

43. NATIONAL COMMISSION ON CONSUMER FINANCE, CONSUMER CREDIT IN THE UNITED STATES (1972).

44. FRB, 1973 ANNUAL REPORT 28.

45. "If the merchandise is sold at competitive prices, why require that firm to make a statement that is not true?" (referring to the fact that there may be no hidden finance charge, but that the spreading of payments is done "to bring in business" and thus more than four installments may be the equivalent of a loss leader). *See* 120 CONG. REC. H10,279 (daily ed. Oct. 9, 1974) (remarks of Rep. Sullivan).

46. 15 U.S.C.A. § 1665(a) (Supp. I, 1975).

47. The *reductio* of the entire FRB position is that someone must pay for the use of money in any four installment transactions. Under Regulation Z § 226.2(k) all transactions involving payment in more than four installments involve a hidden finance charge which must be disclosed. Somehow there is a basic inconsistency in the theory of full disclosure for sales but not for advertising. It would seem that new § 146 is merely a natural extension of *Mourning*.

have no idea that their sales are subject to the provisions of Truth in Lending.[48]

A third area in which specific disclosure requirements have been altered by the 1974 legislation involves notation of closing costs in conjunction with credit disclosures required before the consummation of a transaction. To understand the significance of the new closing cost disclosure requirements an understanding of a few statutory relationships is needed. Chapter 1 of the Act contains general provisions, one of which defines "finance charge."[49] Chapter 2 outlines conduct requirements such as disclosures, civil liability and credit card regulation. Specifically, section 121 contains the general disclosure requirements.[50] The problem of closing cost disclosure arose because section 106 of the 1969 Act specifically excluded them from consideration as finance charges.[51] Thus, unless included in the principal amount, closing costs would never be disclosed under the general theory of Truth in Lending. The idea that closing cost disclosures should be required, either as an increment of the finance charge or as a separate item is somewhat of an extension of the original theory of the Act. This disclosure, however, increases the knowledge of a consumer who is trying to weigh the merits of an individual sales transaction, and certainly furthers the purposes of the Act.

Recognizing that unscrupulous lenders could reap advantages by concealing closing cost figures until after a contract was consummated and the downpayment received, the FRB recommended that these costs be disclosed. Basically, the FRB proposed to amend the general section relating to "exclusions" from real estate finance charges found in section 106(d) (which enumerated items generally considered to be closing costs) and suggested that under FRB regulations closing cost items for realty either be separately listed or included in the finance charge. The Board hinted that it would fix the proper time for making such disclosures as: a reasonable time before closing;[52] before any

48. Just as the basic four installment rule often serves as a trap for unwary sellers, particularly vendors of services, such as doctors and dentists. Any disagreements here are directed to the premise behind the four installment rule rather than its extension to credit advertising.

49. 15 U.S.C. § 1605 (1970).

50. *Id.* § 1631.

51. *Id.* § 1605(a).

52. FRB, 1972 ANNUAL REPORT 35. Recommended closing cost language:

§ 106(e) The following items, when charged in connection with any extension of credit secured by an interest in real property, and when itemized and disclosed in accordance with the regulations of the Board, shall not be included in the computation of the finance charge with respect to that transaction.

downpayment was required; or before the lender was committed to lend.[53] The National Commission on Consumer Finance (NCCF) suggested amendment of the section 121 general disclosure requirements as an alternative. This proposal would require closing cost information in *any* transaction, not limited to realty as in the FRB version, and would require the disclosures only *prior to consummation* of the transaction although this was specifically defined for realty transactions as the time that the lender became committed. As in existing FRB regulations, the NCCF proposal would allow estimates if precise costs could not be given. It was the NCCF proposal that formed the basis for new section 121(c).[54]

As a result of this amendment closing cost disclosures under Truth in Lending are now subject to several basic requirements. First, the provision is a general disclosure provision and does not relate to the finance charge. The creditor may not elect to include closing costs in

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53. FRB, 1973 ANNUAL REPORT 25. Note that the FRB believed it had authority to require closing cost disclosures under its rulemaking powers. However, it delayed rulemaking pending congressional clarification and perhaps for good reason. It can be argued that under the statutory scheme such regulations would be invalid. Clearly under § 106(e) closing costs are not to be included in the finance charge for real estate transactions. Under § 105 the Board may issue regulations to "carry out the purposes of this title." It is an open question whether closing costs are sufficiently related to "credit awareness" to come within § 105. However, under a liberal interpretation, it probably could be so interpreted.

Clearly, the FRB could require either separate disclosure of items or inclusion in finance charge for closing costs in nonrealty transactions under authority of the "catchall" language of § 106(d)(4).

> § 106(d) If any of the following items is itemized and disclosed in accordance with the regulations of the Board in connection with any transaction, then the creditor need not include that item in the computation of the finance charge with respect to that transaction:
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> . . . .
>
> (4) Any other type of charge which is not for credit and the exclusion of which from the finance charge is approved by the Board by regulation.

Note that subsections 106(d)(1)-(3) list specific instances: taxes, security interest insurance, and security interest search fees which would be equivalent to closing costs "incident" to nonrealty transactions. It is also important that § 106(d)(4) applies to *any* transaction while § 106(e) exempts items only in *realty* transactions and thus there is an inherent conflict. Most likely the entire situation is due to legislative oversight. The FRB has partly remedied this by requiring itemization of license, title certification, and registration fees imposed by law which may be part of closing costs in either a non real estate or real estate transaction.

54. 15 U.S.C.A. § 1631(c) (Supp. I, 1975). Note that the 1972 FRB Report recommendation was the first proposal of this language. The first bill proposed thereafter (as a committee amendment) which attempted to deal with the problem was S. 914 which used the FRB version. This was deleted in committee and a compromise measure, S. 2101, adopted the alternative provisions recommended by the NCCF. S. 2101 passed the Senate, but languished in a House subcommittee. Subsequently, the identical language was added to H.R. 11,221 and was enacted without change as Pub. L. No. 93-495.

the finance charge and avoid separate itemization. Secondly, the latest time for making disclosures is at least before downpayment is due in nonrealty transactions and before the loan commitment is made in realty transactions. Thirdly, all closing cost items must be disclosed.[55] Finally, estimates may be used if authorized and in conformity with FRB regulations.[56]

A fourth area, identification of individual sales transactions on monthly billing statements, is one in which problems of interpretation appeared in the original statute. The initial version of section 127 imposed disclosure requirements with respect to "open-end" credit[57] or accounts in which sales could be made from time to time and additional credit extended. Here, two basic types of disclosures are identified: disclosures to be made before an account is opened[58] and periodic disclosures while the account is used.[59] Examples of disclosures required prior to use of an open end account include the method of determining the balance upon which a finance charge will be imposed, the date when a finance charge will be imposed, and the method of determining the amount of this finance charge.[60] Periodic billing statements, usually one per month, must contain such information as the balance at the beginning of the period, amounts and dates of credit extensions during the cycle, amounts credited, finance charges imposed, the bal-

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55. The Act fails to specify exactly which items are included. Examples are given in S. REP. No. 278, 93d Cong., 1st Sess. (1973) to accompany S. 2101, where the language of this provision originated:

> The committee intends that all closing costs payable by the consumer should be disclosed whether or not a particular item of cost is incident to the credit aspect of the transaction. These include but are not limited to charges for application fees, credit reports, surveys, title examination, title insurance, attorney fees, origination fees, preparation of documents, closing fees, recording fees, transfer taxes, prepaid interest, taxes or insurance or loan discounts.

56. As in many other disclosure provisions, this section presents problems of interpretation. Note also the overlap with code sections dealing with finance charges. The real question here becomes if one must include both. Also note the existing overlap with § 106(d) and the regulations. A fair interpretation would find that an option exists as to the nonrealty transaction.

57. Section 103(i) of the Act defines "open end plan" as one in which terms are prescribed under which credit transactions may be made from time to time and finance charges imposed on unpaid balances resulting from these transactions (at certain times). 15 U.S.C. § 1601(i) (1970). See also 12 C.F.R. § 226.2(r) (1974) for a more comprehensive definition and FRB, INTERPRETATION § 226.203 (1969) (open end credit distinguished from other credit).

58. 15 U.S.C. § 1637(a) (1970) establishes the required disclosures prior to opening an open end account.

59. *Id.* § 1637(b) establishes such disclosures for periodic statements.

60. *Id.* § 1637(a)(2) (method of determination of the balance upon which a finance charge may be imposed); *id.* § 1637(a)(1) (when a finance charge may be imposed); and *id.* § 1637(a)(3) (the method of determining the finance charge disclosures).

ance upon which the finance charge was computed, and the outstanding balance at the end of the period.[61] The FRB perceived a problem with respect to section 127(b)(2), which mandates a disclosure of the amount and date of each extension of credit during the billing period. There was some question about how much information was required to enable a customer to discern the "correctness" of listed transactions. Original section 127(b)(2) merely ordained a "brief identification" of purchases involved and allowed an exception when identification had been previously furnished. If a seller presented a sales receipt at the time of the credit purchase that "briefly" identified the goods and services furnished, he was required merely to indicate on his monthly statements the dates and amounts of the charge transactions.[62]

The FRB recommended an addition to the section 127(b)(2) requirements because it believed that this statute could impose burdens upon smaller retailers who "handled many sales departments with one register."[63] However, the FRB's proposed simplification of the section was rejected in favor of a version which originated in the Fair Credit Billing debates.[64] The change that was enacted substantially modified section 127(b)(2) by imposing much stricter requirements and by giving the FRB great discretion in imposing them upon creditors.[65] The FRB and the courts could make the amended section very expensive for sellers and credit card issuers. First, identification is now required for *all* extensions of credit while the prior language required identification only for *purchases*. While this expansion is perhaps beneficial, it increases the risk that creditors in non-sales areas, such as dentists and doctors, innocently may violate the Act, unaware that they are engaged in transactions subject to the identification requirement. Secondly, the language that permitted the identifications to be brief has been deleted. Apparently the FRB is now authorized to require lengthy descriptions.

