HB 174

HB 174

Statement by the AFL-CIO Executive Council

on

The Uniform Consumer Credit Code

Bal Harbour, Florida
February 17, 1969

We have carefully examined the Uniform Consumer Credit Code, a "model state law" which has been prepared for introduction in the 47 state legislatures meeting in 1969.

UCCC would repeal and replace virtually all existing state laws relating to consumer credit. Sponsored by the National Conference of Commissioners on Uniform State Laws, it is offered for adoption as a "package," without amendment. The sponsors urge immediate enactment, despite the fact that the Code is a lengthy, complex, and sweeping legislative proposal. The public has had little opportunity to evaluate either its general impact or its specific provisions.

The Code is not essentially a "consumer statute" but seeks to compromise consumer and creditor interests. While it would make a number of desirable reforms in behalf of the consumer, which should be supported, it also contains serious drawbacks from a consumer point of view.

For this reason we cannot endorse the Code in its present form for enactment as a uniform law throughout the United States.

Our principal objections are as follows:

(1) We are shocked by the extraordinarily high finance charge ceilings authorized by the Code, ranging from 18 to 36 percent per year for installment loans and credit, and believe that they would inevitably result in exhorbitantly high credit costs for borrowers and credit buyers.

(2) We cannot concur in the excessive rate of 10 percent per year, which would be permitted on first mortgages.

(3) We are dissatisfied with the provisions on wage garnishment which could, if care is not taken, result in reduction of existing protections for wage earners in a number of states. We cannot in any case endorse a "take" by creditors as high as 25 percent of a person's wages.

(4) We are alarmed at the general repeal contemplated by the Code of present state consumer credit legislation regardless of whether it is superior to Code provisions or covers subjects not covered in the Code.

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The possible impact of Code enactment would vary in each of the 50 states. Each state will need to make a careful assessment of its existing legislation in comparison with Code provisions.

In states with a large body of existing legislation, state AFL-CIO central bodies will probably find it best to reject the Code and instead seek improvements in their present laws, borrowing good features from the Code where appropriate.

In states with little or very deficient legislation, state central bodies may find it advisable to start with the Code as a working basis, but should seek amendment of its worst features.

In any case, precipitous enactment of the Code on an "as is" package basis should be rejected, as well as deviant forms, containing even worse features, which are likely to be introduced in some of the legislatures.

At the national level, the AFL-CIO staff will render whatever assistance it can to state bodies in connection with UCCC. We will also pursue abatement of consumer credit evils through federal legislation, wherever it is possible and appropriate. The door should not be shut on consumer credit reform through federal action. Enactment of federal minimum standards in the consumer credit field may in fact be necessary to reach the states in which reform is most needed and where creditor lobbies are most likely to succeed in blocking it.

BACKGROUND STATEMENT
ON
UNIFORM CONSUMER CREDIT CODE

The Uniform Consumer Credit Code (UCCC) is a type of "model state law" developed by the National Conference of Commissioners on Uniform State Laws. It was officially promulgated by the Conference on July 30, 1968, and subsequently endorsed, on August 7, 1968, by the American Bar Association. The Code has been in process since 1964, although much of the final text was prepared in 1968 to take account of the Federal Consumer Credit Protection Act, which was signed by the President on May 29, 1968.

Since the original text was released, the Code has undergone additional revisions. The current version of the Code is the "Revised Final Draft, November 1968," published in December 1968.

UCCC is designed as a replacement for virtually all existing state laws relating to consumer credit. Present laws on such provisions as maximum finance charge rates, (including usury rates), disclosure, licensing, administration and enforcement would be repealed. The one major exception to general repeal would be in the case of "supervised financial institutions" -- such as banks, savings and loan associations, and credit unions -- which receive deposits as well as make loans, although the new rate structure would apply to them as well as to other creditors.

Because the Code is designed as a uniform law, to be enacted in the same form in every state, it is offered as a "package" for adoption in its entirety, without amendment. Code sponsors are seeking blanket endorsement of the Code, regardless of any deficiencies and drawbacks.

The Code was not developed as a "consumer statute," as such, but rather seeks a "balance" of consumer and creditor interests. The principal "trade-off" appears to be in the form of high finance charges for creditors in exchange for restrictions on some of the more bloodthirsty techniques by which creditors can enforce repayment of debts plus more comprehensive enforcement procedures than now apply under many types of credit statutes.

Present indications are that the compromise is unlikely to be satisfactory to all groups. The Code has drawn support from various segments of the credit industry, but coldness from others (notably the American Bankers Association). No known support has come from consumer groups. The major exception in the consumer community was an endorsement by the Special Assistant to the President for Consumer Affairs and the President's Committee on Consumer Interests. But the Code has come under heavy fire from the Consumer Federation of America, representing 136 consumer-oriented organizations. To date it has been opposed by at least three important state consumer organizations -- the Association of California Consumers, the Consumers League of New Jersey, and the Pennsylvania League for Consumer Protection -- as well as by the Massachusetts Consumers' Council, an official consumer representation body.

Although Code sponsors have sought immediate, wholesale endorsements of their work, and immediate enactment in the 47 state legislatures meeting in 1969, the general public has had little time to gain an understanding of the

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Code or to develop knowledgeable criticism. The possible impacts would, of course, vary in each of the separate 50 states. Study and criticism will be a continuing process, and common sense dictates a rejection of precipitous enactment.

For states which already have a large body of consumer credit legislation, covering both cash loans and retail sales credit, enactment of UCCC may represent little if any gain in consumer protections and in fact is more likely to result in a net loss. Such states should be extremely critical of UCCC and probably will find it best to reject the Code altogether in favor of continuing improvements in their existing statutes.

On the other hand, states with little or very deficient consumer credit legislation could find that UCCC represents a net gain, in the sense that almost anything would be better than what they have. Even in such situations, a cautious approach is advisable. As indicated in the more detailed comments that follow, finance charge ceilings authorized under UCCC are extraordinarily high for types of credit other than for small loans, and the Code has other drawbacks.

Clearly, an important motivation for urging speedy enactment is the hope of forestalling further federal action in the field of consumer credit. An immediate and announced goal of the Conference is to gain exemptions of state credit laws from applicable provisions of the newly enacted federal Consumer Credit Protection Act. Under the federal law, state laws with "substantially similar" provisions may be exempted from federal requirements for disclosure of the cost of consumer credit and from federal requirements limiting the amount of wages that may be garnished. Further possibilities of federal entry into the consumer credit field could come out of the prospective study by the newly authorized National Commission on Consumer Finance which was set up by the Consumer Credit Protection Act with instructions to make a study and recommendations by January 1, 1971. Also specific federal bills may be expected in the field of credit insurance and in door-to-door credit sales, at a minimum.

MAJOR POINTS ABOUT THE UNIFORM CONSUMER CREDIT CODE

Maximum Charges

1. The Code repeals all existing laws setting maximum rates on consumer loans from banks, credit unions, small loan companies and repeals general usury rate statutes (important primarily in mortgage lending). Maximum rates for retail sales are also repealed including finance charge ceilings set for automobiles, for general retail sales, home repair services and for revolving credit. Existing finance charge ceilings for most creditors would be replaced by uniform ceilings patterned on existing rates for small loan companies, the highest-rate legal lenders in the credit market. In effect, the small loan company rates would become an "umbrella" for all creditors, both for cash loans and for sales credit. The new ceilings would thus raise the legally permitted rates of charge for most creditors in most states.

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For most types of consumer credit, except first mortgages, the effective ceilings would be 36% on the first $300, 21% on the next $700 and 15% on the remainder over $1,000. Ceilings on store revolving credit are set at 24% on the first $500 and 18 percent on the remainder. (See Attachment I for more detailed outline.)

2. Over and above the maximum rate ceilings, the Code permits additional charges for official fees and taxes, and for insurance -- property, liability, credit life, and credit accident and disability. These provisions follow the lines of the Federal Consumer Credit Protection Act, which defines "finance charge" in such a way as to permit their exclusion from the finance charge for disclosure purposes. A number of current small loan laws require the lender to include most of these charges in the finance charge, although extra charges for credit life insurance are now generally permitted. The "additional charge" system provides an additional source of revenue to creditors, since the "extras" can be included in the amount of the loan or credit and a finance charge computed on top of them.

3. In addition to charges for official fees, taxes, and insurance, the Code allows "extras" for "other benefits." This provision, although presented as being in conformity with the federal act, actually opens up what could be a dangerous loophole for "tie-in" charges and purchases to be required by the creditor as a condition of extending credit. The Code nowhere makes a flat prohibition of "tie-in" sales, except for limitations on compulsory purchase of various types of insurance.

4. The Code properly requires that a rebate of finance charges be made to the credit buyer or borrower who pays off the credit balance in advance. The rebate is calculated according to the "Rule of 78". Unfortunately, where graduated rate ceilings are used, as under the Uniform Consumer Credit Code, the Rule of 78 provides the creditor with a windfall of unearned credit charges and a corresponding shortfall to the consumer. The "Revised Final Draft" attempts to deal with the problem, not by eliminating the windfall, but by authorizing alternative calculation of the finance charges in such a way as to "legitimize" the windfall. This point will require more analysis and explanation, but some idea of the problem can be obtained by the summary comparisons shown in Attachment II, based on tables appearing in the explanatory text ("Official Comment") of the Code.

Insurance

UCCC insurance provisions are written within the framework of the Model Credit Insurance Act developed by the National Association of Insurance Commissioners and now in effect in a number of states. Although some of the more disreputable creditor practices in the sale of credit insurance are prohibited, UCCC does nothing to deal with fundamental problems of overcharges for credit, life, accident and health policies documented by the Senate Antitrust and Monopoly Subcommittee in its 1967 investigative hearings. These hearings disclosed widespread profiteering by creditors on the sale of high-priced insurance, paid for in its entirety by borrowers.

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Kickbacks, commissions, and rebates from insurance companies and creditor-owned insurance subsidiaries have built a system of "reverse competition" encouraging the sale of insurance at highest possible rates. UCCC forbids charges beyond the legal maximums permitted by the Commissioner of Insurance but does nothing to reduce them further. Lenders' profits on insurance are specifically protected.

Disclosure Provisions

The sections on disclosure are largely a duplicate of the provisions of the Federal law which contains extensive requirements relating to items of cost of the credit provided, including a statement of the annual percentage rate. Both credit contracts and credit advertising are covered. The principal problem about the disclosure provisions is that since all existing state legislation on disclosure is repealed, any disclosure requirements other than the ones copied from the federal law would disappear. Disclosure statutes may, for example, require disclosure of a buyer's rights under the law, make detailed specifications as to contract forms, or other matters. In effect the federal specifications would substitute for existing requirements rather than add to them. In addition, the disclosure provisions could be rendered ineffective by the fact that specific administrative authority for issuing regulations to interpret the disclosure requirements in the Code is not provided. In particular, the decision as to what is "conspicuous" is left to the courts for determination, on a case by case basis.

Restrictions on Contract Provisions

1. Credit Sales

The UCCC makes a commendable attempt to prohibit or restrain certain types of contracts and contract provisions which are notoriously unfair to credit buyers, but it does not go "all the way."

a. Holder in Due Course

The Code knocks a hole in the onerous "holder-in-due course" doctrine under which a finance company which has bought a credit contract from a retailer is held free of all responsibility to the original buyer and is legally entitled to collect monthly payments from the debtor, regardless of fraud in the original contract, overcharges, defects in the product or other failure in the seller's duties.

The Code would prohibit sellers from taking a "negotiable instrument" in connection with consumer credit contracts. A subsequent buyer of the paper (the "holder") would not qualify for "holder in due course" status if he had notice of the seller's violation. However, no provision is made for labeling consumer paper as such and no penalties attach to the "holder" even he does take paper illegally procured by the seller.

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The Code also invalidates agreements whereby the borrower waives his legal defenses against a subsequent holder ("assignee") of a credit contract. Two Alternatives are provided. Alternative A, which subjects assignees to buyer's defenses, is definitely superior to Alternative B, which requires notice by buyer to assignee of defenses within three months. Even under Alternative A, certain limitations are placed on the liability of the assignee.

b. Balloon Contracts

The Code discourages the writing of "balloon contracts," but does not prohibit them. It merely specifies that the buyer shall have the right to refinance a balloon payment "without penalty" in any case where the balloon is more than twice the average of earlier scheduled payments. Current state laws that deal with balloon payments usually prohibit them.

c. Security for Contract

The Code makes certain restrictions on the security that may be taken in a credit sale. In general the seller may not take a security interest in property of the debtor other than in the goods which are the subject of sale. Exceptions are allowed to permit a security interest in goods on which services are performed or in which goods sold are installed. Also a security interest in land may be taken if goods are affixed to it or improvement services performed on it. The debt must be at least $300 in the case of security interest in goods and at least $1,000 in the case of a security interest in land. These provisions are definitely a step in the right direction, but the $300 and $1,000 limits have been criticized as too low.

d. Add-on Sales

The Code reforms but does not eliminate "add-on" sales whereby a buyer's current purchases are permitted to be taken as security for earlier purchases on which payments have not yet been completed, and vice-versa (earlier purchases become security for later purchases). Situations have occurred in which default on the most recent purchase have occasioned loss to the buyer of the entire set of purchases. The Code provides that a buyer's payments must be allocated to the goods in the order which they were bought and the security interest terminated in each item as the debt on each is paid off.

A question remains as to whether "add-on" sales should be prohibited in their entirety. A consideration against such prohibition in the Code as presently written is that multiple separate sales could result in multiple high-charge contracts under the graduated rate structure.

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e. Wage Assignments

UCCC prohibits wage assignments, as do a number of existing state laws. This is a desirable reform. A wage assignment is an agreement which provides that the creditor can take part of a worker's wages directly from his employer if the debt is not repaid when due. Under UCCC an assignment of earnings may not be taken unless the employee is free to revoke his authorization of the assignment.

f. Referral Sales

Referral sales are prohibited. A desirable reform. Referral selling is a racket whereby the buyer is persuaded to sign a contract by a promise that he can recoup the purchase price in whole or in part by supplying other customers to the seller.

g. Attorney's Fees

Two alternatives are provided: (A) prohibits agreements providing for payment of attorney's fees by the borrower and (B) limits attorney's fees to 15 percent of the unpaid balance. Alternative (A) is clearly superior, particularly since "reasonable expenses" are allowed to the creditor in realizing on his security interest in case of the borrower's default.

h. Confession of Judgment

This is prohibited. A desirable and important reform. A debtor who "confesses judgment" signs away his legal rights to challenge the validity of the debt.

i. Blank Spaces and Contract Accelerations

Two notable omissions in the Code are (1) the failure to prohibit blank spaces in contracts (a common requirement under existing state legislation) a source of easy fraud on the debtor (2) the failure to curb the creditor's unrestricted right to require immediate payment of the unpaid balance of the debt thereby precipitating a debtor's default. Unilateral acceleration by the creditor should be restricted to cases in which substantial default has actually occurred.

2. Loans

Restrictions on loan agreements are less extensive than those for sales. Provisions on balloon payments, wage assignments, attorney's fees, and confessions of judgment are the same. But no restraints are put upon the rights of holders in due course or on rights of assignees. "Supervised lenders" (licensed lenders and supervised financial institutions) may not

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take a security interest in land unless the debt is over $1,000 but other lenders may do so. Again, the $1,000 cut-off has been criticized as too low.

Restrictions on Creditor Collection Practices

1. Deficiency Judgments

The UCCC makes a limited attack on deficiency judgments. It provides that a seller who repossesses or takes back goods that were the subject of sale (or other security for the debt) may not also obtain payment for the "deficiency" between what the goods sell for and the unpaid balance of the debt. However, this provision applies only where the cash price of the sale was $1,000 or less, thus being of no effect for larger purchases such as new cars. No restraint on deficiency judgments applies in the case of cash lenders.

2. Wage Garnishment

UCCC would restrict garnishment along the lines of the Federal Consumer Credit Protection Act which limits garnishment to 25% of disposable earnings or the excess over $48 per week (30 times the federal minimum hourly wage) whichever is less. In UCCC the minimum exemption is improved to $64 (40 times the minimum wage), but the 25% figure remains unchanged.

In addition UCCC would prohibit garnishment before judgment and would prohibit employers from firing workers on account of garnishment. Federal law forbids firing on account of garnishment for "any one indebtedness" and makes no special provision for garnishment before judgment.

The principal immediate problem presented by UCCC is whether its 25% limit and basic exemption amount would replace more favorable provisions under a number of existing state laws, for example, laws which provide a 10% limit or which do not permit garnishment at all. A "savings clause" is included in the Federal statute for such situations, but not in the text of the Code.

In the most recent published edition of the Code (Revised Final Draft, November 1968) the "Official Comment" has been rewritten to disclaim any intent to undercut existing laws which provide additional protections to wage-earners. However, the fact remains that the statutory language does not in itself accomplish this result.

A further technical difficulty presented by the Code is that its garnishment provisions cover only situations in which the garnishment has arisen out of a transaction covered by the Code (generally, debt characterized either by installment repayments or by the imposition of a finance charge). Garnishment arising out of debt not covered by the Code, such as service credit (doctor bills and utility bills), would not be affected.

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Even assuming the most favorable interpretations of the Code, only modest improvement is made over the Federal provisions which will go into effect July 1, 1970. More comprehensive action on garnishment is needed, either to abolish garnishment altogether, or to severely restrict its application.

Contract Cancellation Rights

UCCC includes a section on 'home solicitation sales" giving buyers a three day period in which to cancel a credit contract for goods or services bought from a door-to-door salesman.

The objective of this provision is obviously desirable, but specific points will need to be examined for possible improvements. The provision for a 5% cancellation fee has been particularly criticized.

An additional section, relating to buyer's cancellation rights in the case of a credit sale or loan secured by the buyer's home, is incorporated from the Federal Consumer Credit Protection Act.

Administration and Enforcement

Administration and enforcement is centered in a single Administrator who is given fairly impressive powers in the form of authority to issue "cease and desist" orders, to obtain injunctions and temporary injunctions from the courts, to bring suit for civil penalties, and to recover overcharges in behalf of debtors. Debtors are also given certain rights of bringing private suits.

Licensing requirements are included for all "supervised lenders" and their assignees (i.e., lenders who charge more than 18 percent per year on loans). These provisions would cover lenders presently licensed under state small loan laws and could have the effect of requiring licensing of at least some high rate lenders in the second mortgage market. Licensing provisions are considerably less stringent than those usually applicable to small loan licensees under much existing legislation. No license would be required for lenders charging less than 18 percent per year.

No licensing is required in the credit sales field, either for retailers or for sales finance companies which buy their paper. They are subject only to registration requirements. A number of states currently have licensing requirements for sales finance companies, and in some states retail dealers (especially automobile dealers) must be licensed for credit operations. These laws would be repealed by UCCC. Licensing requirements involve important powers to suspend or revoke the license of an enterprise to continue in business and can provide an important protection against shady operators in the credit field, as well as in securing general compliance with the law.

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Apparently the main weapon in the Code against shady operators in the credit sales field would be recourse by the Administrator to the courts for an injunction against "unconscionable" conduct.

Another notable omission is rule-making power for the Administrator. He is prohibited from issuing regulations except where specifically authorized by the Code to do so. (These relatively few authorizations are nowhere summed up in a list.) It is evidently intended that the Administrator may issue regulations to correspond to those which will be issued by the Federal Reserve Board, assuming the state were to be exempted from the operation of the federal statute with respect to disclosure requirements. However, rule-making powers in the section of the Code dealing with disclosure do not appear sufficient to accomplish this result.

February 7, 1969
AFL-CIO Department of Research/Draper

ATTACHMENT I

FINANCE CHARGE CEILINGS UNDER UNIFORM CONSUMER CREDIT CODE

1. For retail sellers

Installment credit: *
36% on first $300
21% on next $700
15% on excess over $1,000

Revolving credit:
2% per month on first $500 (24% per year)
1½% per month on excess over $500 (18% per year)

2. For licensed lenders and supervised financial institutions
(small loan companies, finance companies, commercial and industrial loan banks, credit unions)

Loans and revolving loan accounts*

36% on first $300
21% on next $700
15% on excess over $1,000

3. Other lenders

a. 18% per year

b. Mortgage loans are exempt from certain key provisions of the Code if finance charge is 10% or less. This is intended to result in an effective ceiling of 10% on first mortgages.

*Alternatively, a rate of 18% is authorized if the yield would be larger.

Note: The Code further provides for an escalation of effective ceilings in accordance with rises in the Consumer Price Index. This is done through increasing the sizes of the loan to which the higher rates apply. For example, if the CPI increased by 10%, the $300 to which the 36% rate applies would go to $330 and the 21% rate would apply up to $1,100 instead of $1,000.

Attachment II

CREDITOR'S EARNED INTEREST CHARGES ON LOAN
OF $1500

Month No.	Normal Computation 1/	Rule of 78 2/	Alternative Permitted in Revised Final Draft 3/
1	$ 27.50	$ 32.66	$ 31.38
2	26.06	29.85	29.05
3	24.60	27.14	26.67
4	23.13	24.43	24.25
5	21.63	21.72	21.77
6	19.67	18.99	19.24
7	17.52	16.28	16.66
8	15.33	13.57	14.03
9	13.10	10.86	11.34
10	10.83	8.15	8.59
11	8.19	5.42	5.79
12	4.12	2.71	2.91
Total	$ 211.68	$ 211.68	$ 211.68

Rebate due if loan is paid off after 5 months (the addition of charges for months 6-12):

(1) Normal computation: $ 88.76
(2) Rule of 78: 75.98
(3) Alternative under Revised Draft: 78.56

1/ Based on month by month application of 36% per year on first $300, 21% on next $700, and 15% on balance over $1,000

2/ Based on distribution of total finance charge according to Rule of 78

3/ Based on recasting of charges at flat annual rate of 25.10 percent, corresponding to 36% on first $300, 21% on next $700, and 15% on balance over $1,000

A SUMMARY

OF THE

UNIFORM CONSUMER CREDIT CODE

PREPARED BY
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The National Conference of Commissioners on Uniform State Laws is an organization of state appointed officials who are practicing lawyers, judges and law school professors. Customarily the governor of each state appoints three men to serve as Commissioners. The Commissioners serve without compensation. The expenses of the Conference are paid from appropriations made by the states, and when special projects are undertaken, foundations and interested groups often make contributions. The function of the Conference is to draft legislation in areas of the law where uniformity among the states is particularly desirable and offer it to the states for enactment.

THE PROBLEM

Consumer credit is treated under a variety of laws in each state today. Historically, a type of statute that has dominated the growth of consumer credit has been the simple general usury statute. These statutes, originating in this country as early as 1664, set flat 6% and 8% per annum ceilings on the rate of interest that may be charged for loans of money. In the twentieth century these ceiling rates have been unevenly increased in some states so that today the ceiling rates range from 6% to 12% per annum with one state having a 16% ceiling, one state a 21% ceiling and two states none at all. The 6% to 12% rates are below those at which legitimate creditors can extend many kinds of consumer credit. As a result, many exceptions and exemptions from usury laws have been created by courts and legislatures. In most states today general usury statutes cover only a small portion of consumer credit transactions, and this coverage is highly erratic and generally unreasoned.

Exceptions to usury statutes have come from both the courts and the legislatures. The so-called "Time Price" doctrine developed by the courts exempts from general usury statutes all sales credit purchases. This doctrine creates an enormous exception to usury statutes and is recognized in all but two of the states.

State legislatures have recognized the distinction between credit sales and direct loans and have enacted many laws regulating credit sales. Often there is one law regulating credit sales of motor vehicles, and another regulating credit sales of goods other than motor vehicles. Sometimes there are additional laws governing home improvement sales, revolving store charge accounts, and insurance premium financing. Generally these laws are limited to consumer transactions, but occasionally they have broader application. Not infrequently these laws provide different ceilings on rates that can be charged, and express the rate ceilings differently (add-on, discount, U.S. Rule, per cent per month, etc.). Often these laws treat substantially similar aspects of different credit transactions differently where no reason for the difference in treatment exists.

In addition to the exemption from usury laws for sales credit, state legislatures have enacted a number of laws permitting loans to be made at rates in excess of the usury rate. Most common are the Small Loan Laws which require the lender to be licensed and limit both the amount and length of the loan. In addition to the Small Loan Laws, many states have enacted so-called Installment Loan Laws, Industrial Loan Laws and other laws exempting from general usury statutes certain classes of lenders such as commercial banks, credit unions and savings and loan associations or a certain class of transactions such as revolving loan accounts. These laws also frequently set different rules for what are very similar aspects of the various transactions.

Finally, some states have enacted laws dealing with specific aspects of consumer credit transactions such as door-to-door sales cancellation acts, rate disclosure (truth-in-lending) acts and so forth.

Compounding the problem of the numerous laws governing the consumer credit market is the new Federal Truth-in-Lending Act which is effective July 1, 1969. It requires full disclosure of the terms of substantially all consumer credit transactions including, among other things, the rate of the credit service or loan finance charge stated in terms of an annual percentage. This law provides that if a state passes a law which requires substantially similar disclosure, the state law will apply and the control will move back from the federal to the state government.

THE UNIFORM CONSUMER CREDIT CODE — GENERALLY

The Uniform Consumer Credit Code is a balanced consumer protection law. It restructures all laws imposing maximum charges on the cost of money or credit, regulates consumer credit generally and brings substantially all consumer credit transactions under one comprehensive code. In the area of maximum charges and rate ceilings it imposes a single and standard set of maximum charges on substantially all types of consumer credit and, except in the case of extortionate charges, frees substantially all types of business credit from any maximum charge or rate ceiling. It puts all creditors extending consumer credit on substantially an equal footing so far as maximum charges and control of practices are concerned. It stimulates competition by eliminating artificial barriers to entry into the credit granting business and by requiring disclosure of the cost of the credit, both in terms of the dollar amount and in terms of an annual percentage rate. While the Uniform Consumer Credit Code sets *maximum ceilings* on rates which may be charged in consumer transactions, it relies on competition to *fix actual effective rates*. It restricts certain practices of creditors which have been shown to be particularly subject to abuse and has broad provisions to eliminate unconscionable conduct.

It is designed to secure for any state enacting it exemption from the Federal Truth-in-Lending Act.

COVERAGE

Generally, the Code applies to consumer credit transactions and excludes business transactions. The basic test is the kind of debtor involved. If the debtor is an individual, some or all of the provisions of the Code apply. If the debtor is an organization, (a corporation, partnership, trust, governmental body or the like), with one minor exception regulatory and maximum rate provisions of the Code do not apply. The non-application of the Code to organizations eliminates the major portion of all business credit from regulatory coverage.

If an individual debtor (sometimes called a sole proprietor) seeks not in excess of $25,000 of credit for a business purpose, the transaction will be covered only by the provisions of the Code relating to maximum rates and charges which can be made. In other words, the sole proprietor of a corner grocery is given maximum rate protection under the Code in transactions up to $25,000 but otherwise the transaction is unregulated.

The major concern of the Code is with consumer credit and except for the provisions on rates and maximum charges having limited applicability to non-consumer transactions, all of the Code's provisions apply only to consumer credit. Consumer credit includes and is limited to credit extended for the personal, family, household or agricultural purpose of the person to whom credit is extended.

Credit extended for agricultural purposes is included in consumer credit, but it is excluded from a number of the substantive provisions found to be unsuited to the particular characteristics of farm financing. Of course, if the debtor is not an individual, regulatory provisions of the Code do not apply.

Credit sales of homes and home mortgages entered into for a consumer purpose are covered by the maximum rate and charge limitations as well as the disclosure requirements of the Code. Transactions in which the rate of credit service or loan finance charge exceeds 10%, calculated as prescribed in the Code, are subject to all of the substantive provisions of the Code.

REGULATION OF PRACTICES

The Code takes three basic approaches to the problem of better enabling the consumer to deal with the professional creditor. First, it requires full disclosure of the cost of credit to the consumer prior to or at the time the transaction is entered into. Second, it makes illegal or severely limits certain specific practices of creditors which have been shown to be subject to abuse. Finally, it has broad provisions for attacking and eliminating unconscionable conduct.

The first approach is the requirement of complete disclosure of the terms of the credit transaction including disclosure of the cost to the debtor both in dollar amounts and in terms of an annual percentage rate. The disclosure provisions are more fully discussed below.

The second approach is to prohibit or greatly limit certain kinds of agreements and practices. In deciding what practices to prohibit or limit, the Commissioners recognized that unless there were very real and corresponding benefits to the consumer, restrictions on rights of creditors could, in fact, hurt consumers because the restrictions might result in higher costs and consequently higher rates throughout the consumer credit market. With this process of evaluating and balancing in mind, the Commissioners sought only to restrict rights and practices in which evidence of serious abuse of consumers was strong.

Among the specific restrictions the Code imposes is the prohibition of negotiable promissory notes in sales credit transactions. Closely related to this is the treatment of the buyer's waiving as to an assignee of the consumer's contract any defenses he might have against the seller. The Code offers alternative sections, either of which might be enacted. The first alternative prohibits and renders non-effective the buyer's waiving his defenses. The second alternative requires the buyer promptly to inform the assignee of any defenses which arise within three months of the sale and if he fails to do so, the assignee is freed from defenses arising during the three month period. Under the present law of most states, once the contract is assigned, the buyer must pay the finance company and try to seek his remedy from the seller. The theory of the Code's provision is that the financing institution is in a better position to guard against the seller pushing shoddy and sub-standard goods or services than the buyer who very likely has only a single isolated transaction with the seller.

Another practice the Code prohibits in sales credit transactions is the seeking of a deficiency judgment after goods have been repossessed if the original cash price of the goods was less than $1,000. In effect, where the cash price is less than $1,000, the Code provides that the creditor must either elect to sue on the contract or repossess the goods; he may not do both. The theory of this section is that in transactions in which the cash price is under $1,000, the right to seek a deficiency after repossession is worth little to the legitimate creditor, but it can be used abusively by the unscrupulous creditor.

The Code eliminates in sales credit the practice of the seller's taking a security interest in a houseful of furniture to secure the payment of the price of a single refrigerator or television set. Although the Code does permit taking a security interest in more than the goods sold when debts arising out of other sales are consolidated, it requires payments to be allocated so that the goods are freed from the security interest on a first in first out basis.

The Code restricts balloon payments which often have been used to push a debtor into extending and refinancing the debt. It also prohibits irrevocable assignments of earnings, garnishment proceedings prior to judgment, and confessions of judgment. It sets limits on charges which can be made on default, attorney's fees which can be collected from debtors, and the amount of a debtor's earnings subject to garnishment. It limits small loans to 25 months or 37 months when the annual rate of loan finance charge exceeds 10%. It gives buyers three days to cancel home solicitation sales and prohibits referral sales. It includes provisions on credit life insurance and credit accident and health insurance like those now in force in states which effectively regulate such insurance.

The third approach of the Code toward eliminating harmful practices

and enabling consumers to deal more effectively with creditors is contained in provisions which permit courts in proceedings commenced by the Administrator to declare any agreement or part of an agreement unconscionable and unenforceable as a whole or in part. The court is empowered to order the enforcement of the agreement in such a way as to avoid any unconscionable result. Debtors themselves and also the Administrator may bring proceedings to recover excess charges, the Administrator may himself order creditors to cease violating the Code and the Administrator may bring court proceedings to obtain injunctions against violations of the Code and against unconscionable conduct. Varying special civil and criminal penalties are provided for different kinds of violations. Studies have shown that the major part of overreaching and abuse stems from a relatively small percentage of creditors. In total effect the Code sets standards of conduct for all creditors participating in consumer credit and provides strong and effective remedies against creditors committing serious abuses without impairing the rights of legitimate creditors and without seriously raising the general cost of credit to consumers.

DISCLOSURE

The disclosure requirements of the Code are in most cases the same as those in the Federal Truth-in-Lending Act. Where they differ, the Code's provisions are more stringent.

Basically, in a credit sale the seller is required to set forth: 1) what is being sold; 2) the cash price; 3) the down payment; 4) the balance owing; 5) amount payable for registration or certificate of title fees not included in the cash price; 6) the amount of official fees and taxes; 7) a brief description of any insurance provided and, if a separate charge is made, the amount of the charge; 8) in the case of a sale of land the amount and a description of the closing costs; 9) the total amount financed; 10) the dollar amount of the credit service charge; 11) the total unpaid balance; 12) the annual rate of the credit service charge; 13) the payment schedule; 14) the charges to be made in the event of default; and 15) a description of any security interest taken.

The dollar amount of the credit service charge is not required in a land transaction if the rate of credit service charge is under 10%.

Similar disclosure is required in the case of loans, and under somewhat different mechanical requirements, in the case of revolving sale and loan accounts, and in refinancings, consolidations, and deferrals.

The percentage rate which is disclosed must be computed according to what is known as the U.S. Rule. This is the method traditionally employed in first mortgage real estate financing where payments are applied first to accrued interest and then to the reduction of principal.

The kinds of charges which may be excluded from the calculation of the rate to be disclosed are limited. Except for certain closing costs in real estate transactions involving a credit service or loan finance

charge not exceeding 10% per year, all extra charges must be included in the credit service or loan finance charge except a defined category called "additional charges". "Additional charges" are official fees and taxes, liability and casualty insurance if the buyer is told that he can choose the insurer, and life, health and accident insurance if such insurance is not a factor in the granting of the credit and the buyer is so told. If insurance charges do not meet these tests, they must be included in the credit service charge or loan finance charge. Other charges of benefit to the debtor apart from the granting of credit may be excluded from the finance charge if the Administrator has approved them.

These exceptions from the credit service and loan finance charge are the same as those in the Federal Truth-in-Lending Act. All other extra charges must be included in the credit service or loan finance charge in calculating the rate.

The theory of the disclosure requirements is that the buyer or borrower will be able to shop for credit just as he shops for other commodities. The dollar cost of having goods or money immediately rather than waiting will be clear to him. The requirements that all creditors state a rate in the same manner (in terms of an annual percentage) will permit the consumer to make meaningful comparisons and choose between alternative sources of credit and get the best deal. Looking at the dollar cost and the rate, the consumer might decide to use savings rather than to incur debt at all.

RATES

The rates in the Code are based on the underlying principle that legislation should *not* attempt to fix rates in the sense that public utility commissions fix rates for public utilities, but rather that the economic forces of free enterprise and supply and demand should set rates through improved competition within maximum ceilings prescribed in the consumer credit area. In consumer credit, ceilings are imposed in part because they have been imposed frequently in the past and in part because consumers are generally considered not to have equal bargaining power with creditors. On the other hand, with two narrow exceptions, no ceilings are imposed for business credit and any residual ceilings still applicable to business credit under general usury statutes are removed.

In deciding what the rate maximums should be, the Commissioners took into account that raising and lowering maximum rates have the inevitable effect of increasing or decreasing the size of the consumer credit market. High maximums permit more persons to obtain credit from legitimate sources; low maximums decrease the number of persons who may obtain credit. The maximum ceilings provided in the Code are designed to permit most credit-worthy consumers to have access to the consumer credit market.

The basic maximum rate in the Code is 18%. There are higher graduated rates where the amount of the credit is small. 36% per annum is permitted on the amount of the unpaid balance up to $300, 21% on the amount from $300 to $1,000 and 15% on the amount over $1,000, with the composite actual rate under these graduated rates levelling off at 18%. In order to charge rates in excess of 18%, a lender (but not a seller) must either be licensed or a supervised financial organization, e.g., a bank, credit union or the like.

On revolving charge accounts in sales credit, the maximum permitted rate is 2% per month (24% per year) on the amount outstanding up to $500, and 1½% per month (18% per year) on the amount in excess of $500.

LICENSING, FEES AND ADMINISTRATION

Each creditor who is regularly engaged in the business of granting consumer credit is required to notify the Administrator that he is so engaged. In addition, he is required to pay an annual fee based upon the amount of the consumer credit obligations owed to him. This fee is designed to defray all or part of the cost of administering the Act.

In order to make loans at rates in excess of 18%, a lender must first obtain a license from the Administrator. The Administrator is directed to investigate the applicant and grant the license only if he finds that the financial responsibility, character and fitness of the applicant are such as to warrant belief that the business will be conducted fairly.

Banks and other institutions which are supervised by other governmental agencies are not subject to the licensing requirement.

The Administrator has broad powers to investigate, issue orders and go to court to obtain compliance by creditors with the act. His actions, however, are subject to notice, fair hearing and other due process requirements.

Among his other powers, the Administrator is authorized to seek an injunction against unconscionable agreements or conduct.

EFFECT OF CODE ON POWERS OF ORGANIZATIONS

The Code prescribes maximum charges for all creditors extending consumer credit and displaces existing limitations on the powers of creditors based on maximum charges.

In the case of sellers of goods or services, small loan companies, licensed lenders, consumer and sales finance companies, industrial banks and loan companies, and commercial banks and trust companies, the Code displaces existing limitations on their powers based solely on amount or duration of credit.

Except as to maximum charges, the Code does not displace limitations on powers of credit unions, savings banks, savings and loan associations, or other thrift institutions.

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Questions & Answers

On

UNIFORM CONSUMER CREDIT CODE

Courtesy of

Alaska Retail Association, Inc.

Box 1727
Anchorage, Alaska

THE UNIFORM CONSUMER CREDIT CODE

Questions and Answers

Q. What is the Uniform Consumer Credit Code?

A. The Uniform Consumer Credit Code is a balanced consumer protection law considered by most authorities to be the finest consumer protection legislation ever written.

Q. Who prepared the UCCC?

A. The Code was prepared by the National Conference of Commissioners on Uniform State Laws.

Q. What is the National conference?

A. The Conference is an organization made up of Commissioners of the 50 states whose function it is to draft uniform legislation to be offered to states for enactment.

Q. How many Commissioners are there in the National Conference?

A. The average number of Commissioners from each state is three making a total of 150 for the Conference as a whole. Provisions for appointment of Commissioners is made by statute with appointments customarily made by the Governor.

Q. What are the qualifications of Commissioners?

A. Commissioners must be either practicing lawyers, judges or law school professors.

Q. Are Commissioners paid for their services?

A. The Commissioners serve without compensation but are reimbursed for most out-of-pocket expenses.

Q. What other laws have been written by the National Conference?

A. The organization which has been in existence since 1892 has drafted several other uniform state laws. Examples of such laws which have been widely enacted include: The Uniform Sales Act, the Uniform Stock Transfer Act, more recently, the Uniform Commercial Code.

Q. What is the relationship of the Commissioners to their respective states?

A. Commissioners are officials of the respective states which they represent and, as such, are public servants with all of the responsibilities and duties incident to public service.

Q. Just how does the role of public servants influence the work of the Commissioners?

A. Commissioners accept their responsibility as public servants with the highest ethics. Every action of the National Conference is determined fully by the public responsibility felt by its members.

Q. How does the Conference draft uniform legislation?

A. The Conference works thoroughly and slowly. Work on the Uniform Commercial Code continued for 12 years before it was finally offered to the states for enactment. The Uniform Consumer Credit Code required more than 4 years in its preparation.

In drafting uniform legislation the Commissioners build solidly on existing law and practice but where they find that by reason of historical accident or some like cause existing laws or practices in their judgment are unsound, archaic or sometimes silly they do not hesitate to provide for their repeal.

Q. Why did the Conference draft Consumer Credit legislation?

A. The major underlying reason for drafting Uniform Credit legislation is the phenomenal growth of consumer credit during the 20th century. The Conference notes that by the latest Federal Reserve figures there is close to 100 billion dollars of installment consumer credit outstanding at any one time in the Unites States, and if household mortgage credit is added to this figure the aggregate total is in the neighborhood of 330 billion dollars. The Conference felt that the extension and growth of such credit are not only matters of social and economic concern, but, also, are matters of major consequence to which the law must adjust.

Q. What is meant by the term "adjust"?

A. As consumer credit developed it became apparent that credit of this type could not live within low rate ceilings. Therefore, a steady series of legal principles or special legislation evolved to circumvent and avoid low rates. This resulted in a proliferation of legislation throughout the nation and despite such proliferation there were still widespread consumer abuses. In 1957, recognizing the need of uniform legislation, the Council of State Governments requested the National Conference to draft such a Credit Code. The Code project got underway in 1964. By that time the Conference was convinced that the need for extensive study and a major drafting effort was clear.

Q. What trend did the Conference follow in developing the Code?

A. The Conference decided to deal with the entire subject of Consumer Credit comprehensively and on fundamental lines, to review all laws relating to Consumer Credit in depth, to consider the background and reasons for Consumer Credit and economic and social aspects of it, and to draft legislation that would treat the entire subject of Consumer Credit on scientific lines rather than a continuance of historical acts.

Q. In defining the Code, the term "balanced" Consumer Protection law has been used. What does this mean?

A. The UCCC restructures all laws imposing maximum charges on the cost of money or credit, regulates consumer credit generally and brings substantially all consumer credit transactions under one comprehensive code. It imposes a single and standard set of maximum charges on almost all types of consumer credit, and except in the case of extortionate charges frees substantially all types of business credit from any maximum charge or rate ceiling. The Code puts all creditors extending consumer credit on virtually an even or balance footing so far as maximum charges and control of balances are concerned. It stimulates competition by eliminating artificial barriers to entry into the credit granting business and be requiring disclosure of the cost of credit both in terms of dollar amounts and in terms of an annual percentage rate. It is a balanced code, fair to all creditors operating in the consumer credit field and fair to consumers.

Q. Should consumer legislation be drafted and enacted at the federal or state level?

A. The National Conference felt that the Code should be enacted at the state level. The Commissioners stated that between a particular buyer and a seller, or a particular borrower and lender both located in the same state it is quite difficult to think of a much more local type of transaction than consumer credit. They, also, pointed out that consumer credit is usually a transaction of small size, ranging from a less than $5.00 sale as a part of a store revolving account or a shopper's credit card operation to purchase of automobiles on time or borrowing from the installment credit department of banks ranging in most cases from $100 to $3,000. The Conference, also, felt that if the Federal Government took control of Consumer Credit entirely this would constitute a very large shift in control from the state to the federal government of an important aspect of American life.

Q. What does the federal government think about federal-state control of Consumer Credit?

A. The Banking & Currency Committees of the Senate and House of Representatives in considering the recently enacted Federal Truth-in-Lending Act expressed an awareness of the federal-state problem and were reluctant and hesitant to pre-empt from the states the field of consumer credit. As a result, the recently enacted federal bill included a provision that the Board of Governors of the Federal Reserve system "shall exempt from the requirements of the Act any class of credit transaction which the Board determines is subject to state law which requires disclosure substantially similar to the federal requirements and contains adequate provisions for enforcement." Thus, it follows that the federal government definitely provided a way and a means by which consumer credit may remain a state controlled field.

Q. Will adoption of the Uniform Consumer Credit Code exempt Alaska from supervision of consumer credit by the federal government?

A. Yes, According to all current information available the UCCC meets the Rederal Reserve test and would divest the state of federal supervision. As far as the Turth-in-Lending Act supervises disclosure and related provisions, the Code does likewise and authorities say is even more stringent than the federal law. In addition, the UCCC goes further in that it sets maximum ceilings and correction of virtually all known consumer abuses.

Q. We have been told by some that if the Legislature copies the Federal Truth-in-Lending Act into Alaska law the federal government will divest itself of control of credit in the state. Is this true?

A. Not necessarily. There is a wide field of interpretation regarding Federal Reserve acceptance of supervisory staffing, regulations, transaction requirements etc.

Q. Does the Code contain the regulations pursuant to the Federal Truth-in-Lending law?

A. The UCCC bill, as introduced in the Alaska Legislature, includes all regulations pursuant to the federal act.

Q. What confusion could arise out of copying the federal law into state law rather than passing the UCCC?

A. (1) There is a question as to whether the state would be divested of Federal supervision.

(2) Such action may lead to conditions in which creditors would be required to make double disclosures.

(3) The law would be a "bits and pieces" type of legislation which usually creates confusion in the marketplace.

(4) Such action is completely unnecessary since the federal act went into effect on July 1, 1969, thus negating any need for a small "Federal Act."

Q. Is exemption from Federal supervision a strong argument for the passage of the UCCC?

A. Yes. Most Alaskans desire to retain jurisdiction over consumer credit and creditors in the consumer credit field of Alaska certainly do not want to operate under two sets of laws. This fact is one of the major reasons why the enactment of the Code is advisable.

Q. Were attempts made to influence the preparation of the Code in order to preserve segmented consumer credit?

A. Yes. Strong pressures were brought to bear upon the National Conference by opponents of consumer protection legislation to produce more of the same confusion which already exists throughout the nation in the consumer credit field. The status quo is referred to as segmented with segmentation being based to a considerable extent on types of creditors, that is, small loan companies, retail merchants, commercial banks, credit unions etc. The Conference was urged to preserve all this segmentation, some or all of the variations in maximum rate ceilings on finance charges, and some or all of the varying methods for starting ceiling rates. In fact, the Conference was pressured to do nothing more than compound the existing confusion.

Q. How did the Conference react to this pressure?

A. The National Conference took the position that a policy of preserving and attempting to improve one or more existing types of legislation would do nothing more than preserve and stratify types of classifications that are now causing confusion and have partially broken down. The Conference felt it could make no contribution unless a comprehensive approach was adopted.

Q. How much of the installment credit outstanding in the United States do the various segments of the credit industry possess?

A. As of December 31, 1967, the percentage share of different segments of the consumer credit industry in installment consumer credit was as follows:

Commercial banks	43.6%
Sales finance companies	21.6%
Credit unions	11.8%
Consumer finance (small loan) companies	8.1
Other financial institutions insurance companies, savings & loan associations, etc.)	2.5%
Retail outlets	12.4%
Total	100.00%

Q. What limits did the Conference feel were needed in the Code's coverage?

A. The Code covers consumer credit as opposed to business credit.

Q. Why is not the purpose test a part of the Code?

A. There are difficulties in applying a pure purpose test. Actually, purpose is nothing more than the mental intent of an individual. The Code made the distinction between consumer credit and business credit on the basis of whether the debtor is a natural person or whether the debtor is an organization. Organization as defined includes corporations, business trusts, partnerships, associations or governmental entities or bodies.