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61. For disclosure requirements on periodic billing statements see examples: balance at beginning of period, *id.* § 1637(b)(1); the amounts and dates of credit extensions during the period, *id.* § 1637(b)(2); amounts credited, *id.* § 1637(b)(3); amount of finance charges imposed, *id.* § 1637(b)(4); the balance upon which the finance charge was computed, *id.* § 1637(b)(8); and the outstanding balance at the end of the period, *id.* § 1637(b)(9).

62. *Id.* § 1637(b)(2). *See also* 12 C.F.R. § 226.7(b)(2) (1974). This regulation specified that "Identification may be made on an accompanying slip or by symbol relating to an identification list printed on the statement." *Id.* at n.7.

63. FRB, 1972 ANNUAL REPORT 17-18.

64. *See* S. 2101, 93d Cong., 1st Sess. (1973).

65. 15 U.S.C.A. § 1637(b)(2) (Supp. I, 1975), *amending* 15 U.S.C. § 1637(b)(2) (1974). Note that the effective date of this change is October 28, 1975. *See* note 171 *infra*.

Thirdly, the FRB now has complete discretion to prescribe the form of identification. It can invalidate present records systems, thus requiring expensive systems changes, especially for companies using computer systems whose equipment may not perform functions demanded by the FRB. Fourthly, a new requirement is imposed to clarify the "sufficiency" of the disclosures. They must allow the obligor to relate identified transactions to sales vouchers previously furnished. What is sufficient is an open factual question. Finally, and most seriously, sales slips alone can no longer satisfy the identification requirement of section 127(b)(2). Under prior law the identification on the slip and a later billing that indicated merely the dates of purchases and amounts was enough. Presumably, with this information, the majority of consumers could match dates and check transactions. However, new section 127(b)(2) rejects this rationale and puts the onus on the creditor to list each extension of credit regardless of any prior documentation. This could also add enormous costs to record keeping and monthly billing. Although there may have been a problem with consumers' inability to tell which purchases were included in the balances shown on the billing statement, it is debatable whether the problem was serious enough to warrant the remedial steps taken.[66]

C. *Clarifying Ambiguities and Closing Loopholes*

In addition to changing various technical provisions in the Act and imposing new disclosure requirements, Congress took certain steps in its 1974 revision of the Act to close loopholes and resolve ambiguities in the original language. The first necessary clarification arose from the interaction between two sections of the Act. The Act as originally enacted regulated disclosures of credit terms in consumer oriented transactions; business or commercial transactions were specifically excluded.[67] Three sections, however, were added to the Act in 1970 to

66. In fact, small businessmen, the original object of the FRB's concern would stand in the poorest situation here. The larger firms run their systems by computer billing and detailed identification, which while expensive, may at least be economically possible. The relative expense in meeting this new requirement may be much greater for the small businessmen and greatly add to competitive disadvantages insofar as record-keeping and billing are concerned. In fact, this requirement alone may require storekeepers to abandon their own credit programs and switch to use of national credit cards such as Mastercharge or Bank Americard.

If the FRB is concerned about the small businessman at this juncture it should use the leeway granted in the revised statute by Congress and loosen the disclosure requirements on this class of creditors.

67. 15 U.S.C. § 1603(1) (1970). See also 12 C.F.R. § 226.3(a) (1974) which mirrors this code section. Note that consumer credit is that extended to a natural per-

deal with credit card use.[68] When the additional sections were added, the business transaction exemption was forgotten, and an uncertainty about the application of sections 132 through 134 to commercial enterprises quickly arose due to the section 104(1) exemption. The FRB felt that, since this was only an oversight, it could remedy the problem through rulemaking. Accordingly, it amended Regulation Z in 1972 to provide that credit card provisions applied to business and other commercial transactions as well as to "personal, family, household or agricultural transactions."[69] In addition, the FRB requested a simple legislative clarification in its 1972 Annual Report.[70] Congress responded but the acknowledgment was not simple.[71] New section 135 will subject businesses to the credit card provisions of the Act, but a limited exception is provided for businesses with ten or more employees. These businesses are allowed to redistribute liability with a credit card issuer by contract although no liability may be imposed upon any employee of the cardholder.[72] Under section 135 a fair number of firms may be liable for credit card problems if they accept such liability through agreement with the issuer. Presumably, cardholders who reissue cards to ten or more employees are large enough to deal at "arms length" with credit card issuers. However, the validity of this presumption for smaller firms is questionable. The exception could prove to be detrimental.[73]

A second clarification made by the 1974 amendments deals with the debtor's right to rescind certain transactions when the creditor has failed to comply with the Act. The right to rescind is an important and novel aspect of the Truth in Lending Act. Originally imposed to strike at perfidious "second mortgage brokers," the basic provision gives the

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son, not a business. *Id.* § 226.2(k) further indicates the basic intent of the Act, to exempt business transactions.

68. Section 132, issuance of credit cards; § 133, liability of holder of credit card; and § 134, fraudulent use of credit card. Act of October 26, 1970, 84 Stat. 1126 (1970).

69. 12 C.F.R. § 226.13(4) (1970). "'Cardholder' means any person to whom a credit card is issued . . . . for commercial purposes." This regulation was challenged immediately after promulgation. Credit Card Serv. Corp. v. Federal Trade Comm'n, D.C. Civ. Act. No. 1357 (1973); Universal Air Travel Plan v. Board of Governors of the Fed. Reserve Sys., D.C. Civ. Act. No. 2485 (1972).

70. The FRB suggestion would have simply added § 135 in the form: "The provisions of section 104(1) shall not apply to sections 132, 133 and 134."

71. 15 U.S.C.A. §§ 1631-45 (Supp. I, 1975), *amending* 15 U.S.C. §§ 1631-44 (1974).

72. *Id.*

73. For example, a small sales firm which employs eleven salesmen. This firm needs credit cards to effectively carry on its business yet may not have the bargaining power to fairly distribute liability between itself and the issuer.

debtor a three-day right to rescind transactions in which a security interest "is or will be retained or acquired in any real property which is used or expected to be used as the residence of the person to whom credit is extended."[74] Section 125(a) specifies that disclosure of this right shall be made to consumers, and section 125(b) determines the effect of an exercise of the right.[75]

An early question about the scope of the right to rescind arose: Does the right attach when a security interest arises through operation of law? The FRB decided that with respect to certain "automatic" types of liens such as mechanics' or materialmen's liens, the right was available.[76] Two early court decisions reached inconsistent results,[77] however, and the FRB solicited legislation to specify that notice was to be given when the creditor *could* obtain a lien on the debtor's residence through operation of state law.[78] Although both court decisions were eventually decided in favor of the FRB position at the circuit court level,[79] the FRB continued to advocate a refinement. This resulted in amendment of section 125 to specifically provide that security interests subject to this section include those "arising by operation of law."[80] This upholds the FRB's interpretation but it must be noted that it is quite limited. More controversial and complicated problems have not

74. 15 U.S.C. § 1635(a) (1970). *See also* 12 C.F.R. § 226.9 (1974) for general requirements and *id.* § 226.9(b) (1974) for specific mandatory disclosure requirements.

75. Under 15 U.S.C. § 1635(b) (1970) a security interest becomes void, money or property received by the creditor must be returned within ten days, and the creditor must take action to terminate the security interest. The debtor may retain the goods until the creditor complies with these requirements, then must tender return to the creditor either at the location of the goods or at the creditor's place of business at the option of the debtor. The creditor has ten days to accept this tender or the debtor may have the property without paying for it. *Id.*

76. FRB, LETTER No. 101 (1969) reprinted in R. CLONTZ, TRUTH IN LENDING MANUAL (1973). Materialmen's liens are within the ambit of § 125(a). See also FRB, LETTER No. 123 (1969) (materialmen and subcontractors) and FRB, LETTER No. 136 (1969) (same).

77. N.C. Freed Co. v. Board of Governors of the Fed. Reserve Sys., Civ. No. 1970-43 (W.D.N.Y., filed Sept. 29, 1971) held that the right to rescind did not arise from the fact that a lien by operation of law could create such a security interest. However, Gardner & North Roofing and Siding Corp. v. Board of Governors of the Fed. Reserve Sys., 464 F.2d 838 (D.C. Cir. 1972) held that the right to rescind did arise in such transactions.

78. FRB, ANNUAL REPORT TO CONGRESS ON TRUTH IN LENDING 19-20 (1971) [hereinafter cited as FRB, 1971 ANNUAL REPORT]. In addition, note that the 1972 FRB ANNUAL REPORT contained suggested statutory language. FRB, 1972 ANNUAL REPORT 21.