Q. Are the Code's provisions fair and equitable to both consumers and the credit industry?

A. Yes. The provisions are workable and provide a greatly superior base for handling consumer credit than the mass of legislation presently on statute books throughout the nation. Although some provisions may appear to favor industry and others favor consumers, in actual fact the provisions will be beneficial to both sides of the economic spectrum.

Q. How does the Code affect usury provisions?

A. The Code provides for the outright termination of all usury provisions and rate ceilings in the case of most business credit. The reasoning which supports this principle is that the operation of the money market and the economic rules of supply and demand are better control factors for interest charges in business credit than any legislation. It, also, notes that business debtors can bargain satisfactorily without the need of legislative assistance. The operation of existing general usury statutes has become so much an empty shell and so generally absurd in its unreasonable and haphazard application that they should be repealed outright as to substantially all business credit, according to most authorities.

Q. In the case of consumer credit, are rate ceilings preserved?

A. Rate ceilings are preserved but are evenly distributed across-the-board to all types of consumer credit.

Q. What is consumer credit as defined by the Code?

A. Consumer credit is credit extended to natural persons for personal, family, household or in some instances agricultural use.

Q. Is there a dollar limitation in regard to the jurisdiction established in the Code?

A. Yes. Consumer credit is credit extended up to a dollar jurisdictional amount of $25,000 except in the case of consumer credit secured by real estate where there is no jurisdictional limit.

Q. What are the rate ceiling found in the Code?

A. The rate ceiling prescribed is on a graduated basis with a maximum of 36% per annum on the first $300, 21% per annum on balances of $300 to $1,000 and 15% per annum on balances above $1,000 with the composite rate resulting from these graduated ceilings leveling off at a base ceiling of 18% per annum on balances from $2,500 to $2,900 and above. A major exception from these standard rate ceilings is in sales credit revolving account where the ceilings are 24% per annum or 2% per month on the unpaid balance on the first $500 of balance, and 18% per annum or 1½% per month on the unpaid balance in excess of $500.

Q. How does the Conferencd justify the standard recommended rate ceilings?

A. First, the Conference emphasizes the basic principle that legislation should not attempt to fix rates in the sense that public utility commissions prescribe rates that may be charged by public utilities. Rather, the Conference says the legislation should do nothing more than fix maximum ceilings which may not be exceeded but should be at a level to permit the extension of almost any type of consumer credit through legitimate channels.

Q. Upon what does the Code rely to fix effective rates?

A. The Code places reliance upon the operation of competition to keep actual rates charged below the legislative ceiling prescribed.

Q. How does the Code provide ways to see that the competition will keep lower than established ceiling rates?

A. The Code notes competition, in order to keep rates low, should be permitted to operate to a maximum extent and provides for "easy" entry into the lending field to make it as competitive as the retail field. This means that as far as is possible all extenders of credit must compete on equal terms with all other extenders of credit. It, also, means that a consumer must be able to intelligntly shop for credit.

Q. The Code, to encourage competition, provides "easy" entry into the lending field. What does this mean?

A. "Easy" entry refers to the provision of the Code which makes it possible for individuals or businesses to enter the cash loan fields without being restricted by artificial barriers.

Q. Are "easy" entry lenders regulated?

A. Yes. The Administrator will establish regulations governing such lenders and the Code, itself, provides that –

(1) Such lenders must secure a license from the Administrator.
(2) They cannot loan money for more than 18% per annum.
(3) They cannot accept deposits.
(4) They must pay the same fee to the Administrator's office on credit outstanding during the year as all other lenders.
(5) They must adhere to all disclosure requirements.
(6) They must abide by all consumer protection provisions of the Code.

Q. Why do banks have regulations applicable to lendin money not placed on "easy" entry lenders?

A. Banks use depositors' money for lending purposes and the various governments provide regulations to protect the depositor. "Easy" entry lenders cannot accept deposits and they will be lending their own personal money.

Q. Can "easy" entry licenses be revoked?

A. Yes. Any irregular practice is sufficient cause for revocation of license.

Q. Are these basic principles of the Code?

A. The Code, as a whole, is framed on these principles.

Q. Does this establish a new principle in American thinking?

A. No. These principles involve no novelty in basic American thinking. In most areas of economic life in America price-fixing by governmental fiat has been avoided rigorously. Price fixing is inherent in general usury statutes and actually constitutes an exception to the traditional American economic view.

Q. Opponents to the Code say that the rate ceilings as applied to the total consumer credit market will cause an increase in finance charges to the consumer. Is this true?

A. This is not true. Studies made by the National Conference point out that competition does in fact keep interest and finance charges down as much in the case of extension credit as in other types of transactions. Examples include interest rates charged to corporations which under existing law in 30 states do not have full benefit of usury statutes. In these states interest rates have been no higher than in states where usury statutes exist. In Massachusetts and New Hampshire there have been no general usury statutes for many years but the general level of interest

rates and finance charges in these states are not significantly different from those in other states. In automobile financing, rates actually charged are in most cases materially lower than ceilings prescribed in the motor vehicle retail installment sales act.

Q. What fact did the Conference recognize as primary in setting the rate ceilings in the Code?

A. The Conference recognized that rates must be sufficient to cover the cost of money, the cost of administering the credit extended, and the risk of nonpayment.

Q. What other factors operate in the cost of granting credit?

A. The Commissioners stated that the cost of money varies in relation to general money market conditions and that the cost of money today is higher than for many years, perhaps, as far back as the stock market crash in 1929. The Conference, also, pointed out that in consumer credit the cost of administering the credit is a most important factor. Commissioners noted one study which showed the average operating expenses other than bad debt reserves of many major national finance companies to be $10.40 on the first $100 of each loan.

Q. Does this explain the higher rate ceilings prescribed for the first $300 of any transaction?

A. Yes, the high cost of setting up any credit transaction on the books of a credit extender explains the high ceiling rate prescribed for the first $300. Actually, the rates prescribed fall at about the midpoint of existing rate limitations in the small loan area and are somewhat above present rates in the area over $3,000.

Q. What did money market studies reveal to the National Conference?

A. Money market studies and economic advice given to the National Conference consistently indicated that the principal effect of fixing maximum rates at a higher or lower level is to permit larger or smaller numbers of consumers into the credit market. High maximums permit more persons to obtain credit from legitimate sources. In contrast, low maximums decrease the number of persons who may obtain credit and drive the borrower and/or buyer to illegal loan sharks.

Q. Is competition the primary factor in establishing effective rates favorable to consumers?

A. Yes. The Code's provisions for improved operation of competition in credit are calculated to keep the rates actually charged well below the maximum ceilings stated.

Q. What are the disclosure requirements in the Code?

A. The Code requires the seller to set forth:

(1) What is being sold.
(2) The cash price.
(3) The down payment.
(4) The balance owing.
(5) Amount payable for registration or certificate of title fees not included in the cash price.
(6) The amount of official fees and taxes.
(7) A description of any insurance provided and if a separate charge is made the amount of the charge.
(8) In the case of a sale of land the amount and a description of the closing costs.
(9) The total amount financed.
(10) The dollar amount of the credit service charge.
(11) The total unpaid balance.
(12) The annual rate of the credit service charge.
(13) The payment schedule
(14) The charges to be made in the event of default.
(15) A description of any security interest taken.

Q. Will the disclosure requirements of the Code enhance competition as a basic principle set forth in the Code?

A. Yes, such disclosure requirements complement quite closely the maximum rate provisions of the Code. They do so by developing a single set of measuring standards by which consumers may shop for credit. Thus, they enhance competition which is relied upon by the Code to keep rates reasonably low.

Q. Does the Code place limitation on creditors' remedies?

A. Yes. The Code contains a number of limitations on creditors' remedies. This is the true reason that there is opposition to the adoption of the Code since these remedies are pure consumer protection.

Q. Does the Code prohibit the use of multiple agreements?

A. Yes. Sellers are prohibited from using multiple agreements for the purpose of obtaining a higher finance charge than would be otherwise permitted.

Q. Are sellers and lessors prohibited from taking negotiable promissory notes to evidence consumer obligation?

A. Yes. The promissory note use has been one of the major consumer abuses where instead of selling the actual installment contract a promissory note has been utilized as a negotiable instrument. Producers of the notes have been held not responsible in any way for claims and defenses of the buyer against the seller.

Q. Does the Code provide that assignees shall be subject to claims and defenses of the buyer against the seller?

A. Yes. The Code provides that an assignee is equally responsible for the quality of goods and services as the original seller. This is an issue of long standing and it is admitted in the consumer credit field. Sellers and banks and finance companies buying sellers' papers argue that assignees shall not be subject to claims and defenses of the buyer against the seller. Consumers, on the other hand, argue with equal strength that a great portion of consumer abuses are traceable to a bank or finance company which is free from claims and defenses of the buyer against the seller.

Q. What is the opinion of merchants regarding this issue?

A. The legitimate merchant does not fear this situation nor should any bank of finance company which does business with legitimate merchants since it has been historically true in Alaska that legitimate stores make restitution for defective goods and services.

Q. Does the Code place controls upon ballon payments?

A. yes. If any scheduled payment is more than twice as large as the average of earlier scheduled payments, the buyer has a right to refinance the amount of that payment at the time it is due without penalty. The terms of the refinancing must be as favorable to the buyer as the terms of the original sale.

Q. Does the Code place limitations on the amount and type of security that may be taken in sales transactions?

A. Yes. A seller may take a security interest
(1) in the property sold;
(2) in goods upon which services are performed;
(3) in property in which goods sold are installed; or
(4) in land to which the goods are affixed or which is maintained, repaired or improved as a result of the sale of the goods or the services, if, in the case of a security interest in land, the debt secured is $1,000 or more or in the case of a security interest in goods the debt secured is $300 or more.

Q. Does the Code make any provisions regarding the assignment of earnings?

A. Yes. A seller or lessor may not take an assignment of earnings of the buyer or lessee for payment or as a security for payment of a debt arising out of a consumer credit sale or a consumer lease.

Q. What does the Code do in respect to referral sales?

A. Referral sale contracts cannot be entered into by sellers and buyers. Any inducement to enter into such a contract is in violation of the Code and the buyer of lessee at his option may rescind the agreement or retain the goods delivered and the benefit of any service performed without any obligation to pay for them.

Q. May terms by changed in the case of revolving charge accounts?

A. Yes. If a change is made in the terms of a revolving charge account the merchant must give the buyer written notice at least 3 times with the first notice issued at least six months before the effective date of the change.

Q. Are there any exceptions to this requirement?

A. Yes. The notice specified is not required if:

(1) The buyer after receiving notice of the change agrees in writing to the change;

(2) The buyer elects to pay an amount designated on a billing statement as including a new charge for the benefit offered to the buyer when the benefit and charge constitute a change in terms and when the billing statement also states the amount payable if the new charge is excluded;

(3) The change involves no significant cost to the buyer;

(4) The buyer has previously consented in writing to the kind of change made and notice of the change is given to the buyer in two billings cycles prior to the effective date of the change; and

(5) The change applies only to purchases made or obligations incurred after a date specified in a notice of the change given in two billing cycles peior to the effective date of the change.

Q. What constitutes notice in regard to changes in revolving credit account?

A. The notice is given to the buyer when mailed to him at the address used by the seller for sending periodic billing statements.

Q. Does the Code provide for a cancelling provision in home solicitation sales?

A. Yes. A buyer has the right to cancel a home solicitation sale until

midnight of the third business day after the day on which he signs the agreement or offer to purchase.

Q. What are the technical procedures in regard to cancellation?

A. Cancellation occurs when the buyer gives written notice of cancellation to the seller.

Q. Where does the Code require that such notice be sent?

A. The notice must be sent to the address listed in the agreement or offer to purchase.

Q. What other provisions for cancellation does the Code provide?

A. The notice of cancellation if by mail is given when the notice is properly addressed with postage prepaid and deposited in a mail box.

Q. Does the notice of cancellation have to take a particular form?

A. No. Notice of cancellation is sufficent if it indicates by any form of written expression the intention of the buyer to cancel the home solicitation sale.

Q. Are there any circumstances under which the buyer may not cancel a home solicitation sale?

A. Yes. The buyer may not cancel a home solicitation sale if he has requested the seller to provide goods or services without delay because of an emergency and the seller in good faith has made a substantial beginning of performance. The buyer also may not cancel a home solicitation sale if the goods cannot be returned to the seller in substantially as good condition as when received by the buyer.

Q. Does the Code provide for the return of goods given as collateral or the down payment by the seller in cancelled home solicitation sales?

A. Yes. Within 10 days after a home solicitation sale has been cancelled the seller must return any payments made by the buyer and any note or other evidence of indebtedness. If the down payment included goods traded the goods must be returned in substantially as good condition as when received by the seller.

Q. Is there a provision made whereby the seller may retain a cancellation fee?

A. Yes. The seller may retain a cancellation fee amounting to 5% of the cash price but not exceeding the amount of the cash down payment. However, if the seller fails to comply with any obligation imposed by the Code, or if the buyer voids the sale on

any ground independent of his right to cancel provided by the provision of the Code, the seller is not entitled to retain a cancellation fee.

Q. What does the Code provide in regard to the duty of the buyer to the seller of the home solicitation sale?

A. Upon demand, the buyer must give to the seller any goods delivered by the seller pursuant to the sale, but he is is not obligated to deliver the goods to any place other than his residence. If the seller fails to demand possession of the goods within a reasonable time after cancellation or revocation, the goods become the property of the buyer without obligation to pay for them. The Code states that 40 days is a reasonable time. The buyer is required to take reasonable care of the goods in his possession both before cancellation or revocation and for a reasonable time afterwards during which time that goods are otherwise at the seller's risk.

Q. Does the Code provide limitations on garnishment?

A. Yes. The maximum part of the aggregate disposable earnings of an individual for any workweek which is subject to garnishment to enforce payment of a judgment arising from a consumer credit sale, consumer lease or consumer loan may not exceed the lesser of:

(1) 25% of the disposable earnings for that week; or

(2) The amount of which his disposable earnings for that week exceed 40 times the Federal Minimum Hourly Wage. Since the Federal Minimum Hourly Wage at this time is $1.60, this means $64.00.

Disposable earnings as defined by the Code means that part of the earnings of an individual remaining after the deductions of those earnings of amounts required by law to be withheld.

Q. What does the Code provide regarding discharging employees for garnishment?

A. The Code states emphatically that no employer shall discharge an employee because his wages have been subject to garnishment.

Q. What does the Code say in regard to repossession of goods and suit for balance due?

A. The Code, as introduced, provides that the seller may repossess goods with a cash price under $1,000 where the debt is not being repaid or may sue for the balance due but the seller may not do both. He must make a choice between the two actions. Deficiency judgments are forbidden.

Q. We note that the Code contains language in regard to unconscionable agreements and conduct. Just what does this section do?

A. The Conference gave a great deal of study to the fact that the greatest majority of consumer abuse is traceable to a relatively small proportion of fringe operators who do not hesitate to over-reach whenever they can whether inside or outside the law. The question arose as to how a statute can provide protection against this kind of conduct. The Commissioners felt that realistic legislation is of limited value unless it has some language pointed toward this problem and believe there is no escape from having that language flexible enough to adjust to the great variety of schemes and practices that an ingenious type of individual may conceive. Therefore, the Code provided "Unconscionability" to meet this situation. The Code contains language with respect to unconscionable agreements and conduct. This has been done for the simple reason that the Commissioners could see no escape from this provision if the provision was to be flexible enough to adjust to the maneuvers of fringe operators.

Q. Is unconscionability a new concept?

A. Unconscionability is not a new concept. There have been decisions providing relief from unconscionable conduct running back over 100 years. It is, also, a part of the Uniform Commercial Code and there is equal or more reason to use it in the Consumer Credit Code.

Q. Are there any limitations on the action of unconscionability?

A. Yes. Considerable care is used to keep the concept within strict boundaries. Debtors for example cannot determine that conduct of a creditor is unconscionable. The Administrator cannot make such a determination, only courts can make this determination, and in courts only the judge and not the jury. The Code provides that the Administrator may bring a civil action to restrain a creditor from engaging in a course of unconscionable conduct either in effecting consumer credit transactions or in collection of debts arising from these transactions. In every case, however, it is only a court that can make a determination of unconscionability.

Q. How will the Code be administered?

A. The Code provides for administration by the State Banking Commissioner, and it prescribes his powers and functions. In the Code he is referred to as the "Administrator."

Q. What are his powers?

A. (1) He will administer the consumer credit market;

(2) He may bring action on behalf of an individual or a class of debtors to recover excess charges made by a creditor;
(3) He may bring actions to restrain a creditor from engaging in unconscionable conduct;
(4) He may issue orders and subject to appropriate administrative review he may order a creditor or others to cease and desist from engaging in violations of the Code;
(5) The Administrator is given substantial investigatory powers with respect to consumer credit extended by merchants or finance companies; and
(6) He is expected to cooperate with officials having supervisory power over banking institutions to obtain compliance with Code provisions.

In addition, the Administrator

(1) has power to issue regulations with respect to specified subjects;
(2) he may foster and aid programs for education of consumers; and
(3) encourage establishment of non-profit consumer credit counseling agencies.

Q. Does the Code provide for advisors to the Administrators?

A. Yes. The Code recognizes the considerable power of the Administrator and to aid and assist him in the effective performance of his duties the Code provides for a Council of Advisors on Consumer Credit. These are to be drawn in relatively equal proportions from consumers or the public, on the one hand, and from members of the consumer industry on the other.

Q. How is the office of the Administrator financed?

A. All persons or businesses doing credit business must so notify the Administrator and must pay to the Administrator $10 for every $100,000 outstanding credit during a fiscal year. This money will be used to carry on the work and meet the expenses of the office of the Administrator.

Q. Do merchants of Alaska support the adoption of the Uniform Consumer Credit Code?

A. Yes, even though the Code will require merchants to pay a substantial fee for its administration which heretofore has not been required of retailers.

Q. Why is the retail industry favorable to its adoption?

A. (1) It is the finest consumer protection Code ever prepared.

(2) The public policy demands its passage.
(3) The Code will do away with the "Bits and Pieces" type of credit legislation.
(4) The UCCC will give the state as near total consumer protection as is legislatively possible.
(5) The Code solves present and future credit problems in a way that will not require future legislative action.
(6) Creditors can live with the Code, and though there are some provisions which retailing does not like, the Code is a document, which taken as a whole, retailing can support and under which retailing can operate. This is the "on balance" concept which is basic to the Code.
(7) The Code attempts to satisfy the interests of the diverse groups represented in the credit field.
(8) The code is favored by the Alaska Retail Association, The Alaska State Chamber of Commerce and most other chambers throughout the state because they recognize it as one of the most fair documents ever devised in th area of consumer credit. Alaskan retailers acknowledge the fact that problems do exist in the consumer credit field and are proud to suoport UCCC as the best existing answer to those problems – from the standpoint of both consumer and creditor.

Instalment Credit
GUIDE

— EXTRA EDITION —

NUMBER 183 AUGUST 19, 1968

UNIFORM CONSUMER CREDIT CODE

With Prefatory Note and Comments

FINAL DRAFT

(DRAFT SUBJECT TO CHANGES TO CONFORM TO CONSUMER CREDIT PROTECTION ACT REGULATIONS)

Extra copies of this Report may be obtained by writing Commerce Clearing House, Inc., 4025 W. Peterson Ave., Chicago, Illinois 60646. Price: 1-4 Copies, $2.00 each; 5-9 Copies, $1.80 each; 10-24 Copies, $1.70 each; 25-49 Copies, $1.50 each.

COMMERCE CLEARING HOUSE, INC.
PUBLISHERS of TOPICAL LAW REPORTS
NEW YORK CHICAGO WASHINGTON

About This Code

The Uniform Consumer Credit Code, having been formulated with the concept that "credit transactions" is but one subject of the law, is intended to replace various laws regulating consumer and other credit transactions.

Application . . . The UCCC is generally applicable to:

(1) consumer credit sales of goods or services for $25,000 or less, consumer leases, and consumer credit sales of an interest in land for any amount;

(2) consumer loans of $25,000 or less, except that loans secured by an interest in land are covered for any amount; and

(3) insurance provided in relation to the consumer credit sale, consumer loan or consumer lease.

Purchases made and debts incurred must be primarily for personal, family, household or agricultural purpose.

Facets . . . The Code provides maximum credit service charges and is intended to replace general usury laws, consumer credit regulatory acts imposing maximum charges, and other acts providing maximum charges for loans or extensions of credit. Provisions cover the enforcement of rights, and other provisions govern administrative regulation. Advertising, referral sales, license for supervised loans, assignment of earnings, unconscionability, revolving charges, cross-collateral, adjustment of dollar amounts, prohibition of certain negotiable instruments, garnishment, and home solicitation are just a few of the many facets covered by this Code.

Exemptions . . . The Code exempts:

(1) credit extended to governments or their agencies;

(2) sale of insurance by an insurer, except for the sale of credit insurance;

(3) public utility or common carrier rates under state or federal regulation; and

(4) licensed pawnbroker transactions.

Consumer credit sale exemptions include 30-day charge accounts and services furnished on short-term credit for which no finance charge is made. Consumer loan exemptions include loans secured by business collateral. Except for disclosure and remedies, sales or loans involving an interest in land are exempt if the finance or service charge is 10% or less per year.

Federal . . . The UCCC conforms to the requirements of the Federal Consumer Credit Protection Act (INSTALMENT CREDIT GUIDE, No. 177, Extra Edition, May 22, 1968, and No. 177, Second Extra Edition, May 24, 1968) so that a UCCC state is exempt from the federal requirements.

Final Draft . . . This Final Draft of the UCCC was approved by the National Conference of Commissioners on Uniform State Laws on July 30, 1968, and by the American Bar Association on August 7, 1968.

COMMERCE CLEARING HOUSE, INC.

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UNIFORM CONSUMER CREDIT CODE

NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS

Final Draft*

UNIFORM CONSUMER CREDIT CODE

With Prefatory Note and Comments*

* Subject to Style Changes and Changes to Conform to Requirements and Regulations of Board of Governors of the Federal Reserve System Pursuant to the Federal Consumer Credit Protection Act, and to Additions to and Corrections of Prefatory Note and Comments.

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Prefatory Note

This, the Final Draft of the Uniform Consumer Credit Code, has been approved by the National Conference of Commissioners on Uniform State Laws on July 30, 1968 and by the American Bar Association on August 7, 1968. It is, however, subject to style changes and to changes to conform it to the requirements and Regulations of the Board of Governors of the Federal Reserve System pursuant to the Federal Consumer Credit Protection Act. Moreover, this Prefatory Note and the Comments are subject to additions and corrections.

The second previous draft, the Tentative Final Draft—Working Draft No. 8, was prepared prior to action by the Congress on a final version of S. 5 (the Proxmire "Truth-in-Lending Act") or H. R. 11601 (the Sullivan "Consumer Credit Protection Act"), but after the passage of those bills by the Senate and the House, respectively. Wide distribution of that draft was made so that the Special Committee might have the advantage of further comments before the 1968 Annual Meeting of the National Conference.

The last previous draft, the Revised Tentative Final Draft—Working Draft No. 9, was prepared in the light of the enactment by the Congress and the approval by the President of S. 5, the Consumer Credit Protection Act (Public Law 90-321, 82 Stat. 146) and, specifically, of § 123 of that Act as follows:

> "§ 123. Exemption for State-regulated transactions
>
> The Board [of Governors of the Federal Reserve System] shall by regulation exempt from the requirements of this chapter [i.e., Chapter 2 of Title I of the Consumer Credit Protection Act, relating to disclosure in consumer credit transactions], any class of credit transactions within any State if it determines that under the law of that State that class of transactions is subject to requirements substantially similar to those imposed under this chapter, and that there is adequate provision for enforcement."

and in the beliefs that:

1. The Board of Governors of the Federal Reserve System will exempt by regulation from the disclosure requirements of Chapter 2 of the Consumer Credit Protection Act the classes of consumer credit transactions governed by the Uniform Consumer Credit Code within any State which enacts the Code, and

2. The provisions of the Uniform Consumer Credit Code relating to consumer credit advertising will conform to the requirements of Chapter 3 of Title I of the Consumer Credit Protection Act, relating to Credit Advertising, and to any implementing regulation prescribed by the Board of Governors of the Federal Reserve System pursuant to § 105 of the Consumer Credit Protection Act as follows:

> "§ 105. Regulations
>
> The Board shall prescribe regulations to carry out the purposes of this title [i.e., Title I including Chapter 1, General Provisions, Chapter 2, Credit Transactions, and Chapter 3, Credit Advertising]. These regulations may contain such classifications, differentiations, or other provisions, and may provide for such adjustments and exceptions for any class of transactions, as in the judgment of the Board are necessary or proper to effectuate the purposes of this title, to prevent circumvention or evasion thereof, or to facilitate compliance therewith."

Time has not permitted the Special Committee to ascertain the views of the Board of Governors of the Federal Reserve System with respect to these matters. Consequently, the Special Committee has requested and received from the National Conference authority, subject to the approval of the Executive Committee of the National Conference, and with the understanding that the changes will be submitted to the National Conference at its 1969 Annual Meeting for ratification, to make changes in this Final Draft to conform it to the requirements and regulations of the Board of Governors of the Federal Reserve System.

Research

Prior to the creation of the Special Committee, the American Bar Foundation, at the request of the Conference and of the Committee's predecessor, the Special Committee on a Uniform Retail Instalment Sales Act, undertook a thorough survey of consumer credit laws of all the States. In 1965, the American Bar Foundation published its "Trends in Consumer Credit Legislation" prepared by Miss Barbara A. Curran of the Foundation's research staff. The book has proved invaluable to the Committee.

Since the creation of the Committee, its members and staff have prepared papers on various legal, economic and sociological aspects of consumer credit. These papers have provided bases for the Committee's discussions with its staff and Advisory Committee and Panels of Advisors on specific subjects, as well as for its policy decisions.

Basic Assumptions

This draft, like those which preceded it, is predicated on various basic assumptions, including:

First, the successful American way of permitting competition to determine prices of non-monopoly commodities and services should also be allowed to apply to the pricing of money and credit;

Second, usury laws imposing inflexible price ceilings on money and credit are historical vestiges of the erroneous supposition that emperors, kings and governments could effectively fix all prices; the need to escape the rigidity of usury laws has led to special laws, which only the expert can find or understand, for most types of credit transactions requiring a charge higher than the usury rate;

Third, consumer credit legislation should be contained in one law so that any attorney can quickly and effectively advise his consumer client;

Fourth, for competition effectively to determine the pricing of money and credit requires:

a. for credit grantors, relatively easy entry into the market to avoid monopoly;

b. for knowledgeable and sophisticated credit recipients, eliminating or at least minimizing controls;

c. for the protection of less knowledgeable and less sophisticated credit recipients:

1. uniform disclosure of the costs and terms of credit to permit informed judgments as to whether or not to use credit, to facilitate

"shopping for credit," and to enable the forces of competition to work freely;

2. ceilings on the price of credit, restrictions on creditors' rights and remedies, and enhancements of debtors' rights and remedies sufficient to prevent overreaching by creditors without unduly limiting the availability of credit;

3. administrative powers and self-executing judicial remedies ample to assure compliance with statutory requirements;

4. enough financial resources available to the Administrator to enable him effectively to exercise the powers of his office; and

5. a broad-gauged Advisory Council to advise the Administrator in the exercise of his powers in the interests of our entire society and economy.

In preparing this draft on these assumptions, the Special Committee has recognized that:

a. a combination of too low ceiling rates, too substantial restrictions on creditors' rights and remedies, or too great enhancements of debtors' rights or remedies, might deprive the less credit-worthy of lawful sources of credit and drive them to "loan sharks" and other illegal credit grantors in whose hands they will enjoy no legal protections; it was to remedy the "loan shark" evil that the Russell Sage Foundation proposed its Uniform Small Loan Laws; and

b. the provisions governing ease of entry into the market, uniform disclosure of costs and terms, rate ceilings, restriction of creditors' rights and remedies, enlargement of debtors' rights and remedies, and powers granted to the Administrator are so inextricably interrelated that any substantial change in one area requires a major review of the balance struck in all other areas.

In order to permit the organization of panels of advisors on the subjects of consumer credit counseling agencies and wage earner receiverships before completing its consideration of those subjects, the Committee has made no attempt to complete the drafting of provisions relating to them, but has reserved for them Articles 7 and 8 of the Code in case, after 1968, the Committee recommends and the National Conference approves the inclusion in the Code of provisions relating to those subjects.

Uniform Legislation Desirable

The Special Committee believes that consumer credit legislation should be uniform among the States. Uniform laws on the subject will benefit both the consumer and the consumer credit industry.

Consumer understanding of credit transactions and of alternative sources of consumer credit is a primary essential for the effective operation of both consumer credit laws and of the forces of competition in consumer credit extensions. The mobility of our people makes uniformity of State consumer credit laws a prerequisite for maximum consumer understanding.

The extent to which segments of the consumer credit industry operate across the State lines makes uniformity of consumer credit laws desirable to facilitate and to reduce the costs of their interstate operations, and thus to promote competition and so ultimately to reduce the costs to the consumer of credit extensions.

Prior Drafts

The First Tentative Draft (Working Draft No. 1) was submitted for consideration to the National Conference at its 1966 Annual Meeting. Comments on that draft by the Committee's advisors and others at that meeting led the Committee to the conclusion that loan transactions and sales transactions should be treated separately.

In reaching that conclusion, the Committee was and is aware that, sociologically and economically, sales credit and loan credit are alike and that their separate treatment results in much duplication in drafting. Nevertheless, we are mindful of the weight given to Uniform Acts by Courts of States which have not enacted them. Thus, long before the Uniform Commercial Code was enacted or even introduced in New York, the New York Court of Appeals relied in part on a provision of the Uniform Commercial Code in overruling the Court's prior decisions on privity of contract and determining who may recover upon a breach of warranty in a sale of goods. The Committee believes that any encouragement to the courts of a State which has not enacted the Uniform Consumer Credit Code to rely on the Code's provisions to reject the time sale price doctrine would have most unfortunate social and economic consequences for both consumers and credit grantors.

A Second Tentative Draft (Working Draft No. 4) was prepared for consideration by the National Conference at its 1967 Annual Meeting. In order to obtain a maximum of comments, suggestions, and criticisms, more than 4,000 copies of the draft and invitations to attend a public discussion of it were distributed. Section F of the National Conference and the Committee accordingly held a public hearing on Working Draft No. 4 in June 1967.

The Second Tentative Draft (Working Draft No. 4) together with an Addendum to it predicated on the written and oral comments received before, during and after the June, 1967, hearing, were submitted to the National Conference at its 1967 Annual Meeting.

The discussions at the 1967 Annual Meeting and further consideration of the comments, compiled section-by-section, on Working Draft No. 4 led to Working Draft No. 5, not publicly distributed but considered by the Committee and its staff in preparing Working Draft No. 6. About 4,000 copies of that draft were distributed. It was considered at length at a public hearing conducted by the Committee in January, 1968. It was further discussed at joint meetings of the Committee and its Advisory Committee and Panels of Advisors on Special Subjects. These discussions and the comments on Working Draft No. 6, compiled section-by-section, led to Working Draft No. 7. That draft was not publicly distributed but provided the basis for the Tentative Final Draft (Working Draft No. 8) which, as noted above, was widely distributed with requests for comments.

Federal Disclosure Legislation

The Congress has passed and the President has approved the Consumer Credit Protection Act (Public Law 90-321; 82 Stat. 146), including as Title I—Consumer Credit Cost Disclosure, the "Truth-in-Lending Act." The Federal Act (§ 123) requires that the Board of Governors of the Federal Reserve System exempt from Federal disclosure requirements "any class of credit transactions within any State

if it [the Board] determines that under the law of that State that class of transactions is subject to requirements substantially similar to those imposed under this chapter [i.e., Chapter 2—Credit Transactions], and that there is adequate provision for enforcement."

The Consumer Credit Protection Act consequently presents an unusual opportunity for the early enactment by the States of the Final Draft of the Uniform Consumer Credit Code. The Federal Act requires a complete review, expansion and revision of most States' consumer credit laws. In the view of the Committee it will be far better for the various States to enact a comprehensive Uniform Consumer Credit Code than to tinker with the hodgepodge of existing State consumer credit legislation.

If the Board of Governors of the Federal Reserve System is to exempt from the requirements of the Federal Act the Uniform Consumer Credit Code as enacted by any State, the Code must require at least the disclosures provided for in the Federal Act. This Final Draft attempts to do so.

Plans for Continuation of Consumer Credit Project

Under the rules of the National Conference this Special Committee will be continued for at least two years for, among others, the following purposes.

1. Assisting in enactment of the Uniform Consumer Credit Code by State Legislatures;

2. Considering insertion in the Code of provisions concerning
   (a) consumer credit counseling agencies,
   (b) wage earner receiverships; and
   (c) other appropriate subjects.

3. Receiving suggestions for modification of the Code and, in its judgment, transmitting those suggestions to the National Conference for consideration.

4. Assisting in educational programs regarding consumer credit.

After the discharge of this Special Committee, the National Conference has under consideration the advisability of creating a Permanent Review Board to receive and consider recommended changes in the Consumer Credit Code.

Liaison with the American Bar Association

In accordance with the standard procedures of the National Conference and the American Bar Association, the Committee has consulted with appropriate sections of the American Bar Association, including the Corporation, Banking and Business Law Section and the Section on Administrative Law, as well as with legal organizations affiliated with the American Bar Association, such as the National Legal Aid and Defender Association.

The Advisory Committee and the Panels of Advisors

In conformity to usual National Conference procedures, the Committee has appointed an Advisory Committee representative of affected segments of the public and of the consumer credit industry.

Whatever the Committee's other accomplishments, it has established, perhaps for the first time, a close personal working relationship, a feeling of mutual respect and a rapport between representatives of the two groups.

It is the hope of the Committee that the Council of Advisors to the Administrator proposed in this and prior drafts will continue to expand communication and relationships between representatives of groups having apparently diverse but actually identical interests—the improvement of our society and economy.

The Committee takes this opportunity of expressing its appreciation to its Advisors for their invaluable help and for the almost unlimited time and effort they have devoted to the Committee's project.

The names and addresses of the members of the Advisory Committee and of the various Panels of Advisors follow. [NOTE: The names and addresses are not reproduced.—CCH.]

UNIFORM CONSUMER CREDIT CODE

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Uniform Consumer Credit Code

An Act

Relating to certain consumer and other credit transactions and constituting the uniform consumer credit code; consolidating and revising certain aspects of the law relating to consumer and other loans, consumer and other sales of goods, services and interests in land, and consumer leases; revising the law relating to usury; regulating certain practices relating to insurance in consumer credit transactions; providing for administrative regulations of certain consumer credit transactions; making uniform the law with respect thereto; and repealing inconsistent legislation.

COMMENT

The long title of the Code should be adapted to the constitutional and statutory requirements and practices of the enacting State.

The concept of the Code is that "credit transactions" is a single subject of the law, notwithstanding its many facets.

Article 1—General Provisions and Definitions

PART 1—SHORT TITLE, CONSTRUCTION, GENERAL PROVISIONS

[¶ 800] [Short Title]

Sec. 1.101. This Act shall be known and may be cited as Uniform Consumer Credit Code.

[¶ 801] Purposes; Rules of Construction

Sec. 1.102. (1) This Act shall be liberally construed and applied to promote its underlying purposes and policies.

(2) The underlying purposes and policies of this Act are:

(a) to simplify, clarify and modernize the law governing retail instalment sales, consumer credit, small loans and usury;

(b) to provide rate ceilings to assure an adequate supply of credit to consumers;

(c) to further consumer understanding of the terms of credit transactions and to foster competition among suppliers of consumer credit so that consumers may obtain credit at reasonable cost;

(d) to protect consumer buyers, lessees, and borrowers against unfair practices by some suppliers of consumer credit, having due regard for the interests of legitimate and scrupulous creditors;

(e) to permit and encourage the development of fair and economically sound consumer credit practices;

(f) to conform the regulation of consumer credit transactions to the policies of the Federal Consumer Credit Protection Act; and

(g) to make uniform the law including administrative rules among the various jurisdictions.

[¶ 802] Supplementary General Principles of Law Applicable

Sec. 1.103. Unless displaced by the particular provisions of this Act, the Uniform Commercial Code and the principles of law and equity, including the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions.

[¶ 803] Construction Against Implicit Repeal

Sec. 1.104. This Act being a general act intended as a unified coverage of its subject matter, no part of it shall be deemed to be impliedly repealed by subsequent legislation if such construction can reasonably be avoided.

[¶ 804] Severability

Sec. 1.105. If any provision of this Act or the application thereof to any person or circumstances is held invalid, the invalidity shall not affect other provisions or applications of this Act which can be given effect without the invalid provision or application, and to this end the provisions of this Act are severable.

[¶ 805] Adjustment of Dollar Amounts

Sec. 1.106. (1) From time to time the dollar amounts in this Act designated as subject to change shall change, as provided in this section, in accordance with and to the extent of changes in the Consumer Price Index for Urban Wage Earners and Clerical Workers: U. S. City Average, All Items, 1957-59 = 100, compiled by the Bureau of Labor Statistics, United States Department of Labor, and hereafter referred to as the Index. The Index for December, 1967, is the Reference Base Index.

(2) The designated dollar amounts shall change on July 1 of each even-numbered year if the percentage of change, calculated to the nearest whole percentage point, between the Index at the end of the preceding year and the Reference Base Index is 10 per cent or more, except that

(a) the portion of the percentage change in the Index in excess of a multiple of 10 per cent shall be disregarded and the dollar amounts shall change only in multiples of 10 per cent of the amounts appearing in this Act on the date of enactment;

(b) the dollar amounts shall not change if the amounts required by this section are those currently in effect pursuant to this Act as a result of earlier application of this section; and

(c) in no event shall the dollar amounts be reduced below the amounts appearing in this Act on the date of enactment.

(3) If the Index is revised after December, 1967, the percentage of change pursuant to this section shall be calculated on the basis of the revised Index. If the revision of the Index changes the Reference Base Index, a revised Reference Base Index shall be determined by multiplying the Reference Base Index then applicable by the ratio of the revised Index to the current Index, as each was for the first month in which the revised Index is available. If the Index is superseded, the Index referred to in this section shall be the one represented by the Bureau of Labor Statistics as reflecting most accurately changes in the purchasing power of the dollar for consumers.

(4) The Administrator shall issue a rule announcing

(a) on or before April 30 of each year in which dollar amounts are to change, the changes in dollar amounts required by subsection (2); and

(b) promptly after the changes occur, changes in the Index required by subsection (3) including, when applicable, the numerical equivalent of the Reference Base Index under a revised Reference Base Index and the designation or title of any index superseding the Index.

(5) No person violates this Act if with respect to a transaction otherwise complying with this Act he relies on dollar amounts either determined in accordance with subsection (2) or appearing in the last rule of the Administrator announcing the then current dollar amounts.

(6) If the percentage of change between the Index at the end of the odd-numbered year preceding the effective date of this Act and the Reference Base Index would require change in the designated dollar amounts pursuant to subsection (2), the designated dollar amounts shall change upon the effective date of this Act and, on or before that date, the Administrator shall issue a rule announcing the changes required by this subsection. Subsection (5) also applies if the transaction is based on dollar amounts appearing in the Act and the Administrator has issued no rule as required by this subsection.

COMMENT

Under this section the dollar amounts designated as subject to change will automatically change on July 1 of each even-numbered year if the change in the Consumer Price Index is great enough. The Act will be enacted in all jurisdictions with the dollar amounts now appearing in it without regard to when enactment occurs. December, 1967, has been selected as the reference base period. Examples of how the section operates follow. Assume in each case that the Index for December, 1967, (the Reference Base Index) is 100. The $300 figure appearing in Section 2.201(2)(a) will be used as an illustrative dollar amount.

Case 1: The Index for December, 1969, is 107. The change from the Reference Base Index of 100 is an increase of 7%. Since the change is less than 10%, no change in dollar amounts occurs.

Case 2: The Index for December, 1971, is 112. The change from the Reference Base Index of 100 is an increase of 12%. Since this is more than 10%, a change occurs. The portion of the 12% in excess of 10% is disregarded; hence, an increase of 10% is indicated. 10% of $300 is $30. The dollar amount is $330, effective July 1, 1972.

Case 3: The Index for December, 1973, is 118. The change from the Reference Base Index of 100 is an increase of 18%. The portion of 18% in excess of 10% is disregarded; hence, an increase of 10% is indicated. However, the $300 amount changed to $330 in 1972 (see Case 2). Since the amount currently in effect ($330) is still the correct amount under this section, no change occurs.

Case 4: The Index for December, 1975, is 122. The change from the Reference Base Index of 100 is an increase of 22%. The portion of 22% in excess of a multiple of 10% (here 20%) is disregarded and a 20% increase is indicated. 20% of $300 is $60. The dollar amount is $360, effective July 1, 1976.

Case 5: The Index for December, 1977, is 117. The change from the Reference Base Index of 100 is an increase of 17%. The portion of 17% in excess of 10% is disregarded and a 10% increase is indicated. 10% of $300 is $30. The dollar amount is $330, effective July 1, 1978, a decrease from the $360 amount in effect since 1976 (see Case 4).

Case 6: State X adopts this Act on July 22, 1980, to become effective on January 1, 1981. The Index for December, 1979, is 135. A comparison of the Reference Base Index (100) with the Index for December, 1979 (135) indicates an increase of the $300 amount by 30% or $90, effective January 1, 1981. On July 1, 1982, the dollar amounts again change if subsection (2) requires.

Case 7: In 1983 BLS revises the Index, changing coverage components, and selecting a new base period. If only the coverage or components were changed, the revised Index should be used for subsequent calculations. However, if a new base period is selected (1981-82=100), an equivalent on the scale of the revised Index must be assigned to the Reference Base Index (December, 1967). Assume that the revised Index is first available for July, 1983. For that month the old Index is 200 and the new Index (1981-2=100) has gone up to 104. The revised Reference Base Index (that is, the Index for December, 1967, on the revised scale) may be found by this calculation:

$$\frac{\text{(old Index)}}{\text{(new Index)}} = \frac{200}{104} = \frac{100}{X} \quad \text{(old Reference Base Index)}$$

$$X = \frac{100 \times 104}{200}$$

X = 52 (revised Reference Base Index)

A comparison of the revised Index for December, 1983 (108) with the revised Reference Base Index (52) shows that the change from the revised Reference Base Index is an increase of 107.7%.

$$\frac{108.0 - 52.0}{52.0} = 1.077 = 107.7\%$$

Under subsection (2), 107.7% becomes 108%. The portion of 108% in excess of a multiple of 10% (here 100%) is disregarded, and a 100% increase is indicated. The dollar amount is $600, effective July 1, 1984.

[¶ 806] Waiver; Agreement to Forego Rights; Settlement of Claims

Sec. 1.107. (1) Except as otherwise provided in this Act, a buyer, lessee, or debtor may not waive or agree to forego rights or benefits under this Act.

(2) A claim by a buyer, lessee, or debtor against a creditor for an excess charge, other violation of this Act, or civil penalty, or a claim against a buyer, lessee, or debtor for default or breach of a duty imposed by this Act, if disputed in good faith, may be settled by agreement.

(3) A claim, whether or not disputed, against a buyer, lessee or debtor may be settled for less value than the amount claimed.

(4) A settlement in which the buyer, lessee, or debtor waives or agrees to forego rights or benefits under this Act is invalid if the court as a matter of law finds the settlement to have been unconscionable at the time it was made. The competence of the buyer, lessee, or debtor, any deception or coercion practiced upon him, the nature and extent of the legal advice received by him, and the value of the consideration are relevant to the issue of unconscionability.

[¶ 807] Effect of Act on Powers of Organizations

Sec. 1.108. (1) This Act prescribes maximum charges for all creditors extending consumer credit, except lessors and those excluded (Section 1.202), and displaces existing limitations on the powers of those creditors based on maximum charges.

(2) With respect to sellers of goods or services, small loan companies, licensed lenders, consumer and sales finance companies, industrial banks and loan companies, and commercial banks and trust companies, this Act displaces existing limitations on their powers based solely on amount or duration of credit.

(3) Except as provided in subsection (1) [and in the Article on Effective Date and Repealer (Article 9)], this Act does not displace limitations on powers of credit unions, savings banks, savings and loan associations, or other thrift institutions whether organized for the profit of shareholders or as mutual organizations.

(4) Except as provided in subsections (1) and (2) [and in the Article on Effective Date and Repealer (Article 9)], this Act does not displace

(a) limitations on powers of supervised financial organizations (subsection (16) of Section 1.301) with respect to the amount of a loan to a single borrower, the ratio of a loan to the value of collateral, the duration of a loan secured by an interest in land, or other similar restrictions designed to protect deposits, or

(b) limitations on powers an organization is authorized to exercise under the laws of this State or the United States.

COMMENT

The bracketed language in subsections (3) and (4) should be included and the brackets omitted if the enacting State adds to the Article on Effective Date and Repealer (Article 9) provisions displacing limitations on powers of the kinds of organizations enumerated in subsections (3) and (4).

PART 2—SCOPE AND JURISDICTION

[¶ 808] Territorial Application

Sec. 1.201. (1) Except as otherwise provided in this section, this Act applies to sales, leases, and loans made in this State and to modifications, including refinancings, consolidations, and deferrals, made in this State, of sales, leases, and loans, wherever made. For purposes of this Act

(a) a sale or modification of a sale agreement is made in this State if the buyer's agreement or offer to purchase or to modify is received by the seller in this State;

(b) a lease or modification of a lease agreement is made in this State if the lessee's agreement or offer to lease or to modify is received by the lessor in this State; and

(c) a loan or modification of a loan agreement is made in this State if a writing signed by the debtor and evidencing the debt is received by the lender in this State.

(2) With respect to sales made pursuant to a revolving charge account (Section 2.108), this Act applies if the buyer's communication or indication of his intention to establish the account is received by the seller in this State. If no communication or indication of intention is given by the buyer before the first sale, this Act applies if the seller's communication notifying the buyer of the privilege of using the account is mailed or personally delivered in this State.