79. N.C. Freed Co. v. Board of Governors of the Fed. Reserve Sys., 473 F.2d 1210 (2d Cir. 1973), *cert. denied*, 414 U.S. 827 (1974), reversed the district court decision.

80. 15 U.S.C.A. § 1635(a) (Supp. I, 1975), *amending* 15 U.S.C. § 1635(a) (1974). Also 15 U.S.C.A. § 1635(b) (Supp. I, 1975), *amending* 15 U.S.C. § 1635(b) (1970).

been answered[81] and the amendment itself raises at least two inquiries: What effect does a valid waiver have on the right to rescind and does the possibility of a judgment lien trigger the right?[82]

A third clarification of the Act also relates to the operation of section 125. As originally enacted this section specified that notice of the right to rescind must be given but no time limit on its availability was included. Since the statute stated that the right existed until midnight of the third day following delivery or the dispensing of other required disclosures,[83] the logical interpretation of this provision was that the right continued until the later of delivery or disclosure, no matter how long such disclosures might take. Fearing that a continuing right could constitute a cloud on titles, the FRB advocated a three year limit on the right,[84] and in 1972 a specific addition to section 125 was proposed.[85] The suggestion was adopted in the 1974 amendments.[86]

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81. Note that other amendments to § 125 of the Act were made by the 1974 Act. *See* notes 83 to 88 *infra.*

Two examples of controversial problems surrounding the right to rescind include: First, does the right to rescind arise from confession of judgment or cognovit note provisions? *See* FRB, INTERPRETATION § 226.202 (1969) (right to rescind arises unless effectively waived in the instrument) reprinted in 1 CCH CONS. CR. GUIDE ¶ 3510.04 (1974). Secondly, what form must such a waiver take?

82. Although it is clear that waiver of a cognovit note or confession of judgment, at least under FRB interpretations, will annul the right to rescind, the application of the waiver principle to the mechanics or materialmen's liens is unclear. FRB, INTERPRETATION § 226.901 (1969) reprinted in 1 CCH CONS. CR. GUIDE ¶ 3589.05 (1975), would imply that a valid waiver here would also terminate the right to rescind. However, since mechanics or materialmen's liens arise by operation of state law it is unclear whether waiver is allowed and what form a valid waiver must take since the statutes are generally silent on this.

The second inquiry raised by the amendment is a continuing one, does the right to rescind arise from the mere possibility of a judgment lien? This carries the lien problem to an absurdity because if such liens give rise to the right to rescind, the § 125 right would arise in all transactions because there is always the possibility that a judgment lien will eventually result from a transaction if the debtor refuses to pay. This is seemingly beyond the intent of § 125 for if Congress meant the right to extend to all transactions it could easily have done so. Therefore the FRB has denied that the right applies to the mere possibility of a judgment lien. *See* FRB, LETTER No. 29 (1969) reprinted in CLONTZ, *supra* note 76, at E-117. "[N]either the right nor the notice applies if the only possibility of a lien in (*sic*) that which would follow an ordinary law suit, including prior service of process and opportunity to present defenses . . . ."

Despite this FRB position, a possibility exists that a court could hold, based upon the new language adopted, that since a judgment lien arises by operation of law, and could be obtained in the debtor's residence, the right to rescind must be given in all credit transactions.

83. 15 U.S.C. § 1635(a) (1970). *See also* 12 C.F.R. § 226.9(a) (1974).

84. FRB, 1972 ANNUAL REPORT 15-16. Note that § 125(a) also continues the right to rescind until other "correct" disclosures are given. Thus any disclosure error in conjunction with a transaction could continue infinitely.

85. FRB, 1972 ANNUAL REPORT 32. Subsequently the NCCF agreed with this suggestion, FRB, 1973 ANNUAL REPORT 22, and it was incorporated by Committee amend-

Three main points must be emphasized with respect to this amendment. First, the indefinite rescission period under prior law has been cut to three years. Secondly, this time period can be shorter if the debtor sells the "property" (presumably either realty or goods purchased as fixtures, although the wording of the statute is unclear as to fixtures). Thirdly, failure to disclose the right to rescind or any other required information is now specifically a continuing violation. For example, failure to specify the total number of payments in the initial contract in a closed end transaction (required in section 128(a)(8)) will now allow the right to continue until the earlier of sale of the property or three years. The relationship between the time limits in section 125, however, and the time limits established in the civil liability sections of section 130 has not been defined and a conflict between these two sections seems imminent. If a debtor brings a civil action for a creditor's section 125 failures, he normally would be barred from recovery after one year.[87] However, if section 125 is read in conjunction with section 130 a recovery could be allowed four years after the initial failure to comply.[88]

A fourth problem area attacked by the 1974 changes deals with the "grace period" for imposition of finance charges on revolving charge accounts. To allow a consumer to shop more intelligently for

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ment to S. 652, 92d Cong., 1st Sess. (1971). *See* S. REP. No. 750, 92d Cong., 2d Sess. 18 (1972). *See also* S. 914, 93d Cong., 1st Sess. 17 (1973) and S. 2101, 93d Cong., 1st Sess. (1973).

86. 15 U.S.C.A. § 1635(f) (Supp. I, 1975), *amending* 15 U.S.C. § 1635(a)-(e) (1974).

87. 15 U.S.C. § 1640(e) (1970) establishes the time limit for bringing civil recovery actions under Truth in Lending as one year.

88. If the right to rescind is specifically a continuing violation, notice of the right must effectively be given during the three year § 125 limits. However, it is arguable that the debtor has one year after the last day of this § 125 violation period to bring a § 130(a) civil damage action, or a total of four years after the right originally arose.

This is probably not what Congress intended. The true intent can better be produced by focusing on the violation of the Act caused by failure to give notice of the right. The remedies of rescission and damages should be separated and for damage purposes the time period should run from the first date that notice was required and limited to one year. The rescission right should start running at the same time and should expire in three years.

Note also that Congress did not clarify another conflict between the rescission provisions of § 125 and the damage provisions of § 130. Are the remedies of these two sections alternative or conjunctive? The courts have split on this question and a clarification is needed. See Bostwick v. Cohen, 319 F. Supp. 875 (N.D. Ohio 1970) (election of remedies required: debtor may have rescission or damages but not both) and Palmer v. Wilson, 359 F. Supp. 1099 (N.D. Cal. 1973) (no election required: debtor may have both rescission and an action for damages), *vacated*, 502 F.2d 860 (9th Cir. 1974) (request for both forms of relief may be granted, but this is directed to the court's discretion and sense of equity rather than automatic).

credit, certain information about open end credit plans must be given prior to the opening of any such account, and certain disclosures must be made on monthly billing statements.[89] A key disclosure is the length of any "free ride," or grace period, during which a debtor need not pay his outstanding balance and will not be assessed a finance charge. For instance, many gasoline companies allow one month to pay before a finance charge will be imposed upon the amounts due. Disclosure of this period allows customers to plan their financial affairs most efficiently and also allows an evaluation or comparison of various credit plans.[90]

Under the initial version of section 127(a)(1) a creditor was required to disclose any free ride period before an account was opened; under section 127(b)(10) he was required to divulge on monthly statements the time that could elapse before any "additional finance charges would be imposed upon amounts due."[91] Presumably, if a creditor disclosed that a free ride period were available, any deviation in actual practice, such as shortening or lengthening the time period, would constitute a violation of the Act, regardless of whether a longer time were given because of billing problems or out of a desire to aid the consumer.[92]

A proposal to allow some grace period beyond that actually dis-

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89. 15 U.S.C. § 1637 (1970). *See* text accompanying notes 58 to 66 *supra.*

90. For example, under Plan A the annual percentage rate is 18% (or 1½% per month), the balance upon which the finance charge is imposed is the "new balance", the free ride period is sixty days, and bills are sent on the first day of each month. Plan B provides that the annual percentage rate is 16% (1⅓% per month), the finance charge is imposed on the new balance, there is NO free ride period, and bills are again sent on the first day of the month. It would appear that Plan B is cheaper to the customer because lower rates of interest apply. However, this may not be the case, because of the free ride allowed under Plan A.

If the customer makes a $100.00 purchase in January and intends to pay in April (assuming that this will be his only account transaction during the year) Plan A is actually cheaper. Under Plan A, the only finance charge imposed on the customer will be $1.50 (1½% on the balance owed as of April 1 of $100.00). Thus the EFFECTIVE annual percentage rate for this transaction is sliced from 18% to 6% because of the free ride period. On the other hand, under Plan B, with the same facts, the customer will make interest payments of $1.33 for January in conjunction with his February 1 billing; $1.35 for February in conjunction with his March 1 billing; and $1.37 for March in conjunction with his April 1 billing or a total of $4.05 for use of the $100.00 for three months. Thus the EFFECTIVE annual percentage rate for Plan B is still 16%. The customer should know the free ride period in order to make a comparison of the EFFECTIVE rates of interest.

91. 15 U.S.C. §§ 1637(a)(1), (b)(10) (1970).

92. The creditor could be found civilly liable for such a violation, for intent has nothing to do with civil liability under the *Ratner* rationale. *See* notes 19-20 and accompanying text *supra.*

closed was made in the Senate and eventually enacted without change.[93] Both section 127(a)(1) and section 127(b)(11) were amended to allow the creditor "at his election and without disclosure" to forego finance charges despite receipt of payment after the end of the free ride period.[94] The only difficulty with the amendment appears in a difference between the language of the Act and the Senate report in which the language was first proposed. The statute specifies no limit on how long the creditor may give the debtor to pay before imposing a finance charge. Presumably, he could dispense with them altogether. The Senate report, however, states that the intent was to limit these grace periods to a maximum of seven days, or the end of the present billing period.[95] The FRB may restore the original intent by regulation although it is uncertain if it has the authority to modify the clear meaning of the statute and it is somewhat uncertain whether imposition of such limits is advisable.

To evaluate the desirability of imposing a time limit on the grace period, the interests of the debtor and the creditor must be understood. Certainly, the consumer who gets the free ride will benefit economically; but if too many creditors use the grace periods inconsistently, any comparison of credit plans will be impaired. Since in the long run the effects of the free ride on the consumer balance out, its impact upon creditors should control. Basically, there are two kinds of creditors who maintain open end charge plans: those who are in the credit business to make a profit and those who are happy to break even or take a loss because they view the credit business as a customer service. Arguably, the first type of creditor will not abuse any unlimited undisclosed free ride provision for it seems that he would be quite willing to disclose the longest free ride period possible to attract more credit customers. Additionally, the second type of creditor would benefit by allowing an unlimited free ride period. Given that his motives are pure and that he is losing money by allowing an extended free ride period, perhaps no time limit should be imposed. Therefore on balance, considering the equivocal nature of an unlimited free ride period from the consumer's viewpoint and the motives for its use by the creditor, there should be no limit on its use.

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93. 15 U.S.C.A. § 1637 (Supp. I, 1975), *amending* 15 U.S.C. § 1637(a)(1), (b)(10) (1974).
94. *Id.*
95. S. REP. No. 750, 92d Cong., 2d Sess. 20 (1972).

D. *Miscellaneous Additions to the Act*

Some of the congressional additions to the Act cannot be easily categorized. The first of these requirements deals with the interrelation between the section 104 exemptions from the Act and the section 125 right to rescind with respect to state agencies. Section 104(1) of the Act eliminates governmental agencies from its purview.[96] However, a question apparently arose about whether state agencies were subject to the right of rescission granted to debtors by section 125 of the Act. Thus, in the 1974 amendments Congress specifically provided that the right to rescind did not apply when the lienholder was a state agency.[97] Although this merely carries out the clear intent of section 104 of the Act and appears to be reasonable, since presumably states will not take advantage of debtors, it did engender a certain amount of controversy in its consideration.[98]

A second addition in this category concerns the liability of assignees of consumer credit contracts. A key question under the original Act was whether an assignee of a contract would be liable for Truth in Lending violations of the original creditor, at least where violations were clear on. the face of the assigned contract. While many courts skirted the issue by broadening the definition of "creditor under the Act" to include various types of assigness,[99] the FRB believed the problem could be reached by negative implication from section 131. The provision stated that a written acknowledgement of receipt would constitute proof of delivery of disclosures in any action brought against an assignee. Proof of receipt was conclusively presumed from the fact that a writing purported to reflect it. In addition, to avoid liability the assignee was required to show that he had no knowledge of lack of receipt and that the violations were not apparent on the face of the statement.[100] By negative implication, if knowledge or an obvious violation

96. 15 U.S.C. § 1603(1) (1970).

97. 15 U.S.C.A. § 1635(e) (Supp. I, 1975), *amending* 15 U.S.C. § 1635(e) (1974).

98. 120 CONG. REC. H10,279 (daily ed. Oct. 9, 1974) (remarks of Rep. Sullivan). Note the inaccuracy of these remarks. Section 412 merely exempts state agencies from transactions in which the right to rescind would arise. Rep. Sullivan presumes that it would remove state agencies from the purview of Truth in Lending. Actually, the kind of exception the Congresswoman is objecting to has already been enacted in § 104(1).

99. *See, e.g.*, Kriger v. European Health Spa Inc., 363 F. Supp. 334 (E.D. Wis. 1973) and other health spa cases holding that assignee banks were creditors contemplated by the Act when they purchased installment contracts for the provision of services. The courts emphasize that the prior knowledge by the spa operator of subsequent sales of the contracts makes the subsequent assignee a creditor under the Act. Actually, given § 130(d) there is perhaps little justification for this extension.

100. 15 U.S.C. § 1641 (1970).

were present, a subsequent assignee could be held liable.[101] The weakness of the FRB's rationale is that section 131 purports to deal only with the "delivery" of disclosures requirement and ostensibly does not attempt to deal with the content of such disclosures. The FRB, therefore, agreed that the matter needed clarification and concurred in an NCCF proposal imposing liability on assignees in limited situations.[102] This proposal was adopted in the 1974 amendments and provided that "except as otherwise provided" the liability of the original creditor would be imposed on a subsequent assignee if a violation were clear on the face of the instrument; liability would not be imposed, however, if the assignment were involuntary.[103]

Two problems arise in this area from new section 115. First, courts may now be more reluctant to extent the "creditor under the Act" definition to assignees. Since the liability of assignees under section 115 is narrower than that of original creditors, the new section could actually diminish the exposure of subsequent assignees to Truth-in-Lending liability. Secondly, the relationship between new section 115 and prior section 130(d) and section 131 is unclear. Section 130 (d) imposes civil liability on assigness where there is a continuing business relationship between the original creditor and the assignee. Presumably, the first phrase of new section 115—"Except as otherwise provided in this title"—would preserve the applicability of section 130 (d) where a continuing business relation exists. The last phrase in section 115 imposes the "involuntary assignment" exception to assignees just as in section 130(d). The potential liability of non-related assignees under section 115 is actually greater than that of related assignees under section 130(d) because section 130(d) contains a "good faith" defense while section 115 does not. The question then becomes

101. FRB, 1973 ANNUAL REPORT 25. The FRB conclusion is by negative inference from § 131. In an action against an assignee without knowledge to the contrary, a written indication of receipt of disclosures by the debtor is conclusive proof of delivery of the disclosures unless the violation is apparent on the face of the statement. The inference is if the violation is apparent on the face of the instrument, any subsequent assignee can be held liable. The FRB position ignores the fact that this section of the Act apparently, or at least on its face, applies only to delivery and not to the content of disclosures.

An equally strong inference was possible from the nature of § 130(d). Since this section imposed liability on specific types of assignees, the inference is that Congress was aware of the assignment problem and chose only to impose liability on certain types, those in a continuing business relationship with the original creditor. Thus it could be argued that under the original Act non-related assignees were not subject to Truth in Lending liability.

102. FRB, 1973 ANNUAL REPORT 25.

103. 15 U.S.C.A. § 1601-14 (Supp. I, 1975).

whether the first sentence of the new section totally pre-empts its application to related assignees when section 130(d) could also be applied. The continued availability of the good faith defense in section 130(d) situations seems to hinge on this construction.[104] In addition, there is a question of continuing applicability of section 131 to the assignment situation.[105]

The liability of assignees of instruments for transactions that require Truth-in-Lending disclosures has become quite complex because of the enactment of new section 115. The statutory framework seems to provide the following. First, where there is a continuing business relationship section 130(d) seems to apply exclusively to impose liability upon assignees, to allow a good faith defense, to provide an excuse for involuntary assignment and to impose liability whether or not the violation is apparent on the face of the instrument. Secondly, where no continuing business relationship exists, section 115 imposes liability and allows an excuse for involuntary assignments and an exception where the violation is not apparent on the face of the document, but disallows any "good faith" defense. Finally, section 131 now appears to be limited to problems of proof at trial where a debtor alleges that required disclosures were not "delivered" to him.[106] Despite the added complexity, new section 115 appears to be a step in the right direction because it removes the possibility that Truth-in-Lending violations can be purged by assignment of the credit instrument.

A third area that concerned Congress is criminal credit card fraud. Credit card fraud was not included in the original Act but was added

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104. Certainly this conflict represents a congressional omission rather than an intent to hold non-related assignees to a higher standard than related assignees. However, it may be a "trade-off" because related assignees are liable whether or not the violation is apparent on the face of the instrument, unlike non-related assignees. Thus it could be that Congress did not intend to allow any defenses for truly "apparent" violations. Although the violation could be cognizable on the face of an instrument and through genuine mistake the assignee could fail to discover it.

105. A third problem is that the relationship between Federal Truth in Lending and state commercial codes regarding the liability of assignees is quite unclear. Certain proponents of this legislation have stated that it limits the holder in due course doctrine. The issue directly presents the problem of what happens when federal law attempts to preempt matters that have traditionally been within the purview of state regulation, such as the holder in due course. Note, however, that the conflict does not really arise here because if the violation is apparent on the face of the instrument, an assignee could not be a holder in due course because he would have had notice of a defense to liability by the obligor. UNIFORM COMMERCIAL CODE § 3-302 (1972).