(3) With respect to loans made pursuant to a lender credit card or similar arrangement (subsection (8) of Section 1.301), this Act applies if the debtor's communication or indication of his intention to establish the arrangement with the lender is received by the lender in this State. If no communication or indication of intention is given by the debtor before the first loan, this Act applies if the lender's communication notifying the debtor of the privilege of using the arrangement is mailed or personally delivered in this State.

(4) The Part on Limitations on Creditors' Remedies (Part 1) of the Article on Remedies and Penalties (Article 5) applies to actions or other proceedings brought in this State to enforce rights arising out of a consumer credit sale, consumer lease, or consumer loan, or modification thereof, wherever made.

(5) If a consumer credit sale, consumer lease, or consumer loan, or modification thereof, is made in another state to a person who is a resident of this State when the sale, lease, loan, or modification is made, the following provisions apply as though the transaction occurred in this State:

(a) a seller, lessor, lender, or assignee of his rights, may not collect charges through actions or other proceedings in excess of those permitted by the Article on Credit Sales (Article 2) or by the Article on Loans (Article 3); and

(b) a seller, lessor, lender, or assignee of his rights, may not enforce rights against the buyer, lessee, or debtor, with respect to the provisions of agreements which violate the provisions on Limitations on Agreements and Practices (Part 4) of the Article on Credit Sales (Article 2) or of the Article on Loans (Article 3).

(6) Except as provided in subsection (4), a sale, lease, loan, or modification thereof, made in another state to a person who was not a resident of this State at the time the sale, lease, loan, or modification was made is valid and

enforceable in this State according to its terms to the extent that it is valid and enforceable under the laws of the state applicable to the transaction.

(7) For the purposes of this Act, the residence of a buyer, lessee, or debtor, is the address given by him as his residence in any writing signed by him in connection with a credit transaction. Until he notifies the creditor of a new or different address, his address is presumed to be unchanged.

(8) Notwithstanding other provisions of this section

(a) except as provided in subsection (4), this Act does not apply if the buyer, lessee, or debtor is not a resident of this State at the time of a credit transaction and the parties then agree that the law of his residence applies; and

(b) this Act applies if the buyer, lessee, or debtor is a resident of this State at the time of a credit transaction and the parties then agree that the law of this State applies.

(9) Except as provided in subsection (8), the following agreements by a buyer, lessee, or debtor are invalid with respect to consumer credit sales, consumer leases, consumer loans, or modifications thereof, to which this Act applies:

(a) that the law of another state shall apply;

(b) that the buyer, lessee, or debtor consents to the jurisdiction of another state; and

(c) that fixes venue.

(10) The following provisions of this Act specify the applicable law governing certain cases:

(a) applicability (Section 6.102) of the Part on Powers and Functions of Administrator (Part 1) of the Article on Administration (Article 6); and

(b) applicability (Section 6.201) of the Part on Notification and Fees (Part 2) of the Article on Administration (Article 6).

[¶ 809] Exclusions

Sec. 1.202. This Act does not apply to

(1) extensions of credit to government or governmental agencies or instrumentalities;

(2) the sale of insurance by an insurer, except as otherwise provided in the Article on Insurance (Article 4);

(3) transactions under public utility or common carrier tariffs if a subdivision or agency of this State or of the United States regulates the charges for the services involved, the charges for delayed payment, and any discount allowed for early payment; or

(4) the rates and charges and the disclosure of rates and charges of a licensed pawnbroker established in accordance with a statute or ordinance concerning these matters.

COMMENT

The Federal Consumer Credit Protection Act is referred to in the Comments as CCPA. Subsection (1) is derived from CCPA Section 104(1). Subsection (3) is derived from CCPA Section 104(4). Unless excluded by regulations, pawnbrokers will be subject to the CCPA. Rather than attempt to study the pawnbroker business

at this time to determine the appropriateness of applying this Code to pawnbroker transactions, the Committee suggests that the exclusion of this type of transaction from the Code be continued.

[¶ 810] [Jurisdiction and Service of Process]

[Sec. 1.203. (1) The [ ] court of this State may exercise jurisdiction over any creditor with respect to any conduct in this State governed by this Act or with respect to any claim arising from a transaction subject to this Act. In addition to any other method provided by [rule or by] statute, personal jurisdiction over a creditor may be acquired in a civil action or proceeding instituted in the [ ] court by the service of process in the manner provided by this section.

(2) If a creditor is not a resident of this State or is a corporation not authorized to do business in this State and engages in any conduct in this State governed by this Act, or engages in a transaction subject to this Act, he may designate an agent upon whom service of process may be made in this State. The agent shall be a resident of this State or a corporation authorized to do business in this State. The designation shall be in a writing and filed with the Secretary of State. If no designation is made and filed or if process cannot be served in this State upon the designated agent, process may be served upon the Secretary of State, but service upon him is not effective unless the plaintiff or petitioner forthwith mails a copy of the process and pleading by registered or certified mail to the defendant or respondent at his last reasonably ascertainable address. An affidavit of compliance with this section shall be filed with the clerk of the court on or before the return day of the process, if any, or within any further time the court allows.]

PART 3—DEFINITIONS

[¶ 811] General Definitions

Sec. 1.301. In addition to definitions appearing in subsequent Articles, in this Act

(1) "Administrator" means the Administrator designated in the Article (Article 6) on Administration (Section 6.103).

(2) "Agreement" means the bargain of the parties in fact as found in their language or by implication from other circumstances including course of dealing or usage of trade or course of performance.

(3) "Agricultural purpose" means a purpose related to the production, harvest, exhibition, marketing, transportation, processing, or manufacture of agricultural products by a natural person who cultivates, plants, propagates, or nurtures the agricultural products. "Agricultural products" includes agricultural, horticultural, viticultural, and dairy products, livestock, wildlife, poultry, bees, forest products, fish and shellfish, and any products thereof, including processed and manufactured products, and any and all products raised or produced on farms and any processed or manufactured products thereof.

COMMENT

This definition of "agricultural products" is derived from the Agricultural Marketing Act of 1946, 7 U. S. C. Section 1626.

(4) "Closing costs" with respect to a debt secured by an interest in land includes:

(a) fees or premiums for title examination, title insurance, or similar purposes including surveys,

(b) fees for preparation of a deed, settlement statement, or other documents,

(c) escrows for future payments of taxes and insurance,

(d) fees for notarizing deeds and other documents,

(e) appraisal fees, and

(f) credit reports.

COMMENT

Except for "including surveys" in subsection(4)(a), this definition is derived from CCPA Section 106(e).

(5) "Conspicuous": A term or clause is conspicuous when it is so written that a reasonable person against whom it is to operate ought to have noticed it. Whether a term or clause is conspicuous or not is for decision by the court.

COMMENT

This definition is derived in part from UCC Section 1-201(10).

(6) "Credit" means the right granted by a creditor to a debtor to defer payment of debt or to incure debt and defer its payment.

(7) "Earnings" means compensation paid or payable to an individual or for his account for personal services rendered or to be rendered by him, whether denominated as wages, salary, commission, bonus, or otherwise, and includes periodic payments pursuant to a pension, retirement, or disability program.

COMMENT

This definition is derived in part from CCPA Section 302(a).

(8) "Lender credit card or similar arrangement" means an arrangement or loan agreement, other than a seller credit card, pursuant to which a lender gives a debtor the privilege of using a credit card, letter of credit, or other credit confirmation or identification in transactions out of which debt arises

(a) by the lender's honoring a draft or similar order for the payment of money drawn or accepted by the debtor;

(b) by the lender's payment or agreement to pay the debtor's obligations; or

(c) by the lender's purchase from the obligee of the debtor's obligations.

(9) "Official fees" means

(a) fees and charges prescribed by law which actually are or will be paid to public officials for determining the existence of or for perfecting, releasing, or satisfying a security interest related to a consumer credit sale, consumer lease, or consumer loan; or

(b) premiums payable for insurance in lieu of perfecting a security interest otherwise required by the creditor in connection with the sale,

lease, or loan, if the premium does not exceed the fees and charges described in paragraph (a) which would otherwise be payable.

COMMENT

This subsection is derived from CCPA Section 106(d).

(10) "Organization" means a corporation, government or governmental subdivision or agency, trust, estate, partnership, cooperative, or association.

(11) "Payable in instalments" means that payment is required or permitted by agreement to be made in (a) two or more periodic payments, excluding a down payment, with respect to a debt arising from a consumer credit sale pursuant to which a credit service charge is made, (b) four or more periodic payments, excluding a down payment, with respect to a debt arising from a consumer credit sale pursuant to which no credit service charge is made, or (c) two or more periodic payments with respect to a debt arising from a consumer loan. If any periodic payment other than the down payment under an agreement requiring or permitting two or more periodic payments is more than twice the amount of any other periodic payment, excluding the down payment, the consumer credit sale, consumer lease, or consumer loan is "payable in instalments."

COMMENT

A consumer credit sale in which the buyer has the options of paying the cash price in full in 90 days without a credit service charge or of paying in instalments the amount financed, including a credit service charge, is "payable in instalments".

(12) "Person" includes a natural person or an individual, and an organization.

(13) "Person related to" with respect to an individual means (a) the spouse of the individual, (b) a brother, brother-in-law, sister, sister-in-law of the individual, (c) an ancestor or lineal descendant of the individual or his spouse, and (d) any other relative, by blood or marriage, of the individual or his spouse who shares the same home with the individual. "Person related to" with respect to an organization means (a) a person directly or indirectly controlling, controlled by or under common control with the organization, (b) an officer or director of the organization or a person performing similar functions with respect to the organization or to a person related to the organization, (c) the spouse of a person related to the organization, and (d) a relative by blood or marriage of a person related to the organization who shares the same home with him.

(14) "Presumed" or "presumption" means that the trier of fact must find the existence of the fact presumed unless and until evidence is introduced which would support a finding of its non-existence.

(15) "Seller credit card" means an arrangement pursuant to which a person gives to a buyer or lessee the privilege of using a credit card, letter of credit, or other credit confirmation or identification primarily for the purpose of purchasing or leasing goods or services from that person, a person related to that person, or others licensed or franchised to do business under his business or trade name or designation.

(16) "Supervised financial organization" means a person, other than an insurance company or other organization primarily engaged in an insurance business,

(a) organized, chartered, or holding an authorization certificate under the laws of this State or of the United States which authorize the

person to make loans and to receive deposits, including a savings, share, certificate or deposit account, and

(b) subject to supervision by an official or agency of this State or of the United States.

(17) "United States rule" means the actuarial method of allocating payments made on a debt between principal or amount financed and loan finance charge or credit service charge, pursuant to which a payment is applied first to the accumulated loan finance charge or credit service charge and the balance is applied to the unpaid principal or amount financed.

COMMENT

For a discussion of the operation of the United States rule, see Comment to Section 2.304.

[¶ 812] Definition: "Federal Consumer Credit Protection Act"

Sec. 1.302. In this Act "Federal Consumer Credit Protection Act" means the Consumer Credit Protection Act (Public Law 90-321; 82 Stat. 146), as amended, and includes regulations issued pursuant to that Act.

[¶ 813] Index of Definitions in Act

Sec. 1.303. Definitions in this Act and the sections in which they appear are:

"Administrator"—Section 1.301(1)
"Administrator"—Section 6.103
"Agreement"—Section 1.301(2)
"Agricultural purpose"—Section 1.301(3)
"Amount financed"—Section 2.111
"Annual percentage rate" (sale)—Section 2.304
"Annual percentage rate" (loan)—Section 3.304
"Business collateral"—Section 3.105
"Cash price"—Section 2.110
"Closing costs"—Section 1.301(4)
"Conspicuous"—Section 1.301(5)
"Consumer credit insurance"—Section 4.103(1)
"Consumer credit sale"—Section 2.104
"Consumer lease"—Section 2.106
"Consumer loan"—Section 3.104
"Consumer related loan"—Section 3.602
"Consumer related sale"—Section 2.602
"Contested case"—Section 6.402(1)
"Corresponding nominal annual percentage rate" (sale)—Section 2.304
"Corresponding nominal annual percentage rate" (loan)—Section 3.304
"Credit"—Section 1.301(6)
"Credit Insurance Act"—Section 4.103(2)
"Credit service charge"—Section 2.109

"Earnings"—Section 1.301(7)
"Federal Consumer Credit Protection Act"—Section 1.302
"Goods"—Section 2.105(1)
"Home solicitation sale"—Section 2.501
"Lender"—Section 3.107(1)
"Lender credit card or similar arrangement"—Section 1.301(8)
"License"—Section 6.402(2)
"Licensing"—Section 6.402(3)
"Loan"—Section 3.106
"Loan finance charge"—Section 3.109
"Merchandise certificate"—Section 2.105(2)
"Official fees"—Section 1.301(9)
"Organization"—Section 1.301(10)
"Party"—Section 6.402(4)
"Payable in instalments"—Section 1.301(11)
"Person"—Section 1.301(12)
"Person related to"—Section 1.301(13)
"Precomputed (loan)"—Section 3.107(2)
"Precomputed (sale)"—Section 2.105(7)
"Presumed" or "presumption"—Section 1.301(14)
"Principal"—Section 3.107(3)
"Regulated lender"—Section 3.501(2)
"Regulated loan"—Section 3.501(1)
"Revolving charge account"—Section 2.108
"Revolving loan account"—Section 3.108
"Rule"—Section 6.402(5)
"Sale of goods"—Section 2.105(4)
"Sale of an interest in land"—Section 2.105(6)
"Sale of services"—Section 2.105(5)
"Seller"—Section 2.107
"Seller credit card"—Section 1.301(15)
"Services"—Section 2.105(3)
"Supervised financial organization"—Section 1.301(16)
"Supervised lender"—Section 3.501(4)
"Supervised loan"—Section 3.501(3)
"United States rule"—Section 1.301(17)

Article 2—Credit Sales

PART 1—GENERAL PROVISIONS

[¶ 814] Short Title

Sec. 2.101. This Article shall be known and may be cited as Uniform Consumer Credit Code—Credit Sales.

[¶ 815] Scope

Sec. 2.102. This Article applies to consumer credit sales, including home solicitation sales, and consumer leases; in addition Part 6 applies to consumer related sales.

[¶ 816] Definitions in Article

Sec. 2.103. The following definitions apply to this Act and appear in this Article as follows:

"Amount financed"	Section 2.111
"Annual percentage rate"	Section 2.304(2)
"Cash price"	Section 2.110
"Consumer credit sale"	Section 2.104
"Consumer lease"	Section 2.106
"Consumer related sale"	Section 2.602
"Corresponding nominal annual percentage rate"	Section 2.304(3)
"Credit service charge"	Section 2.109
"Goods"	Section 2.105(1)
"Home solicitation sale"	Section 2.501
"Merchandise certificate"	Section 2.105(2)
"Precomputed"	Section 2.105(7)
"Revolving charge account"	Section 2.108
"Sale of goods"	Section 2.105(4)
"Sale of an interest in land"	Section 2.105(6)
"Sale of services"	Section 2.105(5)
"Seller"	Section 2.107
"Services"	Section 2.105(3)

[¶ 817] Definition: "Consumer Credit Sale"

Sec. 2.104. (1) Except as provided in subsection (2), "consumer credit sale" is a sale of goods, services, or an interest in land in which

(a) credit is granted by a seller who regularly engages as a seller in credit transactions of the same kind,

(b) the buyer is a person other than an organization,

(c) the goods, services, or interest in land are purchased primarily for a personal, family, household, or agricultural purpose,

(d) either the debt is payable in instalments or a credit service charge is made, and

(e) with respect to a sale of goods or services, the amount financed does not exceed $25,000.

(2) Unless the sale is made subject to this Act by agreement (Section 2.601), "consumer credit sale" does not include

(a) a sale in which the seller allows the buyer to purchase goods or services pursuant to a lender credit card or similar arrangement, or

(b) except as provided with respect to disclosure (Section 2.301) and debtors' remedies (Section 5.201), a sale of an interest in land if the credit service charge does not exceed 10 per cent per year calculated according to the United States rule on the unpaid balances of the amount financed on the assumption that the debt will be paid according to the agreed terms and will not be paid before the end of the agreed term.

(3) The amount of $25,000 in subsection (1) is subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

COMMENT

Subsection (1)(d) excludes from the Code two familiar credit transactions: (1) services furnished on short-term credit with neither a credit service charge nor instalment payments; professional men usually furnish their services on this basis as do many electricians, plumbers, and the like; and (2) the typical 30-day retail charge account. The credit clothing merchant or credit jeweler who does not separately state a credit service charge is covered by this section if his contracts are payable in instalments. Subsection (1)(e) excludes sales of goods or services of over $25,000, but does not do so for sale of real property.

[¶ 818] Definitions: "Goods"; "Merchandise Certificate"; "Services"; "Sale of Goods"; "Sale of Services"; "Sale of an Interest in Land"; "Precomputed"

Sec. 2.105. (1) "Goods" includes goods not in existence at the time the transaction is entered into and merchandise certificates, but excludes money, chattel paper, documents of title, and instruments.

(2) "Merchandise certificate" means a writing issued by a seller not redeemable in cash and usable in its face amount in lieu of cash in exchange for goods or services.

(3) "Services" includes (a) work, labor, and other personal services, (b) privileges with respect to transportation, hotel and restaurant accommodations, education, entertainment, recreation, physical culture, hospital accommodations, funerals, cemetery accommodations, and the like, and (c) insurance provided by a person other than the insurer.

(4) "Sale of goods" includes any agreement in the form of a bailment or lease of goods if the bailee or lessee agrees to pay as compensation for use a sum substantially equivalent to or in excess of the aggregate value of the goods involved and it is agreed that the bailee or lessee will become, or for no other or a nominal consideration has the option to become, the owner of the goods upon full compliance with his obligations under the agreement.

COMMENT

This subsection is derived from CCPA Section 103(g).

(5) "Sale of services" means furnishing or agreeing to furnish services and includes making arrangements to have services furnished by another.

(6) "Sale of an interest in land" includes a lease in which the lessee has an option to purchase the interest and all or a substantial part of the rental or other payments previously made by him are applied to the purchase price.

(7) A sale, refinancing, or consolidation is "precomputed" if the debt is expressed as a sum comprising the amount financed and the amount of the credit service charge computed in advance.

[¶ 819] Definition: "Consumer Lease"

Sec. 2.106. (1) "Consumer lease" means a lease of goods

(a) which a lessor regularly engaged in the business of leasing makes to a person, other than an organization, who takes under the lease primarily for a personal, family, household, or agricultural purpose,

(b) in which the amount payable under the lease does not exceed $25,000, and

(c) which is for a term exceeding four months.

(2) "Consumer lease" does not include a lease made pursuant to a lender credit card or similar arrangement.

(3) The amount of $25,000 in subsection (1) is subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

[¶ 820] Definition: "Seller"

Sec. 2.107. Except as otherwise provided, "seller" includes an assignee of the seller's right to payment but use of the term does not in itself impose on an assignee any obligation of the seller with respect to events occurring before the assignment.

COMMENT

Compare Section 3.107(1) defining lender to include an assignee. This section is intended to confer on the assignee all the rights of the seller. Unless the assignee undertakes direct collection of payments or enforcement of rights arising from the sale, he is not subject to penalties under Section 5.202.

[¶ 821] Definition: "Revolving Charge Account"

Sec. 2.108. "Revolving charge account" means an arrangement between a seller and a buyer pursuant to which (1) the seller may permit the buyer purchase goods or services on credit either from the seller or pursuant to a seller credit card, (2) the unpaid balances of amounts financed arising from purchases and the credit service and other appropriate charges are debited to an account, (3) a credit service charge if made is not precomputed but is computed on the outstanding unpaid balances of the buyer's account from time to time, and (4) the buyer has the privilege of paying the balances in instalments.

[¶ 822] Definition: "Credit Service Charge"

Sec. 2.109. "Credit service charge" means the sum of (1) all charges payable directly or indirectly by the buyer and imposed directly or indirectly by the seller as an incident to the extension of credit, including any of the following types of charges which are applicable: time price differential, service, carrying or other charge, however denominated, premium or other charge for any guarantee or insurance protecting the seller against the buyer's default or other credit loss; and (2) charges incurred for investigating the collateral or credit-worthiness of the buyer or for commissions or brokerage for obtaining the credit, irrespective of the person to whom the charges are paid or payable, unless the seller had no notice of the charges when the credit was granted. The term does not include charges as a result of default, additional charges (Section 2.202), delinquency charges (Section 2.203), or deferral charges (Section 2.204).

COMMENT

The first part of the definition is derived from CCPA Section 106(a), with changes made to relate the definition to sales. The second part broadens the definition to include charges with respect to commissions and brokerage within the credit service charge whether or not the creditor imposed them so long as he knew of the charges.

[¶ 823] Definition: "Cash Price"

Sec. 2.110. The "cash price" of goods, services, or an interest in land means the price at which the goods, services, or interest in land are offered for sale by the seller to cash buyers in the ordinary course of business, and may include (1) applicable sales, use, and excise and documentary stamp taxes, (2) the cash price of accessories or related services such as delivery, installation, servicing, repairs, alterations, and improvements, and (3) amounts actually paid or to be paid by the seller for registration, certificate of title, or license fees. The cash price stated by the seller to the buyer pursuant to the provisions on disclosure (Part 3) of this Article is presumed to be the cash price.

[¶ 824] Definition: "Amount Financed"

Sec. 2.111. "Amount financed" means the total of the following items to the extent that payment is deferred:

(1) the cash price of the goods, services, or interest in land, less the amount of any down payment whether made in cash or in property traded in,

(2) the amount actually paid or to be paid by the seller pursuant to an agreement with the buyer to discharge a security interest in or a lien on property traded in, and

(3) if not included in the cash price

(a) any applicable sales, use, or excise and documentary stamp taxes,

(b) amounts actually paid or to be paid by the seller for registration, certificate of title, or license fees, and

(c) additional charges permitted by this Article (Section 2.202).

PART 2—MAXIMUM CHARGES

[¶ 825] Credit Service Charge for Consumer Credit Sales other than Revolving Charge Accounts

Sec. 2.201. (1) With respect to a consumer credit sale, other than a sale pursuant to a revolving charge account, a seller may contract for and receive a credit service charge not exceeding that permitted by this section.

(2) The credit service charge, calculated according to the United States rule, may not exceed the equivalent of the greater of either of the following:

(a) the total of

(i) 36 per cent per year on that part of the unpaid balances of the amount financed which is $300 or less;

(ii) 21 per cent per year on that part of the unpaid balances of the amount financed which is more than $300 but does not exceed $1,000; and

(iii) 15 per cent per year on that part of the unpaid balances of the amount financed which is more than $1,000; or

(b) 18 per cent per year on the unpaid balances of the amount financed.

(3) This section does not limit or restrict the manner of contracting for the credit service charge, whether by way of add-on, discount, or otherwise, so long as the rate of the credit service charge does not exceed that permitted by this section. If the sale is precomputed,

(a) the credit service charge may be calculated on the assumption that all scheduled payments will be made when due, and

(b) the effect of prepayment is governed by the provisions on rebate upon prepayment (Section 2.210).

(4) For the purposes of this section, the term of a sale agreement commences with the date the credit is granted or, if goods are delivered or services performed 10 days or more after that date, with the date of commencement of delivery or performance. Differences in the lengths of months are disregarded and a day may be counted as 1/30th of a month. Subject to classifications and differentiations the seller may reasonably establish, a part of a month in excess of 15 days may be treated as a full month if periods of 15 days or less are disregarded and that procedure is not consistently used to obtain a greater yield than would otherwise be permitted.