106. Very likely the original intent of this section. *See* discussion at note 101 *supra*.

in 1970 as one of three sections dealing with credit cards.[107] Problems were detected in the scope of these criminal provisions and, not surprisingly, remedial legislation was introduced.[108] The resulting amendment of section 134 completely overhauled the criminal sanctions and significantly changed the definition of credit card misuse. First, the type of conduct proscribed has been considerably broadened. Prior section 134 merely made the act of "use" of a tainted credit card criminal conduct, while new section 134 penalizes the act, attempt or conspiracy.[109] Secondly, the nature of the criminal conduct has been redefined. Under the 1970 version of section 134 tainted cards must have been used in a "transaction affecting interstate or foreign commerce." While this is retained in the new section, various other activities have been included: transport (or attempt or conspiracy) of stolen cards;[110] receipt of goods obtained with tainted cards;[111] use of interstate or foreign commerce (with unlawful intent) to sell or transport a tainted card;[112] receipt of travel tickets obtained with tainted cards;[113] and furnishing items in transactions affecting interstate or foreign commerce through use of tainted cards.[114] Thirdly, the types of property obtained have been extended from "goods and services" to "money, goods, services and anything else of value." Fourthly, the valuation of items received has been clarified and the lower limit for criminal liability has been reduced. Under prior law the value of property received had to have a retail value of 5000 dollars or more. The statute failed to specify whether this was cumulative, per card, or per criminal transaction. The new section only requires receipt (or use) of property of 1000 dollars value or more, and is specifically cumulative as to time, adding the total of transactions within one year. The coverage under the "value received" requirements is much broader and, in addition, a special category has been established for travel tickets. Here, the annual value received need only be 500 dollars to find a criminal violation. Otherwise the requirements are the same as for other property receipt violations. Finally, the penalties imposed for violation have been stiffened.

107. Sections 132-43 of the Act, added by Pub. L. No. 91-508, § 502, 84 Stat. 1126 (1970).
108. *See* S. Rep. No. 750, 92d Cong., 2d Sess. (1972).
109. 15 U.S.C.A. § 1644 (1975). See specifically new § 135, *id.* § 1644(a).
110. *Id.* § 1644(b).
111. *Id.* § 1644(d).
112. *Id.* § 1644(c).
113. *Id.* § 1644(e).
114. *Id.* § 1644(f).

The 10,000 dollar fine provision remains the same but the maximum prison term has been doubled to a period of ten years.

Despite the changes in section 134 various themes remain constant. First, the knowledge requirement is the same in both the old and the new Act: The actor must have known of the "taint" attaching to the credit cards. Secondly, the definition of tainted cards remains identical: "counterfeit, fictitious, altered, forged, lost, stolen, or fraudulently obtained." Finally, the requirement of interstate or foreign commerce is retained because of the necessity for federal jurisdiction. In short, the misuse-of-credit-card criminal statute has been vastly expanded in its specific coverage. Presumably, it will cover a broader range of criminal activity. Its impact on credit card misuse, however, remains to be seen.

E. *Civil Liability*

Despite the importance of other alterations and additions to the Truth in Lending Act, the provisions relating to civil liability engendered the greatest controversy during debates and are likely to register the greatest impact. Since Congress originally intended that enforcement of the Act would occur mainly through civil actions, the liability provisions are central to the regulatory scheme. Immediately after the passage of the Act in 1969 certain problems concerning the scope of liability, the defenses available to creditors, and the applicability of civil damages to class actions arose and early proposals recommended clarifications. However, the changes were so controversial that five years passed before their enactment.

Courts hearing Truth in Lending cases initially held that despite its rather open language and despite congressional history to the contrary, the section 130(c) defense of "bona fide error" was limited to clerical errors.[115] An early concern of the FRB was that a creditor would be held liable for violating the Act when he relied on an FRB Opinion which was later found to be invalid.[116] The FRB thus pro-

115. *See* discussion at note 20 *supra.*

116. This fear was soon vindicated. In addition to *Ratner* discussed in notes 15 to 21 *supra, see* Ives v. W.T. Grant Co., 4 CCH CONS. CR. GUIDE ¶ 98,847 (D. Conn. 1974). Here defendant attempted to assure that the disclosures made in conjunction with a "coupon book" credit plan were made in conformity with the Act and Regulations. However, the court rejected the § 130(c) defense, noting that errors of law were not permitted under Truth in Lending as a defense to liability and that once a violation was shown, only proof that it resulted from clerical error would negate defendant's liability. *Id.* at 88,526.

In the *Ratner* case, specific reliance by defendant upon an FRB regulation was re-

posed a good faith reliance defense similar to one used for SEC compliance.[117] The first change in section 130 contemplated by Congress dealt with this FRB request and new section 130(f) provides a good faith reliance defense for creditors who rely upon FRB rules, regulations or interpretations, notwithstanding the fact that after reliance such requirements are "amended, rescinded, or determined to be invalid for any reason."[118] This amendment is quite limited and fails to deal with other problems of section 130(c) interpretation.[119]

A second important change in the provisions of section 130 made by the 1974 amendments refines the definition of "transaction" in section 130(a). The original version of the Act specified that a 100 dollar minimum and a 1000 dollar maximum recovery for violations was to be provided "per transaction." No meaning was given to this term. In closed end transactions, in which only one set of disclosures was required, it was fairly clear that "transaction" referred to initial disclosures made at the conclusion of the agreement. However, in open end plans, in which disclosures were required both upon opening of such accounts and also in conjunction with monthly billing statements, the meaning of this term was quite unclear. "Transaction" could have been intended to mean the entire process of opening and using an account, or only those occasions that called for specific disclosures[120] or each account transaction. All three interpretations were supportable and logically justifiable given the original ambiguity.

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jected when the regulation was held invalid and defendant was found to be liable for civil damages despite this reliance.

In the view of one writer, such interpretation was considered quite invalid. "If the Ratner case is followed by other courts, any safety in compliance with Regulation Z will go by the Board . . . . The writer finds Judge Frankell's general approach to the power of the Board extremely disturbing." R. CLONTZ, *supra* note 76, at 3-159.

117. FRB, 1971 ANNUAL REPORT 14-15. Use of a method similar to that of the SEC was recommended in the 1972 Annual Report. The SEC provision reads:

> No provision of this subchapter imposing any liability shall apply to any act done or omitted in good faith conformity with any rule or regulation of the Commission notwithstanding that such rule or regulation may, after such act or omission, be amended or rescinded or be determined by judicial or other authority to be invalid for any reason.

15 U.S.C. § 77s(a) (1970). The only change in the FRB adaptation adds "interpretation" to the class of items upon which the creditor may rely. *See* FRB, 1972 ANNUAL REPORT 32.

118. 15 U.S.C.A. § 1640(f) (Supp. I, 1975), *amending* 15 U.S.C. § 1640 (1974). The FRB proposal was enacted without change and seems to have engendered little controversy, except on the part of individuals who desired a broader defense. *See* S. REP. No. 750, 92d Cong., 2d Sess. 45-46 (1972) (remarks of Sen. Tower).

119. Such as the split over whether it applies merely to clerical errors or covers other types of reliance errors. *See* discussion at note 20 *supra.*

120. In other words, one penalty for failure to disclose items prior to opening an account, and a separate penalty for each violation on a monthly billing statement.

The FRB believed that "transaction" in section 130 meant the entire process of opening and using an account. This interpretation subjected creditors to the least possible liability. However, in open end credit, a single error could be repeated each time a monthly billing statement was sent and penalty damages for Truth-in-Lending failures could be multiplied. The problem became critical when one court held that "transaction" as used in section 130 indicated separate penalties for each separate document or billing statement contemplated by the Act. In *Thomas v. Myers-Dickson Furniture Co.*[121] the trial court held, and the circuit court affirmed, that "transaction" for the purposes of section 130(a) liability meant each periodic billing statement. Thus, if a creditor made an error on one of his statements and repeated the error on subsequent statements, he could be liable for a minimum of 1200 dollars and a maximum of 12,000 dollars for monthly statement violations, in addition to costs and attorneys fees.[122] The FRB interpretation of "transaction" was accepted by Congress in the 1974 amendments, effectively overruling the holding in *Thomas*. New section 130(g) states that multiple failures to disclose Truth-in-Lending information in connection with a *single account* entitled the debtor to only one recovery. An exception is made for situations in which violations are repeated after a recovery is granted.[123] The enactment of this provision adds another element to the already confused picture of defenses to Truth-in-Lending civil liability[124] and "transaction," as ultimately defined, provides the least rather than the greatest amount of liability for a given set of open end credit violations.

A third provision which changes section 130 was enacted to remedy an initial oversight. Initially, section 130(a) provided that civil penalties in the amount of two times the finance charge imposed with a 100 dollar minimum and a 1000 dollar maximum recovery per transaction were the damages recoverable in an individual action, plus court costs and attorneys fees if the action was successful.[125] Significantly, the Act did not provide for a recovery of "actual damages" such as costs of defending actions on a security interest upon which the right of rescission had not been disclosed. Congress apparently believed that fi-

121. 1969-1973 TRANSFER BINDER CCH CONS. CR. GUIDE ¶ 99,056 (N.D. Ga.), *aff'd*, 479 F.2d 740 (5th Cir. 1973).

122. Obtained by coupling the liability provisions of § 130(a) with the one year statute of limitations of § 130(e).

123. 15 U.S.C.A. § 1640(g) (Supp. I, 1975), *amending* 15 U.S.C. § 1640 (1974).

124. *See* discussion in text accompanying notes 150 to 161 *infra*.

125. 15 U.S.C. § 1640(a) (1970).

nance charges would be the main damage component in any violation of the Act and civil damages originally were predicated entirely on this element. In addition, the original Act was mainly concerned with disclosure rather than any aspect of the bargain between the creditor and the debtor.

The altered Act gives the wronged debtor the opportunity to seek both actual damages and penalty damages in his suit, in addition to reimbursement for costs and attorneys fees.[126] Now, for example, if a

126. 15 U.S.C.A. § 1640(a) (Supp. I, 1975), *amending* 15 U.S.C. § 1640(a) (1974). Specifically, see the amended version of § 1640(a): § 1640(a)(1) actual damages; § 1640(a)(2)(A) punitive damages; and § 1640(a)(3) attorneys fees.

Note also that the preamble to liability in this section has been significantly changed and considerably broadens the coverage of Truth in Lending liability and removes at least one possible defense to liability. Under the older statute civil liability was imposed for "failure to disclose" information required to be disclosed *by the Act.* Thus it was arguable that no liability attached for the manner of disclosure (failure to disclose clearly and conspicuously as required by various sections of the Act and the Regulations) or for violation of the Regulations, if the disclosures were in addition to those required under the Act. However, this defense was never accepted by the courts.

The new language clearly refers to liability for violation of "any requirement" of Truth in Lending rather than "disclosure" and thus removes one loophole. However, the problem of violations of regulations that impose requirements in addition to the Act has not been clarified. However, given that the regulations are promulgated "under" authority granted by the Act, they can be interpreted as a "requirement" and this ambiguity is also resolved.

Finally, one question raised by subsection (a) that has not been answered directly or by implication from the 1974 amendments is which parties have standing to sue under the Act. If a debtor has incurred no actual damages (no injury) and has not incurred any finance charges, may he still bring an action and recover costs and attorneys fees? If the action is in the nature of an injunction (there is a question here if Truth in Lending injunctions are authorized; however, they have been granted. See Ives v. W.T. Grant Co., 4 CCH CONS. CR. GUIDE ¶ 98,526 (D. Conn. 1974).) and if it is successful, costs and attorneys fees are indicated. However, if the suit is one for actual or punitive damages and plaintiff can show no injury, can the plaintiff succeed? Courts have split on this issue. The *Ratner* court held yes, since one purpose of the Act is to encourage private litigation to enforce it. *See* Ratner v. Chemical Bank New York Trust Co., 329 F. Supp. 270, 283 (S.D.N.Y. 1971). However there is authority to the contrary. Rodriguez v. Family Publications Serv., 57 F.R.D. 189 (C.D. Cal. 1972).

Undoubtedly the policy of private enforcement would be furthered by permitting any person to assert a Truth in Lending violation. However, there are serious constitutional standing and policy problems in allowing one without a cognizable injury (perhaps defining the injury as "legal" rather than economic would surmount this, but this is perhaps logically indefensible) to bring an action because the individual presumably would have little real interest in the true nature of the outcome and in addition, the enormous litigation possible should cause courts to scrutinize carefully the standing problem. For example, in the Northern District of Georgia over 28% of the cases filed in 1974 were Truth in Lending actions, a staggering caseload. Mullinax v. Willett Lincoln-Mercury, Inc., 381 F. Supp. 422, 423-24 (N.D. Ga. 1974). In their haste to avoid creating a new federal bureaucracy, Congress may have overburdened the court system and in effect, made it the bureaucracy that was intended to be avoided. On balance, Congress should at least clarify the standing problem, and specify a minimal interest in the action, perhaps by requiring that the plaintiff at least have paid some finance charges to the defendant before allowing him to bring an action.

debtor can show that disclosure failures caused him to pay more in finance charges than he would have if proper disclosures had been made, he may recover the difference in out-of-pocket costs and also penalty damages based on the amount of finance charges actually paid or incurred. There seems to have been little controversy over this change and its ostensible purpose—to put a debtor in the position he assumed before the wrongful conduct of the creditor harmed him—seems as laudable as the purpose of the punitive damage provision: to encourage compliance through private actions.[127]

A fourth and perhaps the most controversial topic in the amendment package concerns the availability and scope of class actions for Truth-in-Lending enforcement. The Act as originally passed was silent about the availability of class actions in section 130 suits, and this ambiguity was almost immediately tested as consumer advocates sought to "stick the big boys." In *Ratner v. Chemical Bank New York Trust Co.*[128] the court held that Congress did not intend to allow class actions in suits under the Act because of the terrifyingly large potential liability of defendants.[129] One commentator noted that a single class action alone could represent a potential minimum liability of over one billion dollars to defendant, Bank of America.[130] Thus, the main controversy over civil liability class actions concerned not whether such actions would be permitted but what proper limits should be placed upon the punitive recoveries.

The FRB recommended in its 1972 Truth-in-Lending report to Congress that the punitive damage limit be set at the greater of 50,000 dollars or one percent of the creditor's net worth, in addition to actual damages, costs, and attorneys fees. The FRB proposal also recommended that the actual figure be set "in the discretion of the court"

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127. There are few indications of disagreement with this change and apparently failure to provide for recovery of actual damages in the original Act was merely an oversight.

128. 54 F.R.D. 412 (S.D.N.Y. 1972).

129. Briefly, if perhaps too broadly stated, the reasons against maintenance of this as a class action are: (1) there is no affirmative need or justification for such a proceeding in the actual circumstances of the case; (2) the allowance of thousands of minimum recoveries like plaintiff's would carry to an absurd and stultifying extreme the specific and essentially inconsistent remedy Congress prescribed as means of private enforcement.

Id. at 414. Note that at $100.00 per class member, the minimal recovery in this class action would have been 13.2 million dollars and this, despite a highly technical and debatable violation of the Act, induced by an FRB regulation.

130. S. REP. No. 750, 92d Cong., 2d Sess. 8 (1972) (observations of Sen. Byrd).

Most likely for this reason as much as any other, very few class actions have been allowed under the Act.

and specified factors that should be considered in calculating the award.[131] This proposal was changed by the Senate subcommittee to the lesser of 50,000 dollars or two percent of the creditor's net worth.[132] Senator Proxmire, who introduced the original Senate bill, was infuriated by this compromise. He characterized the proposed legislation as the "Bank Protection Act of 1972," doubted if it was worthy of congressional approval, and declined to report it to the Senate. Although deletion of other provisions contributed to his ire, Senator Proxmire believed that setting the class action limits at the lesser of 50,000 dollars or two percent of the net worth of the creditor was too low, although he favored setting some limits on the punitive damage recovery.[133] The measure passed the Senate, but died in a House subcommittee.

Subsequently, two additional measures were introduced in the Senate: Senate Bill 914 by Senator Proxmire and Senate Bill 1630 by Senator Byrd which culminated in a compromise proposal, Senate Bill 2101. Senator Proxmire's proposal would have restored the limits proposed by the FRB: the *greater* of 50,000 dollars or one percent of net worth.[134] Senate Bill 1630 adopted the limits previously accepted in the Senate: the *lesser* of 50,000 dollars or two percent. Senate Bill 2101, on the other hand, raised the dollar limits but set the alternative as the *lesser* of 100,000 dollars or one percent of the creditor's net worth.[135] Again, the compromise proposal passed the Senate and again Senator Proxmire had grave misgivings about the effectiveness of the class action limits.[136] The bill languished in House subcommittee and the identical language was added as a Senate amendment to a House version of the FDIC Act and was eventually enacted. The class action provisions finally approved use the lesser of 100,000 dollars or one percent limits and allow wide discretion at the trial court level in setting the exact amount of recovery for punitive damages, with certain standards to be considered by the court. Actual damages, costs and

131. FRB, 1972 ANNUAL REPORT 31.

132. S. REP. No. 750, 92d Cong., 2d Sess. (1972).

133. *Id.* at 33. Proxmire thought that this would not serve as a proper deterrent to future violators.

134. S. 914, 93d Cong., 1st Sess. (1973).

135. S. 2101, 93d Cong., 1st Sess. (1973). *See* S. REP. No. 278, 93d Cong., 1st Sess. (1973).

136. S. REP. No. 278, 93d Cong., 1st Sess. 35 (1973). Individual views of Mr. Proxmire and Sen. Hathaway: "We support the need for placing a reasonable upper limit on a creditor's class action liability under Truth in Lending. However, we believe the specific limits recommended by the Committee are too low and will not provide a meaningful deterrent against potential violations."

attorneys fees may also be recovered in the class action in addition to punitive damages.[137]

Class actions are now clearly allowed for Truth-in-Lending violations, within limited recovery amounts, if procedural burdens can be overcome.[138] The impact on creditors remains to be seen. It is likely, however, that the class action will spur greater compliance than is envisioned by critics of the amendments despite the low limits, yet will fail to achieve the goal of consumer awareness advocated by original proponents of the disclosure provisions. This could occur, not as a result of any creditor failures, but from shortcomings in the statutory framework of the Act and in its underlying theory.[139]

A fifth change in the scope of section 130, limitation of the right to offset, is somewhat cryptic but seems related to the alteration in class action policy established by the 1974 amendments. New section 130 (h) provides that a debtor may not offset any amount for which a creditor is potentially liable under section 130(a)(2) against any debts owing unless Truth in Lending liability has been determined by a court in a judgment in which the debtor was a party.[140] The intent of this amendment is unclear,[141] and the only significant comment that can be found in the debates is in Senate Report 93-278 to Senate Bill 2101.[142] Apparently, it was feared that a non-named plaintiff in a Truth-in-Lending class action would decide to withhold payment of a debt, assuming that the creditor would be forced to bring a separate action to compel payment of the debt in which the debtor would use the defense of Truth-in-Lending violation and claim an offset. At this point, although the creditor might like to join the individual defendant with the

137. 15 U.S.C.A. § 1640(a) (Supp. I, 1975), *amending* 15 U.S.C. § 1640(a) (1974). See specifically, new § 1640(a)(1), actual damages; § 1640(a)(2)(B), punitive damages for class actions; and § 1640(a)(3), costs and attorneys fees and standards for judicial imposition of class action penalty damages.