(5) Subject to classifications and differentiations the seller may reasonably establish, he may make the same credit service charge on all amounts financed within a specified range. A credit service charge so made does not violate subsection (2) if

(a) when applied to the median amount within each range, it does not exceed the maximum permitted by subsection (2), and

(b) when applied to the lowest amount within each range, it does not produce a rate of credit service charge exceeding the rate calculated according to paragraph (a) by more than 8 per cent of the rate calculated according to paragraph (a).

(6) Notwithstanding subsection (2), the seller may contract for and receive a credit service charge of not more than $5 when the amount financed does not exceed $75 or not more than $7.50 when the amount financed exceeds $75.

(7) The amounts of $300 and $1,000 in subsection (2) are subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

COMMENT

1. *Purpose of rate ceilings provisions.* The purpose of this section and Section 3.508 (Loan Finance Charge for Supervised Loans) is to set ceilings and not to fix rates. Even under present statutes, considerable rate competition exists. The intent of this Act is to provide even more effective competition. Therefore, while this section sets rate ceilings, several other sections are designed to generate sufficient competition to set rates. In addition, other provisions have been omitted by design, because they would have tended to restrict competition. Other provisions related to this section include:

(1) Provisions for disclosure of the credit service charge and loan finance charge both in dollar amounts and as annual percentages (Article 2, Part 3; Article 3, Part 3) are designed to facilitate comparative shopping. This is the most effective means of limiting prices. For most goods and services offered for sale in competitive markets, disclosure of the price has been deemed sufficient to regulate prices.

(2) The absence of special rate ceilings according to the type of credit grantors, type of item financed, or the form of credit extension is by design. Segmentation of the market for credit by differentiated rate ceilings tends to reduce competition and introduce rigidities into the market that benefit a few suppliers at the expense of others and work to the disadvantage of consumers.

(3) Greater freedom of entry to the credit field is fostered by several provisions, as well as by several deliberate omissions. Re-

volving credit may be offered both in connection with credit sales, loans, and supervised loans. No type of credit grantor is limited by this Act in the amount of credit that may be extended. By design the license required to make supervised loans is made readily accessible to those showing financial responsibility, character, and fitness. Provisions for minimum financial assets and for a showing of convenience and advantage have been deliberately omitted, since their inclusion would tend to restrict competition and require establishment of rates, rather than ceilings.

Because of the different cost structures that will be developed as a result of this Act, comparison of these rate ceilings cannot be made to existing rate ceilings. In this respect, the rate ceilings in this section are intimately related to other parts of the Act which provide for limitations on agreements and practices (Article 2, Parts 4 and 5; Article 3, Part 4) and for limitations on creditors' remedies (Article 5, Part 1). Provisions such as holding the assignee subject to defenses (Section 2.404), buyer's right to cancel (2.502), no assignment of earnings (2.410; 3.403), and restrictions on deficiency judgments in consumer credit sales (5.103) will tend to raise operating costs of credit grantors above current levels. Other things being equal, these provisions would require higher rate ceilings than now exist. If they were not provided, the least credit-worthy consumers now in the market would be relegated to the illegal market.

The rate ceiling declines with the amount of credit granted by design. There are substantial fixed costs in granting consumer instalment credit. Up to a point the relative amount of fixed costs decline as the amount of credit granted increases. The present rate structure is designed not to restrict the amount of credit granted in any size category. Consequently, any changes in the rate ceilings provided would require a complete re-evaluation of the gradation in the structure, as well as of the other above-mentioned sections of this Act which are closely related in an economic sense to this rate ceiling.

2. *Explanation of operation of rate ceilings.* This explanation of maximum rates applies equally to credit service charges made under Section 2.201 and to loan finance charges made under Section 3.508.

It should be made clear that the graduated rates permitted are calculated on the periodic declining unpaid balances. The provisions for graduated rates should not be construed as requiring simultaneous liquidation of different portions of the original unpaid balance. Thus, the 21% annual rate permitted on unpaid balances exceeding $300, but not exceeding $1,000, does not apply to the initial unpaid balance in that range for the scheduled maturity of the loan, but only to the extent that periodic declining unpaid balances fall within the range from $300.01 to $1,000.

The operation of this principle with respect to a $1,500 principal amount of advance for twelve months is illustrated in Table A below. The table shows the total dollar charge, the monthly payments and the charge earned each month when the rates stated in Sections 2.201 and 3.508 are computed on the unpaid balance as of each scheduled payment date and each payment is applied first to the earned charge and then to principal. It also shows the unpaid balances which result from applying the rates stated in Sections 2.201 and 3.508 and the parts of each unpaid balance to which each rate applies each month. The total dollar charge so computed is $211.71, but 3¢ is waived rather than increase the final payment.

TABLE A

Amortization Schedule for $1,500 Paid In Twelve Equal And Consecutive Monthly Installments of Principal And Charge Combined With The Charge Computed At Maximum Graduated Rates Authorized by Sections 2.201 and 3.508—36% Per Year on That Part Of The Unpaid Balances Not Exceeding $300, Plus 21% Per Year On That Part Of The Unpaid Balances Exceeding $300 But Not Exceeding $1,000, Plus 15% Per Year On That Part Of The Unpaid Balances Exceeding $1,000, Yields $211.68.

Mo.	Unpaid Principal Balances Outstanding During Month @ 36%	@ 21%	@ 15%	Total	Application of $142.64 Monthly Payments Charges	Principal
1	$300.00	$700.00	$500.00	$1,500.00	$ 27.50	$ 115.14
2	300.00	700.00	384.86	1,384.86	26.06	116.58
3	300.00	700.00	268.28	1,268.28	24.60	118.04

Mo.	Unpaid Principal Balances Outstanding During Month @ 36%	@ 21%	@ 15%	Total	Application of $142.64 Monthly Payments Charges	Principal
4	300.00	700.00	150.24	1,150.24	23.13	119.51
5	300.00	700.00	30.73	1,030.73	21.63	121.01
6	300.00	609.72	....	909.72	19.67	122.97
7	300.00	486.75	....	786.75	17.52	125.12
8	300.00	361.63	....	661.63	15.33	127.31
9	300.00	234.32	....	534.32	13.10	129.54
10	300.00	104.78	....	404.78	10.83	131.81
11	272.97	....	....	272.97	8.19	134.45
12	138.52	....	....	138.52	4.12*	138.52
TOTALS					$211.68	$1,500.00

Note: Interest rates are applied to parts of unpaid principal balances scheduled to be outstanding. For example, the interest on $1,030.73 is computed as follows:

36% on	$ 300.00 =	$ 9.00
21% on	700.00 =	12.25
15% on	30.73 =	.38
	$1,030.73	$21.63

* The charge earned the last month is $4.15, but 3¢ is waived and applied to principal to make the final payment equal to the others.

For purposes of disclosure under Section 2.304(2) and 3.304(2) the credit grantor must determine the single annual percentage rate which, when applied according to the U. S. rule, earns the same dollar amount of charge that is produced by the graduated rates. Table B shows that an annual rate of 25.10% applied monthly to the periodic declining unpaid balances produces the same total dollar charge of $211.68 calculated by application of graduated rates in Table A.

TABLE B

Amortization Schedule for $1,500 Paid in Twelve Equal And Consecutive Monthly Installments Of Principal and Charge Combined Showing That The Flat Annual Percentage Rate of 25.10% Computed By The U. S. Rule Yields $211.68.

Mo.	Unpaid Principal Balances	Application of $142.64 Monthly Payments Charges	Principal
1	$1,500.00	$ 31.38	$ 111.26
2	1,388.74	29.05	113.59
3	1,275.15	26.67	115.97
4	1,159.18	24.25	118.39
5	1,040.79	21.77	120.87
6	919.92	19.24	123.40
7	796.52	16.66	125.98
8	670.54	14.03	128.61
9	541.93	11.34	131.30
10	410.63	8.59	134.05
11	276.58	5.79	136.85
12	139.73	2.91*	139.73
		$211.68	$1,500.00

* The charge earned the last month is $2.92, but 1¢ is waived and applied to principal to make the final payment equal to the others.

The Code is intended to give the creditors the following choices in making their charges under Section 2.201 and Section 3.508:

(1) The contract may be precomputed to include the dollar finance charge for payment according to schedule. In the example shown, the dollar finance charge of $211.68 would be added to the original unpaid principal, making a total of $1,711.68 to be repaid in twelve monthly instalments of $142.64.

A precomputed contract is subject to rebate for prepayment in full and to default and deferment charges in the case of delinquency or deferral. In such cases the creditor has the option (a) to rebate according to Section 2.210 or 3.210 and to make default or deferment charges according to Sections 2.203 and 2.204 or 3.203 and 3.204, *or* (b) to recompute charges at the flat annual percentage rate which yields the precomputed charge when computed according to the U. S. rule. (In the example shown that rate is 25.10%.) Under this second option, the flat annual percentage rate would be computed on the actual unpaid balances of the original principal amount (excluding precomputed charge) for the actual time outstanding and the total charge so computed would be in lieu of the precomputed charge and default and deferment charges. In the case of a precomputed loan (but not sale), if two or more instalments are delinquent ten days, the lender may convert to the flat annual percentage rate (or graduated rates) as of the due date of the first delinquent instalment rather than recompute from the beginning. See Section 3.203(4). The conversion is by rebating the precomputed charge as of the due date of the first delinquent instalment. Charges at the flat annual percentage rate on unpaid balances after conversion are in lieu of the rebate and subsequent default and deferment charges.

(2) The agreement may call for the maximum flat annual rate of charge (or lesser annual flat rate) computed on actual unpaid balances for the actual time outstanding. The flat annual percentage is the rate which yields the charge for payment according to schedule when the rate is computed according to the U. S. rule. In the example, the rate is 25.10%. In this case there is no rebate for prepayment in full because the charges are collected only as earned, and there are no separate charges for default or deferment.

(3) The agreement may call for the computation of the graduated rates on parts of the actual unpaid balance for the time actually outstanding when each payment is made. In this case there is no rebate for prepayment in full because charges are collected only as earned, and there are no separate charges for default or deferment.

(4) In the case of a credit service charge for revolving charge accounts, the charge for each period must be computed on the parts of the unpaid balance from time to time as defined in Section 2.207(2). In the case of a revolving loan account, the charge for each period must be computed on the parts of the unpaid balance from time to time as defined in Section 3.201(4).

3. *Explanation of subsection (5).* With respect to Section 2.201(5), the variation permitted is limited to 8 per cent of the *rate* of the finance charge and does not permit an 8 *percentage point* variation. For example, if a credit grantor were to levy an annual add-on finance charge of $10 per $100 of initial unpaid balance, under the provisions of this section he could establish the following maximum range for one-year contracts:

Amount Financed	Credit Service Charge
$92.40-$107.60	$10.00

The median amount financed is $100.00; that is, this amount is $7.60 from both the upper and lower limits of the specified range. Alternatively, it is just halfway between $92.40 and $107.60.

The specified range is limited by the 8 per cent requirement. On one-year contracts the add-on finance charge results in an actuarial rate of 17.972 per cent. Subparagraph (b) specifies that the yield on the lowest amount within the range may not be more than 8 per cent higher than the yield provided on the median amount. Thus the yield on the lowest amount may not exceed 19.410 per cent ($.08 \times 17.972 + 17.972 = 19.410$). It follows that the lower amount must be such that the $10 credit service charge produces an annual rate not in excess of 19.410 per cent. Interpolation from annuity tables shows that the lower amount must be about $92.40. Since the median is halfway between the upper and lower limits, the upper amount must be $107.60. These are close approximations; in actual practice very precise limits can be determined.

To gain the convenience of using a single dollar amount of credit service charge for a specified range of amounts financed the credit grantor must undercharge for amounts financed above the median. Thus the $10 credit service charge is $0.76 less than the $10.76 credit service charge that could have

been received by precise application of an add-on rate of $10 per $100 per annum on the initial unpaid balance. These results are summarized below for one-year monthly instalment contracts.

(A) Amount financed	(B) Actual finance charge	(C) Accurate finance charge	(D) Dollar difference (C) — (B)	(E) Annual percentage
$107.60	$10.00	$10.76	—$0.76	16.73%
$100.00	$10.00	$10.00	0.00	17.97%
$ 92.40	$10.00	$ 9.24	+$0.76	19.41%

4. *Explanation of subsection (6).* Subsection (6) of this section permits minimum charges equal to those for which the CCPA requires no annual percentage rate disclosure. The CCPA does not set limits on the amounts of minimum charges, but does require annual percentage rate disclosure when the minimum charges exceed those permitted by subsection (6). Subsection (6) also sets limits on the amounts of minimum charges.

[¶ 826] Additional Charges

Sec. 2.202. (1) In addition to the credit service charge permitted by this Part, a seller may contract for and receive the following additional charges in connection with a consumer credit sale:

(a) official fees and taxes;

(b) charges for insurance as described in subsection (2); and

(c) charges for other benefits, including insurance, conferred on the buyer, if the benefits are of value to him apart from the granting of the credit, the charges are reasonable in relation to the benefits, and the Administrator has by rule determined that the charges are permissible additional charges.

(2) An additional charge may be made for insurance written in connection with the sale, other than insurance protecting the seller against the buyer's default or other credit loss,

(a) with respect to insurance against loss of or damage to property, or against liability, if the seller furnishes a clear and specific statement in writing to the buyer, setting forth the cost of the insurance if obtained from or through the seller, and stating that the buyer may choose the person through which the insurance is to be obtained; and

(b) with respect to consumer credit insurance providing life, accident or health coverage, if the insurance coverage is not a factor in the approval by the seller of the extension of credit and this fact is clearly disclosed in writing to the buyer, and if, in order to obtain the insurance in connection with the extension of credit, the buyer gives specific affirmative written indication of his desire to do so after written disclosure to him of the cost thereof.

(3) For the purposes of the Part on Disclosure and Advertising (Part 3), if the credit service charge with respect to a sale of an interest in land does not exceed 10 per cent per year (paragraph (b) of subsection (2) of Section 2.104), reasonable closing costs even though not within subsection (1) may be treated as additional charges.

COMMENT

Paragraph (c) of subsection (1), above, sets standards to be observed by the Administrator in determining whether charges are permissible additional charges pursuant to paragraph (c). These standards conform to the legislative history of CCPA Section 106 (d)(4) as indicated in the "Statement of Managers" on page 25 of the Conference Report on the CCPA under the heading "Other Charges." Section 6.104(2) of this

Code directs the Administrator to take into account federal regulations on the subject before adopting his rules.

CCPA Section 106(b) requires that charges or premiums for insurance be included in the "finance charge" for the purposes of disclosing the annual percentage rate or corresponding nominal annual percentage rate unless the insurance meets the tests specified in paragraph (a) or paragraph (b) of subsection (2). The effect of subsection (2) is to require that charges or premiums for insurance be included in the credit service charge for ceilings purposes as well unless the insurance meets the tests specified in paragraph (a) or paragraph (b) of subsection (2).

[¶ 827] Delinquency Charges

Sec. 2.203. (1) With respect to a precomputed consumer credit sale, refinancing, or consolidation, the parties may contract for a delinquency charge on any instalment not paid in full within 10 days after its scheduled due date in an amount not exceeding the greater of

(a) an amount, not exceeding $5, which is 5 per cent of the unpaid amount of the instalment, or

(b) the deferral charge (subsection (1) of Section 2.204) that would be permitted to defer the unpaid amount of the instalment for the period that it is delinquent.

(2) A delinquency charge under paragraph (a) of subsection (1) may be collected only once on an instalment however long it remains in default. No delinquency charge may be collected if the instalment has been deferred and a deferral charge (Section 2.204) has been paid or incurred. A delinquency charge may be collected at the time it accrues or at any time thereafter.

(3) No delinquency charge may be collected on an instalment which is paid in full within 10 days after its scheduled instalment due date even though an earlier maturing instalment or a delinquency charge on an earlier instalment may not have been paid in full. For purposes of this subsection payments are applied first to current instalments and then to delinquent instalments.

(4) The amount of $5 in subsection (1) is subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

COMMENT

It should be noted that this section and later sections providing for deferral charges (Section 2.204), credit service charge upon refinancing (2.205), and rebate upon prepayment (2.210) apply only to precomputed sales. When a credit service charge is precomputed, the calculations are based on the assumption that all scheduled payments will be made when due (2.201(3)). If a buyer is late in making a payment on a precomputed sale, the seller would receive no income for the period of the delay unless a separate delinquency charge were permitted. The alternative of not permitting delinquency charges is rejected, because the result would be to enforce a lower effective ceiling on credit service charge rates for delinquent buyers than for buyers who paid promptly. The same line of reasoning that calls for a delinquency charge also supports rebates of appropriate portions of the credit service charge upon prepayment (2.210). Instead of paying behind schedule, the buyer is paying ahead of schedule. Consequently, he is entitled to a rebate of a portion of the prescheduled credit service charge.

The adjustments to the precomputed credit service charge permitted in these sections are not needed for revolving charge accounts. In general, the credit service charge accumulates in direct relation to the size of the unpaid balance and the period for which it has been outstanding. If the buyer is late in making a payment the credit service charge continues to accumulate, so that the seller is compensated for his forbearance. Similarly, the buyer may prepay the sale at any time and is obligated to pay only the credit service charge that has accumulated to the date of prepayment.

[¶ 828] Deferral Charges

Sec. 2.204. (1) With respect to a precomputed consumer credit sale, refinancing or consolidation, the parties before or after default may agree in writing to defer payment of all or part of one or more unpaid instalments, and the seller may make and collect a charge not exceeding the rate previously stated to the buyer pursuant to the provisions on disclosure (Part 3) applied to the amount or amounts deferred for the period of deferral calculated without regard to differences in lengths of months, but proportionally for a part of a month, counting each day as 1/30 of a month. A deferral charge may be collected at the time it is assessed or at any time thereafter.

(2) The seller may, in addition to the deferral charge, make appropriate additional charges (Section 2.202), and the amount of these charges which is not paid in cash may be added to the amount deferred for the purpose of calculating the deferral charge.

(3) The parties may agree in writing at the time of a precomputed consumer credit sale, refinancing, or consolidation that if an instalment is not paid within 10 days after its due date, the seller may unilaterally grant a deferral and make charges as provided in this section. No deferral charge may be made for a period after the date that the seller elects to accelerate the maturity of the agreement.

(4) A delinquency charge made by the seller on an instalment may not be retained if a deferral charge is made pursuant to this section with respect to the period of delinquency.

[¶ 829] Credit Service Charge on Refinancing

Sec. 2.205. With respect to a consumer credit sale, refinancing, or consolidation, the seller may by agreement with the buyer refinance the unpaid balance and may contract for and receive a credit service charge based on the amount financed resulting from the refinancing at a rate not exceeding that permitted by the provisions on credit service charge for consumer credit sales (Section 2.201). For the purpose of determining the credit service charge permitted, the amount financed resulting from the refinancing comprises the following:

(1) if the transaction was not precomputed, the total of the unpaid balance and accrued charges on the date of refinancing, or, if the transaction was precomputed, the amount which the buyer would have been required to pay upon prepayment pursuant to the provisions on rebate upon prepayment (Section 2.210) on the date of refinancing, except that for the purpose of computing this amount no minimum credit service charge (subsection (6) of Section 2.201) shall be allowed; and

(2) appropriate additional charges (Section 2.202), payment of which is deferred.

[¶ 830] Credit Service Charge on Consolidation

Sec. 2.206. If a buyer owes an unpaid balance to a seller with respect to a consumer credit sale, refinancing, or consolidation, and becomes obligated on another consumer credit sale, refinancing, or consolidation, with the same seller, the parties may agree to a consolidation resulting in a single schedule of payments pursuant to either of the following subsections:

(1) The parties may agree to refinance the unpaid balance with respect to the previous sale pursuant to the provisions on refinancing (Section 2.205)

and to consolidate the amount financed resulting from the refinancing by adding it to the amount financed with respect to the subsequent sale. The seller may contract for and receive a credit service charge based on the aggregate amount financed resulting from the consolidation at a rate not exceeding that permitted by the provisions on credit service charge for consumer credit sales (Section 2.201).

(2) The parties may agree to consolidate by adding together the unpaid balances with respect to the two sales.

COMMENT

Refinancing under Section 2.205 means that the balance owing is treated as though it is prepaid, with the buyer being credited with all refunds; a credit service charge is then calculated on the basis of the balance owing less refunds. Consolidation, which is covered in 2.206, refers to the process of adding together amounts owing with respect to more than one sale. There are two ways of consolidating and both are described in 2.206. Subsection (1) involves the familiar rewrite; the old balance is refinanced and added to the amount financed under the new sale. The credit service charge is based on the aggregate amounts financed. Under subsection (2) no refinancing is involved. The *balances owing* are simply added together and made payable on one schedule of payments. This usually means that the maturity of the first sale will be extended.

[¶ 831] Credit Service Charge for Revolving Charge Accounts

Sec. 2.207. (1) With respect to a consumer credit sale made pursuant to a revolving charge account, the parties to the sale may contract for the payment by the buyer of a credit service charge not exceeding that permitted in this section.

(2) A charge may be made in each billing cycle which is a percentage of an amount no greater than

(a) the average daily balance of the account,

(b) the unpaid balance of the account on the same day of the billing cycle, or

(c) the median amount within a specified range within which the average daily balance of the account or the unpaid balance of the account on the same day of the billing cycle is included. A charge may be made pursuant to this paragraph only if the seller, subject to classifications and differentiations he may reasonably establish, makes the same charge on all balances within the specified range and if the percentage when applied to the median amount within the range does not produce a charge exceeding the charge resulting from applying that percentage to the lowest amount within the range by more than 8 per cent of the charge on the median amount.

(3) If the billing cycle is monthly, the charge may not exceed 2 per cent of that part of the amount pursuant to subsection (2) which is $500 or less and 1½ per cent on that part of this amount which is more than $500. If the billing cycle is not monthly, the maximum charge is that percentage which bears the same relation to the applicable monthly percentage as the number of days in the billing cycle bears to 30. For the purposes of this section, a variation of not more than 4 days from month to month is "the same day of the billing cycle."

(4) Notwithstanding subsection (3), if there is an unpaid balance on the date as of which the credit service charge is applied, the seller may contract for and receive a charge not exceeding 50¢, if the billing cycle is monthly or longer, or the pro rata part of 50¢ which bears the same relation to 50¢ as the number of days in the billing cycle bears to 30, if the billing cycle is shorter than monthly.

(5) The amounts of $500 in subsection (3) are subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

COMMENT

CCPA Section 127(b)(6) requires the disclosure of the finance charge on open end credit plans in terms of an annual percentage rate if "the total finance charge exceeds 50¢ for a monthly or longer billing cycle, or the pro rata part of 50¢ for a billing cycle shorter than monthly." It would for all practical purposes be impossible to express a minimum charge in terms of an annual percentage rate. Consequently, subsection (4) prescribes as the minimum the amount of the charge for which the CCPA requires no annual percentage rate disclosure. It also prescribes the method of calculating the pro rata part of the permitted minimum charge when the billing cycle is less than one month.

[¶ 832] Advances to Perform Covenants of Buyer

Sec. 2.208. (1) If the agreement with respect to a consumer credit sale, refinancing, or consolidation contains covenants by the buyer to perform certain duties pertaining to insuring or preserving collateral and the seller pursuant to the agreement pays for performance of the duties on behalf of the buyer, he may add the amounts paid to the debt. Within a reasonable time after advancing any sums, he shall state to the buyer in writing the amount of the sums advanced, any charges with respect to this amount, and any revised payment schedule and, if the duties of the buyer performed by the seller pertain to insurance, a brief description of the insurance paid for by the seller including the type and amount of coverages. No further information need be given.

(2) A credit service charge may be made for sums advanced pursuant to subsection (1) at a rate not exceeding the rate stated to the buyer pursuant to the provisions on disclosure (Part 3) with respect to the sale, refinancing, or consolidation, except that with respect to a revolving charge account the amount of the advance may be added to the unpaid balance of the account and the seller may make a credit service charge not exceeding that permitted by the provisions on credit service charge for revolving charge accounts (Section 2.207).

[¶ 833] Right to Prepay

Sec. 2.209. Subject to the provisions on rebate upon prepayment (Section 2.210), the buyer may prepay in full the unpaid balance of a consumer credit sale, refinancing, or consolidation at any time without penalty.

[¶ 834] Rebate Upon Prepayment

Sec. 2.210. (1) Except as provided in subsection (2), upon prepayment in full of the unpaid balance of a precomputed consumer credit sale, refinancing, or consolidation, an amount not less than the unearned portion of the credit service charge calculated according to this section shall be rebated to the buyer. If the rebate otherwise required is less than $1, no rebate need be made.

(2) Upon prepayment in full of a consumer credit sale, refinancing, or consolidation, other than one pursuant to a revolving charge account, if the credit service charge then earned is less than any permitted minimum credit service charge (subsection (6) of Section 2.201) contracted for, whether or not the sale, refinancing, or consolidation is precomputed, the seller may collect or retain the minimum charge, as if earned, not exceeding the credit service charge contracted for.

(3) Except as otherwise provided in this subsection with respect to a sale of an interest in land or a consumer credit sale secured by an interest in land, the unearned portion of the credit service charge is a fraction of the credit service charge of which the numerator is the sum of the periodic balances scheduled to follow the computational period in which prepayment occurs, and the denominator is the sum of all periodic balances under either the sale agreement or, if the balance owing resulted from a refinancing (Section 2.205) or a consolidation (Section 2.206), under the refinancing agreement or consolidation agreement. In the case of a sale of an interest in land or a consumer credit sale secured by an interest in land, reasonable sums actually paid or payable to persons not related to the seller for customary closing costs included in the credit service charge are deducted from the credit service charge before the calculation prescribed by this subsection is made.

COMMENT

Subsection (3), together with paragraph (a) of subsection (4), states the "Rule of 78" with respect to a sale, refinancing or consolidation payable in equal instalments at equal intervals from the date of the sale, refinancing or consolidation to the final scheduled payment date. In the case of such a sale, refinancing or consolidation, "computational period" may read as "scheduled payment period", and the provisions relating to irregular payment schedules, viz., paragraphs (b), (c) and (d) of subsection (4) and subsection (5) in its entirety, may be disregarded.

(4) In this section

(a) "periodic balance" means the amount scheduled to be outstanding on the last day of a computational period before deducting the payment, if any, scheduled to be made on that day;

(b) "computational period" means one month if one-half or more of the intervals between scheduled payments under the agreement is one month or more, and otherwise means one week;

(c) the "interval" to the due date of the first scheduled instalment or the final scheduled payment date is measured from the date of a sale, refinancing, or consolidation, or any later date prescribed for calculating maximum credit service charges (subsection (4) of Section 2.201), and includes either the first or last day of the interval;

(d) if the interval to the due date of the first scheduled instalment does not exceed one month by more than 15 days when the computational period is one month, or 11 days when the computational period is one week, the interval shall be considered as one computational period.

(5) This subsection applies only if the schedule of payments is not regular (subsection (6) of Section 2.304).

(a) If the computational period is one month and

(i) if the number of days in the interval to the due date of the first scheduled instalment is less than one month by more than 5 days, or more than one month by more than 5 but not more than

15 days, the unearned credit service charge shall be increased by an adjustment for each day by which the interval is less than one month and, at the option of the seller, may be reduced by an adjustment for each day by which the interval is more than one month; the adjustment for each day shall be 1/30th of that part of the credit service charge earned in the computational period prior to the due date of the first scheduled instalment assuming that period to be one month; and

(ii) if the interval to the final scheduled payment date is a number of computational periods plus an additional number of days less than a full month, the additional number of days shall be considered a computational period only if 16 days or more. This subparagraph applies whether or not subparagraph (i) applies.

(b) Notwithstanding paragraph (a), if the computational period is one month, the number of days in the interval to the due date of the first instalment exceeds one month by not more than 15 days, and the schedule of payments is otherwise regular, the seller may, at his option, exclude the extra days and the charge for the extra days in computing the unearned credit service charge; but if he does so and a rebate is required before the due date of the first scheduled instalment, he shall compute the earned charge for each elapsed day as 1/30th of the amount the earned charge would have been if the first interval had been one month.

(c) If the computational period is one week and

(i) if the number of days in the interval to the due date of the first scheduled instalment is less than 5 days, or more than 9 days but not more than 11 days, the unearned credit service charge shall be increased by an adjustment for each day by which the interval is less than 7 days and, at the option of the seller, may be reduced by an adjustment for each day by which the interval is more than 7 days; the adjustment for each day shall be 1/7th of that part of the credit service charge earned in the computational period prior to the due date of the first scheduled instalment assuming that period to be one week; and

(ii) if the interval to the final scheduled payment date is a number of computational periods plus an additional number of days less than a full week, the additional number of days shall be considered a computational period only if 4 days or more. This subparagraph applies whether or not subparagraph (i) applies.

(6) If a deferral (Section 2.204) has been agreed to, the unearned portion of the credit service charge shall be computed without regard to the deferral. The amount of deferral charge earned at the date of prepayment shall also be calculated. If the deferral charge earned is less than the deferral charge paid, the difference shall be added to the unearned portion of the credit service charge. If any part of a deferral charge has been earned but has not been paid, that part shall be subtracted from the unearned portion of the credit service charge, or shall be added to the unpaid balance.

(7) This section does not preclude the collection or retention by the seller of delinquency charges (Section 2.203).

(8) If the maturity is accelerated for any reason and judgment is obtained, the buyer is entitled to the same rebate as if payment had been made on the date judgment is entered.

(9) Upon prepayment in full of a consumer credit sale by the proceeds of consumer credit insurance (Section 4.103), the buyer or his estate is entitled to the same rebate as though the buyer had prepaid the agreement on the date the proceeds of the insurance are paid to the seller, but no later than 10 business days after satisfactory proof of loss is furnished to the seller.

COMMENT

Subsection (9) applies only in the case of consumer credit insurance as defined in Section 4.103, *i.e.*, insurance over which the creditor has partial control, and resolves a question under prior law. When a consumer credit sale is prepaid in full by proceeds of insurance other than consumer credit insurance, the prior provisions of Section 2.210 apply. Examples of the application of Section 2.210 follow:

Example 1:

Time sale contract executed July 1, 1968, and goods delivered the same day. Payable in 12 equal monthly payments beginning August 1, 1968.

1. Sale price is $1,000.00, credit service charge is $71.24, and the monthiy payment is $89.27. Debtor prepays in full on October 1, 1968.

a. The "computational period" is one month (subsection (4)(b)). The "interval to the due date of the first instalment" starts July 1 (subsection (4)(c) and subsection (4) of Section 2.201) and, being one month, constitutes one computational period. No part of subsection (5) is applicable.

The denominator of the fraction called for by subsection (3) is therefore the sum of the 12 scheduled unpaid balances as of the last days of the months of July, 1968, through June, 1969, *before* deducting the payments scheduled for those days (subsection (4)(a)).

Sum of 12 balances (1,071.24; 981.97; 892.70 . . . 89.27) = 6,963.06.

b. The computational periods in the numerator of the fraction called for by subsection (3) begin with the one starting on October 2, 1968, so the numerator is the sum of the nine scheduled unpaid balances as of the first days of the months of November, 1968, through July, 1969, *before* deducting the payments scheduled for those days (subsection (4)(a)).

Sum of nine balances (803.43; 714.16; 624.89 . . . 89.27) = 4,017.15.

c. Refund is $\frac{4{,}017.15}{6{,}963.06} \times 71.24 = \$41.10$

Example 2:

Time sale contract executed July 1, 1968, and goods delivered same day. Payable in 26 equal weekly payments beginning July 8. Sale price is $400.00, credit service charge is $31.60, and the weekly payment is $16.60. Debtor prepays in full on July 29, 1968.

a. The "computational period" is one week (subsection (4)(b)). The "interval to the due date of the first instalment" starts July 1 (subsection (4)(c) and subsection (4) of Section 2.201) and, being one week, constitutes one computational period. No part of subsection (5) is applicable.

The denominator of the fraction called for by subsection (3) therefor is the sum of the 26 scheduled unpaid balances as of July 8, 15, 22, 29 and so on, *before* deducting the payments scheduled for those days (subsection (4)(a)).

Sum of 26 balances (431.60, 415.00, 398.40, . . ., 16.60) = 5,826.60.

b. The computational periods in the numerator of the fraction called for by subsection (3) begin with the one starting on July 30, so the numerator is the sum of the 22 scheduled unpaid balances beginning August 5, 1968, *before* deducting the payments scheduled for those days (subsection (4)(a)).

Sum of 22 balances (365.20, 348.60 . . . 16.60) = 4,199.80.

c. Refund is $\frac{4{,}199.80}{5{,}826.60} \times 3.160 = \$22.78$

Example 3:

Time sale executed June 26, 1968, and goods delivered July 9, 1968. Payable in 12 equal monthly payments beginning August 15. Sale price is $1,000.00, credit service charge is $71.24, and the monthly payment is $89.27. Debtor prepays in full on November 10, 1968.

a. The "computational period" is one month (subsection (4)(b)). The "interval to the due date of the first instalment" starts July 9 (subsection (4)(c) and subsection (4) of Section 2.201) and constitutes one computational period (subsection (4)(d)). Since the interval is 37 days, the seller has the option of reducing the rebate by an adjustment for seven days (subsection (5)(a)(i)). Subsection (5)(a)(ii) does not apply.

The denominator of the fraction called for by subsection (3) therefore is the sum of the 12 scheduled unpaid balances as of the 15th days of the months of August through July *before* deducting the payment scheduled for those days (subsection (4)(a)).

Sum of 12 balances (1,071.24; 981.97; 892.70 . . . 89.27) = 6,963.06.

The adjustment is found by taking 7/30 of the credit service charge earned in the computational period to the first scheduled due date or:

$$\frac{7}{30} \times \frac{\text{Beginning balance}}{\text{Denominator as determined above}} \times \text{Credit Service Charge.}$$

$$\frac{7}{30} \times \frac{1{,}071.24}{6{,}963.06} \times 71.24 = \$2.56.$$

b. The computational periods in the numerator of the fraction called for by subsection (3) begin with the one starting on November 16 (subsection (3)) so the numerator is the sum of the eight scheduled balances as of the 15th of the months of December, 1968, through July, 1969, *before* deducting the payment scheduled for that day.

Sum of eight balances (714.16; 624.89; 535.62 . . . 89.27) = 3,213.72.

c. Refund is $\frac{3{,}213.72}{6{,}963.06} \times 71.24 = \$32.88.$

$32.88 minus adjustment of $2.56 = $30.32.

Example 4:

Time sale executed June 28, 1968, and goods delivered July 3, 1968. Payable in 26 weekly payments beginning July 8. Sale price is $400.00, credit service charge is $31.60, and the weekly payment is $16.60. Debtor prepays in full on July 23, 1968.

a. The "computational period" is one week (subsection (4)(b)). The "interval to the due date of the first instalment" starts June 28 (subsection (4)(c) and subsection (4) of Section 2.201) and constitutes one computational period (subsection (4)(d)). Since the interval is ten days, the seller has the option of reducing the rebate by an adjustment for three days (subsection (5)(b)(i)). Subsection (5)(b)(ii) does not apply.

The denominator of the fraction called for by subsection (3) therefore is the sum of the 26 scheduled unpaid balances as of July 8, 15, 22 and 29 and so on, *before* deducting the payments scheduled for those days (subsection (4)(a)).

Sum of 26 balances (431.60; 415.00; 398.40 . . . 16.60) = 5,826.60.

The adjustment is found by taking 3/7 of the credit service charge earned in the computational period to the first scheduled due date or:

$$\frac{3}{7} \times \frac{\text{Beginning balance}}{\text{Denominator as determined above}} \times \text{Credit service charge.}$$

$$\frac{3}{7} \times \frac{431.60}{5{,}826.60} \times 31.60 = \$1.00.$$

b. The computational periods in the numerator of the fraction called for by subsection (7) begin with the one starting July 30, so the numerator is the sum of the 22 scheduled unpaid balances beginning August 5, 1968, *before* deducting the payments scheduled for those days (subsection (1)(a)).

Sum of 22 balances (365.20; 348.60 . . . 16.60) = 4,199.80.

c. Refund is $\frac{4{,}199.80}{5{,}826.60} \times 31.60 = 22.78.$

$22.78 minus adjustment of $1.00 = $21.78.

Example 5:

Time sale executed July 9, 1968, and the goods delivered July 12, 1968. Payments scheduled on November 15, 1968 and November 15, 1969. Sale price is $1,000.00, credit service charge is $104.36, and each of the two payments is $552.18. Debtor prepays on January 10, 1969.

a. The "computational period" is one month (subsection (4)(b)). The "interval to the due date of the first instalment" starts on July 9, 1968 (subsection (4) of Section 2.201) and is more than 45 days, so the special rule of subsection (4)(d) and the adjustment of subsection (5)(a)(i) do not apply. The interval to the final scheduled payment date is 16 months and six days. The additional days, being less than 16, are disregarded (subsection (5)(a)(ii)).

The denominator of the fraction called for by subsection (3) therefore is the sum of the 16 scheduled unpaid balances as of the 8th days of the months of August, 1968, through November, 1969 (subsection (4)(a)).

Balance of $1,104.36 for four computational periods	= $ 4,417.44
Balance of $552.18 for 12 computational periods	= 6,626.16
Total denominator	$11,043.60

b. The computational periods in the numerator of the fraction called for by subsection (3) begin with the one starting on February 9, 1969, so the numerator is the sum of the nine scheduled unpaid balances as of the 8th days of the months of March through November, 1969.

Balance of $552.18 for nine computational periods $4,969.62.

c. Refund is $\frac{\$\ 4,969.62}{\$11,043.60} \times 104.36 = \$46.96$

Example 6:

Same facts as in Example 5, except the debtor did not pay the installment due 11/15/68 in full, but paid $184.18 (approximately 1/3 of the installment) and was permitted to defer the rest ($368.00) until March 15 (four months). A deferral charge of $17.00 was assessed, so the amount coming due March 15 is $385.00. Debtor prepays in full on 10 January 1969.

a. Compute the rebate of credit service charge as though the extension had not occurred (subsection (6)) and as though the balances had been reduced as *scheduled* (subsection (4)(a)). The computations are the same as in Example 5 and the rebate of credit service charge is $46.96 as in Example 5.

b. Compute also the rebate of unearned deferral charge. Of the 120 days of the extension period 64 remained at the time of the prepayment so the rebate of deferral charge is:

$$\frac{64}{120} \times 17 = \$9.07$$

PART 3—DISCLOSURE AND ADVERTISING

[¶ 835] Applicability; Information Required

Sec. 2.301. (1) For purposes of this Part, consumer credit sale includes the sale of an interest in land without regard to the rate of the credit service charge if the sale is otherwise a consumer credit sale (Section 2.104).

(2) The seller shall disclose to the buyer to whom credit is extended with respect to a consumer credit sale the information required by either

(a) this Part, or

(b) except with respect to a consumer credit sale of an interest in land or secured by an interest in land, the Federal Consumer Credit Protection Act.

(3) For the purposes of paragraph (b) of subsection (2), information which would otherwise be required pursuant to the Federal Consumer Credit Protection Act is sufficient even though the transaction is one of a class of credit transactions exempted from that Act pursuant to a determination by the Board of Governors of the Federal Reserve System that the class of transactions is subject under the law of this State to requirements substantially similar to those imposed under that Act.

(4) The lessor shall disclose to the lessee to whom credit is extended with respect to a consumer lease the information required by this Part.

[¶ 836] General Disclosure Requirements and Provisions

Sec. 2.302. (1) The disclosure by this Part

(a) shall be made clearly and conspicuously;

(b) shall be in writing, a copy of which shall be delivered to the buyer or lessee, but need not be contained in a single writing nor made in the order set forth in this Part;

(c) may use terminology different from that employed in this Part if it conveys substantially the same meaning;

(d) may be supplemented by additional information or explanations supplied by the seller or lessor;

(e) need be made only to the extent applicable and only as to those items for which the seller or lessor makes a separate charge to the buyer or lessee;

(f) shall be made on the assumption that all scheduled instalments are paid when due; and

(g) comply with this Part although rendered inaccurate by any act, occurrence, or agreement subsequent to the required disclosure.

(2) Except with respect to sales made by telephone or mail (Section 2.305) and consolidations (Section 2.308),

(a) the disclosures required by this Part shall be made before credit is extended, but may be made in the sale, refinancing, or consolidation agreement, lease, or other evidence of indebtedness to be signed by the buyer or lessee if set forth conspicuously therein, and need be made only to one buyer or lessee if there are more than one, and

(b) if an evidence of indebtedness is signed by the buyer or lessee, the seller or lessor shall give him a copy when the writing is signed.

(3) Except as provided with respect to rescission by a buyer (Section 5.204) and civil liability for violations of disclosure provisions (subsection (4) of Section 5.203), written acknowledgment of receipt by a buyer or lessee to whom a statement is required to be given pursuant to this Part

(a) in an action or proceeding by or against the original seller or lessor, creates a presumption that the statement was given, and

(b) in an action or proceeding by or against an assignee without knowledge to the contrary when he acquires the obligation, is conclusive proof of the delivery of the statement and, unless the violation is apparent on the face of the statement, of compliance with this Part.

[¶ 837] Overstatement

Sec. 2.303. The disclosure of an amount or percentage which is greater than the amount or percentage required to be disclosed under this Part does not in itself constitute a violation of this Part if the overstatement is not materially misleading and is not used to avoid meaningful disclosure.

COMMENT

This section is derived from CCPA Sections 103(1) and 107(b).

[¶ 838] Calculation of Rate to Be Disclosed

Sec. 2.304. (1) Except as otherwise specifically provided, if a seller is required to give to a buyer a statement of the rate of the credit service charge he shall state the rate in terms of an annual percentage rate as defined in subsection (2) or in terms of a corresponding nominal annual percentage rate as defined in subsection (3), whichever is appropriate.

(2) "Annual percentage rate"

(a) with respect to a consumer credit sale other than one made pursuant to a revolving charge account, is either

(i) that nominal annual percentage rate which, when applied to the unpaid balances of the amount financed calculated according to the United States rule, will yield a sum equal to the amount of the credit service charge, or

(ii) that rate determined by any method prescribed by the Administrator as a method which materially simplifies computation while retaining reasonable accuracy as compared with the rate determined pursuant to subparagraph (i);

(b) with respect to a consumer credit sale made pursuant to a revolving charge account, is the quotient expressed as a percentage of the total credit service charge for the period to which it relates divided by the amount upon which the credit service charge for that period is based, multiplied by the number of these periods in a year; if the period is one day, the number of periods in a year is deemed to be 360.

(3) "Corresponding nominal annual percentage rate" is the percentage or percentages used to calculate the credit service charge for one billing cycle or other period pursuant to a revolving charge account multiplied by the number of billing cycles or periods in a year; if the period is one day, the number of periods in a year is deemed to be 360.

(4) If a seller is permitted to make the same credit service charge for all amounts financed within a specified range (subsection (5) of Section 2.201) or for all balances within a specified range (subsection (2) of Section 2.207), he shall state the annual percentage rate or corresponding nominal annual percentage rate, whichever is appropriate, as applied to the median amount of the range within which the actual amount financed or balance is included.

(5) If a debt is payable on a schedule of instalment payments which is regular except for one or more of the following irregularities:

(a) the amount of one instalment payment is not substantially equal to the amount of each of the other instalment payments;

(b) the interval between the date the credit is granted and the first instalment payment is not equal to the interval between instalment payments; or

(c) in one or more payment periods no instalment payment is due, not exceeding one-fourth of the payment periods in any year if the length of the term of the agreement is a year or more, or one-fourth of the payment periods if the length of the term of the agreement is less than a year, the seller may, at his option, calculate the rate to be disclosed as if the debt were payable under an agreement having the same amount financed, the same length of term to the nearest full scheduled payment period, and a regular schedule of payments having the same interval between payments as the interval between the majority of instalments as scheduled in the sale agreement.

(6) A schedule of payments is regular if (a) the instalment payments other than the down payment are substantially equal in amount, (b) the interval between instalment payments is one month, or the intervals between instalment payments are equal and less than one month, and (c) the interval between the date the credit is granted and the first instalment payment is equal to the interval between instalment payments.

(7) If the credit service charge does not begin to accrue until after the date the credit is granted, the seller may, at his option, calculate the rate to be disclosed on the basis of the period between the date when the credit service

charge begins to accrue and the date of the final payment under the agreement, and, if he does so, he shall inform the buyer of the date when the credit service charge begins to accrue.

(8) A statement of rate complies with this Part if it does not vary from the accurately computed rate by more than the following tolerances:

(a) the annual percentage rate may be rounded to the nearest quarter of 1 per cent for consumer credit sales payable in substantially equal instalments when a seller determines the total credit service charge on the basis of a single add-on, discount, periodic, or other rate, and the rate is converted into an annual percentage rate under procedures prescribed by the Administrator;

(b) the Administrator may authorize the use of rate tables or charts which may provide for the disclosure of annual percentage rates which vary from the rate determined in accordance with paragraph (a) by not more than the tolerances the Administrator may allow; the Administrator may not allow a tolerance greater than 8 per cent of that rate except to simplify compliance where irregular payments are involved; and

(c) in case a seller determines the annual percentage rate in a manner other than as described in paragraph (a) or (b), the Administrator may authorize other reasonable tolerances.

COMMENT

1. Definition of "annual percentage rate" is derived from CCPA Section 107(a). The definition "corresponding nominal annual percentage rate" is derived from CCPA Section 127(a)(4) and (b)(5). Subsections (5) - (7) are intended to deal with irregular contracts and are subject to approval by the Board. Subsection (8) is derived from CCPA Section 107(c) - (e).

2. The assumption underlying the United States rule is that a periodic payment is applied first to the unpaid credit service charge. If the payment exceeds the unpaid credit service charge, the remainder of the payment is applied to reduce the unpaid balance of the amount financed. This procedure is based upon *Story v. Livingston*, 38 U. S. 359 (1839).