138. Such class action problems have been created by Eisen v. Carlisle & Jacquelin, 417 U.S. 156 (1974).

139. *See* discussion at note 23 *supra* indicating that the problem with the Act is not creditor compliance, but consumer awareness.

140. 15 U.S.C.A. § 1640(h) (Supp. I, 1975), *amending* 15 U.S.C. § 1640 (1974).

141. No mention of this section is made in the FRB reports or in the reports accompanying the proposed Senate bills.

142. This somewhat vague comment on the intent of the section is found in the summary of sections rather than in the comments made by the drafters:

> This provision is intended to prevent customers from simply deducting from their obligation to a creditor the minimum $100 award, which is provided for in individual actions without being a party to an action in which such a liability is determined by the court. However, nothing in this section prevents a series of individual civil actions to recover $100 in the case of any violation.

S. REP. No. 278, 92d Cong., 2d Sess. 16 (1972).

class as a named plaintiff, he may have difficulty under the joinder sections of the Federal Rules of Civil Procedure.[143] In addition, if enough debtors withheld payment once a class action was filed, the creditor might be forced to settle without regard to the merits, merely to save his business from economic collapse. Most likely the section was intended to preserve the ability of individual debtors to bring a series of individual actions against a creditor, while at the same time compelling them either to join a pending class action or to file a separate affirmative action for relief. Beyond this there seems to be little justification for new section 130(h).

A sixth major change in section 130 alters two of the original statutory defenses. Section 130(b) provides that a defense is available to creditors who discover errors, correct them, and report the corrections to the obligor, before fifteen days have passed and before the debtor initiates an action under this section.[144] This has been changed to conform with section 130(a) by providing that it is available for failures to comply with any requirement imposed under "this chapter."[145] Thus the section 130(b) defense has been broadened and clearly applies to any asserted violation of Truth-in-Lending requirements, at least with respect to chapter two credit disclosures.[146] Subsection 130 (c), as noted before, establishes the "bona fide error" defense.[147] The defense has been broadened to resist liability determinations for any violation of "Title II"[148] and is now available for Truth-in-Lending suits in actions brought under the new Fair Credit Billing Act (chapter four of the Act).[149]

The resulting pattern of defenses available under section 130 of the Act is so complex that scrutiny of their interaction is warranted. Basically, there are now seven key defenses available to a creditor con-

143. FED. R. CIV. P. 19(a) including the involuntary joinder provisions.

144. 15 U.S.C. § 1640(b) (1970).

145. 15 U.S.C.A. § 1640(b) (Supp. I, 1975), *amending* 15 U.S.C. § 1640(b) (1974).

146. Note, however, that this defense is not available for failures to comply with new Chapter 4 of the Truth in Lending Act, the Fair Credit Billing procedures added by the 1974 amendments, tit. III, 88 Stat. 1500.

147. 15 U.S.C. § 1640(c) (1970).

148. 15 U.S.C.A. § 1640(c) (Supp. I, 1975), *amending* 15 U.S.C. § 1640(c) (1974).

149. Note also, while civil liability clearly attaches only to violations of Chapter 2 (Truth in Lending Disclosures) and Chapter 4 (Fair Credit Billing) it does not attach to Chapter 1 (General Provisions) or Chapter 3 (Credit Advertising). *See* Jordan v. Montgomery Ward & Co., 317 F. Supp. 948 (D. Minn. 1970), *aff'd*, 442 F.2d 78 (8th Cir.), *cert. denied*, 404 U.S. 870 (1971). Should Congress decide to amend the Act again, § 130(c) would continue to apply to any new sections added.

fronted with liability for Truth-in-Lending violations. First, various definitional defenses are available to defendants. The creditor may claim that he is not a "creditor under the Act,"[150] that his operations fall within an exception, or that plaintiff has no standing to assert a Truth-in-Lending violation against him.[151] A second class of defenses can best be categorized as transactional defenses. The defendant may claim that he has disclosed all required information or that such disclosures are not so confusing and misleading as to violate the Act. A third class concerns "clerical errors." If violations are a result of clerical errors, despite procedures maintained to avoid them, there is no question that a valid defense is presented under section 130(c).[152] In addition, some courts have interpreted the provisions of section 130(c) as granting a general reliance or good faith defense and believe that it applies to all unintentional errors if procedures to avoid the errors have been established.[153] A fourth category of defenses relates to assignee liability. These include assertions that the assignment has been involuntary or that the violation is not clear on the face of the assigned instrument.[154] A fifth defense is the "fifteen day" defense under which the creditor can correct errors discovered without incurring liability if notification is made to the debtor before the end of fifteen days and before the debtor initiates an action.[155] A sixth defense is the FRB reliance defense added by section 130(f).[156] This addition, however, is not very broad and there are significant problems concerning scope of coverage in various other defenses.[157] The final category can be described as "limitation defenses" in the class action situations. These are the delineated factors that should mitigate class action liability.[158]

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150. 15 U.S.C.A. § 1602(f) (Supp. I, 1975), *amending* 15 U.S.C. § 1602(f) (1970). Note that this section has been extensively changed by the Fair Credit Billing Title of the 1974 Act.

151. *See* discussion in text accompanying note 126 *supra.*

152. *See* discussion at note 20 *supra.*

153. *Id.*

154. *See* notes 99 to 103 *supra.*

155. *See* notes 144 to 146 *supra.*

156. *See* notes 115 to 119 *supra.*

157. *Id.* Thus § 130(c) and other defenses are still needed when the creditor has not relied specifically on an FRB rule, regulation or interpretation.

158. Note that very little discussion has been directed at the factors suggested by Congress as relevant to setting the punitive damage recoveries in class actions. Under the Act as passed these factors and the weight to be given to each should become extremely important. The statutory list is a good beginning but judicial decision must "flesh-out" these standards to give a creditor some idea of what he is up against. Weight given to certain key factors can encourage or discourage a creditor's willingness to com-

The total "hotch pot" nature of creditor defenses and the differences expressed by courts and observers on the relevant scope of these defenses stem perhaps from a difference in perception of the proper function of civil liability under the Act. It is generally agreed that the basic function of civil liability is to encourage compliance with disclosure provisions of the Act. The original intent of Congress clearly specified that the majority of enforcement activity should occur in this area to avoid expense resulting from establishment and maintenance of

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ply with the Act. Factors entering into the class action liability thus fall into two categories, statutory factors and nonstatutory.

There are five statutory factors that a court must consider in setting the punitive damage limits: First, the extent of the actual damages awarded. As a measure of total harm caused by defendant's Truth in Lending violations, this factor should be given considerable weight by a court confronted with a Truth in Lending violation. Actual harm in this area may extend beyond monetary damages, but this is one factor that is at least easily measured. Second, the frequency and persistence of failures of compliance must be measured. As a factor delving into the element of intent and wilfulness or gross negligence, this factor should be accorded great weight. Third, the number of persons adversely affected. This factor is closely related to the first one discussed above. To the extent that it represents another measure of the degree of harm caused by defendant's conduct, this factor should be given considerable weight. Here the key concept is "adversely." If a rather broad meaning is given to the term in the context of technical and *de minimus* violations, with no real distinction drawn between gross conduct on the part of the creditor and good faith, there will be less incentive for a creditor to comply, when he figures that liability will depend on the fall of the dice rather than upon any factor within his control. Fourth, the resources of the creditor should be given little weight in granting punitive recoveries. The mere fact that a creditor stands in a position to spread the costs of Truth in Lending damages over a wider range of debtors should not be so great a factor as the type of conduct involved and the number of persons harmed. It perhaps could be a factor in lowering the recovery allowed when the creditor is small, but here again, if the conduct is gross and a great number of consumers hurt, this is the kind of entity or individual that Truth in Lending should really hurt. Thus some, but little weight should be given to this factor. Finally, the extent to which defendant's conduct was intentional must be weighed by the court. This factor should be given considerable weight if carefully defined. As a legal term of art, intent has been characterized as an intent to do the act. *See* Ratner v. Chemical Bank New York Trust Co., 329 F. Supp. 270, 281 (S.D.N.Y. 1971). In considering punitive damages in Truth in Lending violations, use of intent in this manner will detract from the purpose of the Act. Intent here should be defined as intent to violate the Act or inflict harm, going to the quality of defendant's acts, rather than looking to any elements of volition.

There are factors which have not been itemized by Congress, but which should have a bearing on the amount of punitive damages set by a court in a class action situation. The first of these nonstatutory standards should be the quality of defendant's conduct. If the deterrent is to be meaningful under § 130 "bad" conduct should be more heavily penalized than "good." A second factor not considered by Congress but which is essential is the extent to which the violation constitutes a key disclosure under the Act (such as the annual percentage rate, or the amount of finance charges) or whether the violation is failure to comply with a *de minimus* or technical requirement of the Act.

In short, the greatest weight in measuring punitive damages in Truth in Lending actions should be given to elements that focus on defendant's conduct and the type of violation which has been found. Thus a valid defense to class action liability should be that under the standards of § 130(a) defendant's conduct indicates that if any recovery is to be provided, that it be as minimal as possible.

a new pervasive federal bureaucracy.[159] Beyond these basic agreements, opinions on the proper scope of the civil liability provisions vary widely. Contributing to this problem is the fact that the defensive provisions of section 130 are so vague and ambiguous that they can mean all things to all people.[160] It is little wonder that the civil liability provisions show a total lack of coherence in providing for administration of the Act. A pressing current need is for Congress or the courts to provide a manageable framework and definition in the area of defenses to Truth-in-Lending civil liability.[161]

F. Administration of the 1974 Amendments

Given the wide reach of Truth-in-Lending changes, it is likely that many problems in implementation will occur. One consideration is the timing of initiation of various provisions of the Act. Two timing provisions are contemplated by the 1974 legislation.

The first of these regulates the changes in the civil liability provisions of the Act. Section 408(e) of the 1974 amendments attempts to apply these changes to legal actions pending at the time of enactment. Specifically, the new section 130 provisions apply to suits in which the right to appeal has not yet lapsed.[162] Congress apparently had little doubt about the validity of retroactive operation, relying upon an analogy to the Bank Merger Act of 1966[163] and its subsequent vindication by the courts.[164] The constitutional validity of retroactivity will have to be determined and this issue is certain to hinge upon whether or not the amendments attempt to change existing rights or influence court litigation or are mere indications of prior congressional intent. It seems clear that the crux of this determination should focus on the *scope* of the amendments. The new Act provides for recovery of actual damages for the first time and allows class actions. Arguably, these provisions are new and can represent an attempted interference by Congress in pending controversies. Alternatively, it can be asserted that the enactments are mere clarifications and therefore can constitutionally be applied to current cases.

Assuming the constitutional validity of the section 130 timing provision, a second problem is raised by "revival" of class actions in the

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159. *See* note 4 *supra.*
160. *See* discussion at note 20 *supra.*
161. However, the most pressing need is a consideration of consumer education.
162. 15 U.S.C.A. § 1640 note (Supp. I, 1975).
163. 12 U.S.C. § 1828 (1970).
164. United States v. Third Nat'l Bank, 390 U.S. 171 (1968). *See* S. REP. No. 278, 93d Cong., 1st Sess. 15-16 (1973).

1974 amendments. Many pending Truth-in-Lending suits were originally filed as both individual and class actions. Most of the class actions were dismissed and litigation proceeded on the merits of the individual action. If such a case is currently pending, does section 408(e) revive the class action portion of the dispute? The language of this section would revive the class action unless it has been "determined [dismissed] by final judgment of a court of competent jurisdiction and no further review of such judgment may be had by appeal or otherwise."[165] In short, if the dismissal and appeal are final, no revival will occur; but if dismissal of the class action is still subject to appeal, then the class action portion of the suit may be revived. In such cases the issue should become the proper time for appeal of the class action dismissal when the individual action was retained for adjudication. Generally, the proper time for appeal depends on the finality of an order dismissing the class action portion of the suit.[166] If the dismissal were a final order, the time for appeal most likely has passed. This depends in part upon the unconditional or conditional nature of the order of dismissal.[167] Presumably, if the class action dismissal is unconditional, it can be appealed as a final order.[168] However, in actual practice, the finality of such a determination is probably rare. The Federal Rules specifically deal with finality when parts of an action or some of the parties therein are dismissed while others remain.[169] Although class determinations can be final before resolution of an individual action on the merits, they are usually appealed at the same time as appeals from determinations on the individual merits.[170] Consequently, for many Truth-in-Lending actions currently proceeding on the individual merits (in which the potential liability of a defendant has likely been narrowed) after the dismissal of a class action count, there is a substantial

165. 15 U.S.C.A. § 1640 note (Supp. I, 1975).

166. 28 U.S.C. § 1291 (1971).

167. FED. R. CIV. P. 23(c)(1) provides that dismissals of class actions may be conditional or unconditional.

168. 28 U.S.C. § 1291 (1971) establishes the final order requirements.

169. Note that such procedure depends on certain steps taken by the trial judge in such a class determination. Under the Federal Rules, when multiple parties are involved, the court may direct entry of judgment as to one or more, but fewer than all of them if: First, there is an express determination that there is no justifiable reason for delay and second, the trial court makes an express direction for entry of judgment. FED. R. CIV. P. 54(b). Until such action is taken, a partial disposition of the case is not a final order. *See* C. WRIGHT, LAW OF THE FEDERAL COURTS 454-55 (1968, Supp. 1972).

170. Note also that the Second Circuit has held more specifically that an order striking the class action portion of a suit may be appealed only if it is "the death-knell of the action." *See, e.g.*, Korn v. Franchard Corp., 443 F.2d 1301 (2d Cir. 1971) and Weingartner v. Union Oil Co., 431 F.2d 26 (9th Cir. 1970), *cert. denied*, 400 U.S. 1000 (1971).

likelihood that the class may be reinstated under the present limits of section 130(a) unless section 408(e) is found to be unconstitutional or the order dismissing the action is found to have been final under rule 54(b).

A second timing rule imposed by Congress in the 1974 legislation concerns the effective date of the other amendments. But for two exceptions the amendments are effective immediately upon enactment—October 28, 1974. The two exceptions are section 409 and section 411 which regulate the disclosure of closing cost information and the identification of specific transactions on the monthly billing statement.[171] Since these additions call for some modifications in present forms and billing operations and require FRB regulation, Congress has given one year from the date of enactment to implement them—October 28, 1975. This seems fair, however; if substantial FRB regulations are to be adopted the preparation period is none too long.

III. CONCLUSION

Truth in Lending apparently is not working as well as it should. Is it then, as some studies indicate, a failure? Not necessarily. But Congress will have to take some bold steps to make the basic theory workable. This could take the form of at least three steps.

The first step could be establishment of a consumer protection agency. This idea is not new and will not be developed at length here; but thought should be given to transferring enforcement and policy making functions under the Truth in Lending Act to such an agency,[172] perhaps including the exclusive right to maintain class actions. Part of the private class action recoveries could go to the government to fund such an agency.[173] As an adjunct to this, a useful provision might impose a fifty percent tax on attorneys fees recovered in the same class action for the same fund. This would deter strike suits by attorneys with delusions of enrichment.

A second necessary step in improving the Truth in Lending Act would be to provide clear and effective defenses for creditors who validly attempt to comply with the Act, but for some "non-negligent" reason are unable to do so. Congress should provide rewards for good faith attempts to comply as well as penalizing violators. If a creditor

171. 15 U.S.C.A. § 1665a note (Supp. I, 1975).
172. See H.R. 1183, 94th Cong., 1st Sess. (1975) for a recent proposal.
173. Comment, *From Nam to Qui Tam, Truth in Lending Class Action Developments,* 24 HASTINGS L.J. 813 (1973).

realizes that he can obtain a return on his compliance investment (for example, on the money spent to hire attorneys and to revise credit disclosures) by being vindicated in a law suit, he may more readily undertake voluntary and more effective steps to comply with the Act. On the other hand, if he is thrown into the same bag as creditors who intentionally attempt to evade the Act whenever a minor technical violation is found, there will be little incentive for him to devote maximum efforts toward compliance.

Thirdly, and most importantly, consumer education is the crux of Truth in Lending. Congress must take effective steps to develop an awareness of how credit works, what "annual percentage rate" means, what the free ride period connotes, what differences can result merely from the method by which a creditor applies the annual percentage rate to a particular balance, and most important, that there are wide differences in the credit plans available to consumers. Although many other groups have realized that education is the key ingredient to Truth in Lending success,[174] Congress has devoted most of its time and energy to programs that make credit more expensive for the creditor to offer and so complex as to constitute nearly a relief act for attorneys. A simplistic program, such as an FTC developed television advertising campaign, would probably do more good than all of the 1974 amendments combined. In addition, every high school curriculum should include credit education as part of the course offering.[175]

Finally, Congress should provide funding for more empirical studies of Truth in Lending. Rather than dealing in generalities, figures should be available when considering credit conduct regulation comparing the potential costs of compliance to creditors (which will be passed on to consumers) with the benefits to consumers. In short, Congress needs to become more aware of the potential impact of proposed credit regulation.

Credit has developed into a key American industry with all of the connotations of gigantic growth that plagued the nation during massive growth of other industries. Disclosure regulation can be a viable alternative to permeating control of the credit industry if it is carefully refined in a studied manner, avoiding the regulatory mistakes of the past.

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174. *See* note 29 *supra.*
175. Apparently many schools are now doing just this. *See* note 29 *supra.*