To illustrate the application of this rule assume that the amount financed on a four-month contract is $500, and that the credit service charge is $12.56. Four monthly payments of $128.14 are contemplated. Thus the amount financed ($500) plus the credit service charge ($12.56) equals the original unpaid balance ($512.56), which is divided into four equal monthly payments, the first payment being one month from date of contract. The application of the United States rule is demonstrated below:

(A)		(B)		(C)		(D)		(E)
				Application of payment				
Unpaid balance of amount financed		Monthly rate		Credit service charge		Amount financed		Total monthly payment (C) + (D)
500.00	×	1%	=	5.00		123.14		128.14
376.86	×	1%	=	3.77		124.37		128.14
252.49	×	1%	=	2.52		125.62		128.14
126.87	×	1%	=	1.27		126.87		128.14
				12.56	+	500.00	=	512.56

Rate disclosure involves finding that rate which will generate the stated credit service charge when applied to the unpaid balances of the amount financed according to the United States rule. A monthly rate of 1% produces a credit service charge of $12.56, the difference between the sum of the monthly payments and the amount financed. The annual percentage rate would be twelve times the monthly rate, or 12%. In mathematical literature this is generally referred to as the nominal annual rate.

Note the application of the U. S. rule. In the first month the first $5 (1% × $500) of the monthly payment of $128.14 is applied to the credit service charge, leaving a balance of $123.14. This remainder is then applied to reduce the unpaid balance of the amount financed from $500 to $376.86. The same process is repeated in subsequent months.

[¶ 839] Sales Made by Telephone or Mail

Sec. 2.305. (1) With respect to a consumer credit sale, other than a sale made pursuant to a revolving charge account, if the seller receives a purchase order or offer by mail or telephone without personal solicitation, the seller complies with this Part if (a) he makes the disclosures at the time and in the manner provided in the general disclosure requirements and provisions (subsection (2) of Section 2.302), or (b) the seller's catalog or other printed material distributed to the public sets forth the cash price, the method of determining the deferred payment price, and the terms of financing, including the annual percentage rate, and before the first payment is due on the sale, he gives the information required by this Part including the notice prescribed in subsection (2).

(2) The notice shall be in writing and conspicuous and shall provide that if the buyer does not wish to make the purchase on credit, he may, within 15 days of receipt of the notice, prepay the obligation as to that purchase for an amount stated or identified in the notice and avoid the payment of any credit service charge as to that purchase. A prepayment under this Section is subject to the provisions of this Act on prepayment, except that no credit service charge shall be made if prepayment in full is made within the period specified in the notice. Payment by mail is effective when posted.

COMMENT

This section is derived in part from CCPA Section 128(c).

[¶ 840] Consumer Credit Sales Not Pursuant to Revolving Charge Account

Sec. 2.306. (1) This section applies to a consumer credit sale not made pursuant to a revolving charge account (Section 2.310).

(2) The seller shall give to the buyer the following information:

(a) brief description or identification of the goods, services, or interest in land;

(b) cash price of the goods, services, or interest in land, and any applicable sales, use, excise, transfer, or documentary stamp taxes not included in the cash price; if property and related services are sold as part of one transaction, the price of the property and services may be separately stated or combined;

(c) amount of the down payment and a statement of the portion paid in money and the portion paid by an allowance for property traded in; if there is a security interest in the property traded in which the seller agrees to discharge, the seller shall also state the amount which the seller agrees to pay to discharge the security interest and this amount may be deducted from the allowance for property traded in;

(d) difference between the amount of cash price (paragraph (b)) and the amount of down payment (paragraph (c));

(e) amount paid or payable for registration, certificate of title or license fees, if not included in the cash price, and a description or identification of the fees;

(f) amount of official fees and taxes if not included in the cash price and a description or identification of them;

(g) brief description of insurance to be provided or paid for by the seller including the type and amount of the coverages, and if a separate charge is made, the amount of the charge;

(h) amount of other additional charges (Section 2.202), and a brief description or identification of them;

(i) amount financed (sum of amounts stated in paragraphs (d), (e), (f), (g), and (h));

(j) except in the case of a sale of a dwelling when the credit service charge does not exceed 10 per cent per year (Section 2.104), the amount of the credit service charge and the amount of the unpaid balance (amount financed plus credit service charge);

(k) rate of the credit service charge as applied to the amount financed in accordance with the provisions on calculation of rate (Section 2.304), except in the case of a credit service charge which does not exceed $5 when the amount financed does not exceed $75 or $7.50 when the amount financed exceeds $75;

(l) number of payments, amount of each payment, due date of first payment, and the due date of subsequent payments or interval between payments;

(m) default, delinquency, or similar charges payable in the event of late payments; and

(n) description of any security interest held or to be retained or acquired by the seller in connection with the extension of credit, and a clear identification of the property to which the security interest relates.

COMMENT

This section is derived in part from CCPA Section 128.

[¶ 841] Refinancing

Sec. 2.307. If the seller refinances the balance owing with respect to a consumer credit sale, refinancing, or consolidation pursuant to the provisions on refinancing (Section 2.205), he shall state to the buyer the following:

(1) unpaid balance before refinancing;

(2) amount and brief itemization of rebates to which buyer would have been entitled if the debt had been prepaid pursuant to the provisions on rebate upon prepayment (Section 2.210) on the date of refinancing, except that for the purpose of computing this amount no minimum credit service charge (subsection (6) of Section 2.201) shall be allowed;

(3) amount and brief itemization of additional charges in connection with the refinancing and a brief indication of any change in the type or terms of insurance;

(4) amount financed resulting from the refinancing;

(5) amount of credit service charge;

(6) amount of unpaid balance;

(7) number of payments, amount of each payment, due date f first payment, and the due date of subsequent payments or interval between payments; and

(8) rate of the credit service charge as applied to the amount financed in accordance with the provisions on calculation of rate (Section 2.304), except in the case of a credit service charge which does not exceed $5 when the amount financed does not exceed $75 or $7.50 when the amount financed exceeds $75.

[¶ 842] Consolidation

Sec. 2.308. (1) Except as provided in subsection (2), if the parties agree to consolidate an existing unpaid balance from a previous consumer credit sale, refinancing, or consolidation, with the amount financed from a subsequent consumer credit sale, refinancing, or consolidation, the seller shall state:

(a) with respect to the refinanced unpaid balance, the information required by the provisions on refinancing (subsections (1) through (4) of Section 2.307);

(b) with respect to the subsequent sale, the information required by the provisions on consumer credit sales other than revolving charge accounts (paragraphs (a) through (j) of subsection (2) of Section 2.306);

(c) the aggregate amount financed, the amount of the credit service charge, the amount of the unpaid balance, the number of payments, the amount of each payment, the due date of the first payment, and the due dates of subsequent payments or the interval between payments; and

(d) the rate of the credit service charge as applied to the aggregate amount financed in accordance with the provisions on calculation of rate (Section 2.304), except in the case of a credit service charge which does not exceed $5 when the aggregate amount financed does not exceed $75 or $7.50 when the amount financed exceeds $75.

(2) If a consumer credit sale is made pursuant to an agreement providing for the addition of the unpaid balance resulting from a subsequent sale to an existing unpaid balance resulting from a previous sale, and the buyer has approved in writing both the annual percentage rate or rates and the method of computing the credit service charge or charges,

(a) the information required to be given with respect to the subsequent sale (Section 2.306) may be given on or before the due date of the first instalment under the consolidated schedule of payments; and

(b) with respect to the consolidation, the seller, on or before the due date of the first instalment under the consolidated schedule of payments, shall state to the buyer the amount of the consolidated unpaid balance, the number of payments, amount of each payment, the due date of the first payment, and the due dates of subsequent payments or the interval between payments.

COMMENT

Subsection (2) is derived from CCPA Section 128(d). The security problem raised in that section of the CCPA is covered in Section 2.409.

[¶ 843] **Deferral**

Sec. 2.309. If the seller makes a deferral pursuant to the provisions on deferral charges (Section 2.204), he shall state to the buyer, at the time of or promptly after the deferral:

(1) amount deferred;

(2) any appropriate additional charges (Section 2.202);

(3) aggregate amount deferred, which is the sum of the amount in (1) and any unpaid amount included in (2);

(4) time to which payment is deferred; and

(5) amount and annual percentage rate of the deferral charge and when it is payable.

[¶ 844] **Revolving Charge Accounts**

Sec. 2.310. (1) Before making a consumer credit sale pursuant to a revolving charge account, the seller shall give to the buyer the following information:

(a) conditions under which a credit service charge may be made, including the time period, if any, within which any credit extended may be repaid without incurring a credit service charge;

(b) method of determining the balance upon which a credit service charge will be computed;

(c) method of determining the amount of the credit service charge, including the periodic percentage or percentages used to calculate the credit service charge and the amount of any minimum credit service charge;

(d) corresponding nominal annual percentage rate (subsection (3) of Section 2.304); if more than one corresponding nominal annual percentage rate may be used, the amount of a balance to which each corresponding nominal annual percentage rate applies shall also be stated;

(e) if the seller elects he may also state either

(i) the average effective annual percentage rate of return received from revolving charge accounts for a representative period of time; or

(ii) if circumstances are such that the computation of a rate under subparagraph (i) would not be feasible or practical, or would be misleading or meaningless, a projected rate of return to be received from revolving charge accounts; the Administrator shall prescribe rules, consistent with commonly accepted standards for accounting or statistical procedures, to carry out the purposes of this paragraph (e);

(f) conditions under which additional charges may be made and the method by which they will be determined; and

(g) conditions under which the seller may retain or acquire a security interest in property to secure the balances resulting from sales made pursuant to the revolving charge account, and a description of the interest or interests which may be retained or acquired.

(2) If there is an outstanding balance owing at the end of the billing cycle or if a credit service charge is made with respect to the billing cycle, the seller shall give to the buyer the following information within a reasonable time after the end of the billing cycle:

(a) outstanding balance at the beginning of the billing cycle;

(b) cash price and date of each sale during the billing cycle and, unless previously furnished, a brief description or identification of the goods or services sold;

(c) amount credited to the account during the billing cycle;

(d) amount of credit service charge and additional charges debited during the billing cycle, with an itemization or explanation to show the total amount of credit service charge, if any, due to the application of one or more periodic percentages and the amount, if any, imposed as a minimum charge;

(e) the periodic percentage used to calculate the credit service charge; if more than one periodic percentage is used, each percentage and the amount of the balance to which each applies;

(f) the balance on which the credit service charge is computed and a statement of how the balance is determined; if the balance is determined without first deducting all amounts credited during the period, that fact and the amounts credited shall also be stated;

(g) if the credit service charge for the billing cycle exceeds 50¢ for a monthly or longer billing cycle, or the pro rata part of 50¢ for a billing cycle shorter than monthly, the credit service charge expressed as an annual percentage rate (paragraph (b) of subsection (2) of Section 2.304); if more than one periodic percentage is used to calculate the credit service charge, the seller may, in lieu of stating a single annual percentage rate, state more than one annual percentage rate and the amount of the balance to which each annual percentage rate applies;

(h) if the credit service charge for the billing cycle does not exceed 50¢ for a monthly or longer billing cycle, or the pro rata part of 50¢ for a billing cycle shorter than monthly, the corresponding nominal annual percentage rate (subsection (3) of Section 2.304);

(i) if the seller elects, the average effective annual percentage rate of return or the projected rate as prescribed in paragraph (e) of subsection (1);

(j) outstanding balance at the end of the billing cycle; and

(k) date by which or period within which payment must be made to avoid additional credit service charges.

COMMENT

1. This section is derived in part from CCPA Section 127.

2. If the balance on which the charge is calculated is $750 and the creditor's monthly percentages are 1½% on the first $500 and 1% on the remainder, he would state the corresponding nominal annual percentage rates as 18% on the first $500 and 12% on the remaining $250.

[¶ 845] Consumer Leases

Sec. 2.311. With respect to a consumer lease the lessor shall give to the lessee the following information:

(1) brief description or identification of the goods;

(2) amount of any payment required at the inception of the lease;

(3) amount paid or payable for official fees, registration, certificate of title, or license fees or taxes;

(4) amount of other charges not included in the periodic payments and a brief description of the charges;

(5) brief description of insurance to be provided or paid for by the lessor, including the types and amounts of the coverages;

(6) number of periodic payments, the amount of each payment, the due date of the first payment, the due dates of subsequent payments or interval between payments, and the total amount payable by the lessee;

(7) statement of the conditions under which the lessee may terminate the lease prior to the end of the term; and

(8) statement of the liabilities the lease imposes upon the lessee at the end of the term.

[¶ 846] Content of Periodic Statements

Sec. 2.312. The Administrator may by rule require a creditor who transmits periodic statements in connection with any consumer credit sale, not made pursuant to a revolving charge account, to set forth in each statement each of the following items:

(1) the annual percentage rate of the credit service charge with respect to each consumer credit sale to which the statement relates;

(2) the date by which or the period, if any, within which payment must be made in order to avoid further credit service charges or other charges; and

(3) the other items set forth in the provisions on disclosure with respect to revolving charge accounts (subsection (2) of Section 2.310) appropriate to the terms and conditions under which the consumer credit sale is made.

COMMENT

Since this section, derived from CCPA Section 126, may not be in the best interests of consumers, it becomes operative only upon a ruling by the Administrator.

[¶ 847] Advertising

Sec. 2.313. (1) No seller or lessor shall engage in this State in false or misleading advertising concerning the terms or conditions of credit with respect to a consumer credit sale or consumer lease.

(2) Without limiting the generality of subsection (1) and without requiring a statement of rate of credit service charge if the credit service charge is not more than $5 when the amount financed does not exceed $75 or more than $7.50 when the amount financed exceeds $75, an advertisement with respect to a consumer credit sale made by the posting of a public sign, or by catalog, magazine, newspaper, radio, television, or similar mass media, is misleading if

(a) it states the rate of credit service charge and the rate is not stated in the form required by the provisions on calculation of rate to be disclosed (Section 2.304), or

(b) it states the dollar amounts of the credit service charge or instalment payments, and does not also state the rate of any credit service charge and the number and amount of the instalment payments.

(3) In this section a catalog or other multiple-page advertisement is considered a single advertisement if it clearly and conspicuously displays a credit terms table setting forth the information required by this section.

(4) This section imposes no liability on the owner or personnel, as such, of any medium in which an advertisement appears or through which it is disseminated.

(5) Advertising which complies with the Federal Consumer Credit Protection Act does not violate subsection (2).

PART 4.—LIMITATIONS ON AGREEMENTS AND PRACTICES

[¶ 848] Scope

Sec. 2.401. This Part applies to consumer credit sales and consumer leases.

[¶ 849] Use of Multiple Agreements

Sec. 2.402. A seller may not use multiple agreements with intent to obtain a higher credit service charge than would otherwise be permitted by this Article or to avoid disclosure of an annual percentage rate pursuant to the provisions on disclosure and advertising (Part 3). The excess amount of credit service charge provided for in agreements in violation of this section is an excess charge for the purposes of the provisions on the effect of violations on rights of parties (Section 5.202) and the provisions on civil actions by Administrator (Section 6.113).

[¶ 850] Certain Negotiable Instruments Prohibited

Sec. 2.403. In a consumer credit sale or consumer lease, other than a sale or lease primarily for an agricultural purpose, the seller or lessor may not take a negotiable instrument other than a check as evidence of the obligation of the buyer or lessee. A holder is not in good faith if he takes a negotiable instrument with notice that it is issued in violation of this section. A holder in due course is not subject to the liabilities set forth in the provisions on the effect of violations on rights of parties (Section 5.202) and the provisions on civil actions by Administrator (Section 6.113)

COMMENT

Since the prohibition against negotiable notes in consumer financing will be well known in the financial community after enactment of this Act, professional financers buying consumer paper will normally not qualify as holders in due course with respect to notes taken by dealers in violation of this section and negotiated to them. However, it is possible that in rare cases second or third takers may not know of an instrument's consumer origin; in this unusual situation the policy favoring negotiability is upheld in order not to cast a cloud over negotiable instruments generally. A person who takes a negotiable note in violation of this section is subject to Sections 5.202 and 6.113.

[¶ 851] Assignee Subject to Defenses

Sec. 2.404. *Alternative A:* With respect to a consumer credit sale or consumer lease, other than a sale or lease primarily for an agricultural purpose, an assignee of the rights of the seller or lessor is subject to all claims and defenses of the buyer or lessee against the seller or lessor arising out of the sale or lease notwithstanding an agreement to the contrary, but the assignee's liability under this section may not exceed the amount owing to the assignee at the time the claim or defense is asserted against the assignee. Rights of the buyer or lessee under this section can only be asserted as a matter of defense to or set-off against a claim by the assignee.

[¶ 852] When Assignee Not Subject to Defenses

Sec. 2.404. *Alternative B:* (1) With respect to a consumer credit sale or consumer lease, other than a sale or lease primarily for an agricultural purpose, an agreement by the buyer or lessee not to assert against an assignee a claim or defense arising out of the sale or lease is enforceable only by an assignee not related to the seller or lessor who acquires the buyer's or lessee's contract in good faith and for value, who gives the buyer or lessee notice of the assignment as provided in this section and who, within 3 months after the mailing of the notice of assignment, receives no written notice of the facts giving rise to the buyer's or lessee's claim or defense. This agreement is enforceable only with respect to claims or defenses which have arisen before the end of the 3-month period after notice was mailed. The notice of assignment shall be in writing and addressed to the buyer or lessee at his address as stated in the contract, identify the contract, describe the goods or services, state the names of the seller or lessor and buyer or lessee, the name and address of the assignee, the amount payable by the buyer or lessee and the number, amounts and due dates of the instalments, and contain a conspicuous notice to the buyer or lessee that he has 3 months within which to notify the assignee in writing of any complaints, claims or defenses he may have against the seller or lessor and that if written notification of the complaints, claims or defenses is not received by the assignee within the 3-month period, the assignee will have the right to enforce the contract free of any claims or defenses the buyer or lessee may have against the seller or lessor which have arisen before the end of the 3-month period after notice was mailed.

(2) An assignee does not acquire a buyer's or lessee's contract in good faith within the meaning of subsection (1) if the assignee has knowledge or, from his course of dealing with the seller or lessor or his records, notice of substantial complaints by other buyers or lessees of the seller's or lessor's failure or refusal to perform his contracts with them and of the seller's or lessor's failure to remedy his defaults within a reasonable time after the assignee notifies him of the complaints.

(3) To the extent that under this section an assignee is subject to claims or defenses of the buyer or lessee against the seller or lessor, the assignee's liability under this section may not exceed the amount owing to the assignee at the time the claim or defense is asserted against the assignee and rights of the buyer or lessee under this section can only be asserted as a matter of defense to or set-off against a claim by the assignee.

[¶ 853] Balloon Payments

Sec. 2.405. With respect to a consumer credit sale, other than one primarily for an agricultural purpose or one pursuant to a revolving charge account, if any scheduled payment is more than twice as large as the average of earlier scheduled payments, the buyer has the right to refinance the amount of that payment at the time it is due without penalty. The terms of the refinancing shall be no less favorable to the buyer than the terms of the original sale. These provisions do not apply to the extent that the payment schedule is adjusted to the seasonal or irregular income of the buyer.

[¶ 854] Restriction on Liability in Consumer Lease

Sec. 2.406. The obligation of a lessee upon expiration of a consumer lease, other than one primarily for an agricultural purpose, may not exceed twice the average payment allocable to a monthly period under the lease. This

limitation does not apply to charges for damages to the leased property or for other default.

[¶ 855] Security in Sales or Leases

Sec. 2.407. (1) With respect to a consumer credit sale, a seller may take a security interest in the property sold. In addition, a seller may take a security interest in goods upon which services are performed or in which goods sold are installed or to which they are annexed, or in land to which the goods are affixed or which is maintained, repaired or improved as a result of the sale of the goods or services, if in the case of a security interest in land the debt secured is $1,000 or more, or, in the case of a security interest in goods the debt secured is $300 or more. The seller may also take a security interest in any property of the buyer to secure the debt arising from a consumer credit sale primarily for an agricultural purpose. Except as provided with respect to cross-collateral (Section 2.408), a seller may not otherwise take a security interest in property of the buyer to secure the debt arising from a consumer credit sale.

(2) With respect to a consumer lease other than a lease primarily for an agricultural purpose, a lessor may not take a security interest in property of the lessee to secure the debt arising from the lease.

(3) A security interest taken in violation of this section is void.

(4) The amounts of $1,000 and $300 in subsection (1) are subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

[¶ 856] Cross-Collateral

Sec. 2.408. (1) In addition to contracting for a security interest pursuant to the provisions on security in sales or leases (Section 2.407), a seller in a consumer credit sale may secure the debt arising from the sale by contracting for a security interest in other property if as a result of a prior sale the seller has an existing security interest in the other property. The seller may also contract for a security interest in the property sold in the subsequent sale as security for the previous debt.

(2) If the seller contracts for a security interest in other property pursuant to this section, the rate of credit service charge thereafter on the aggregate unpaid balances so secured may not exceed that permitted if the balances so secured were consolidated pursuant to the provisions on consolidation involving a refinancing (subsection (1) of Section 2.206). The seller has a reasonable time after so contracting to make any adjustments required by this section. "Seller" in this section does not include an assignee not related to the original seller.

[¶ 857] Debt Secured by Cross-Collateral

Sec. 2.409. (1) If debts arising from two or more consumer credit sales, other than sales primarily for an agricultural purpose or pursuant to a revolving charge account, are secured by cross-collateral (Section 2.408) or consolidated into one debt payable on a single schedule of payments, and the debt is secured by security interests taken with respect to one or more of the sales, payments received by the seller after the taking of the cross-collateral or the consolidation are deemed, for the purpose of determining the amount of the debt secured by the various security interests, to have been first applied to the

payment of the debts arising from the sales first made. To the extent debts are paid according to this section, security interests in items of property terminate as the debts originally incurred with respect to each item is paid.

(2) Payments received by the seller upon a revolving charge account are deemed, for the purpose of determining the amount of the debt secured by the various security interests, to have been applied first to the payment of credit service charges in the order of their entry to the account and then to the payment of debts in the order in which the entries to the account showing the debts were made.

(3) If the debts consolidated arose from two or more sales made on the same day, payments received by the seller are deemed, for the purpose of determining the amount of the debt secured by the various security interests, to have been applied first to the payment of the smallest debt.

COMMENT

Subsection (1) states the first-in-first-out rule for consolidations and subsection (2) applies the same principle to revolving charge accounts. Subsection (3) covers the case in which the buyer purchases a $750 TV in one department at 9:30 a. m. and a $150 typewriter in another department at 10:00 a. m. Subsequently the debts are consolidated. This subsection relieves the seller of having to keep records of the exact hour a sale is made. It is derived from Consumer Credit Protection Act Section 128(d).

[¶ 858] No Assignment of Earnings

Sec. 2.410. A seller or lessor may not take an assignment of earnings of the buyer or lessee for payment or as security for payment of a debt arising out of a consumer credit sale or a consumer lease. An assignment of earnings in violation of this section is unenforceable by the assignee of the earnings and revocable by the buyer or lessee. This section does not prohibit an employee from authorizing deductions from his earnings if the authorization is revocable.

[¶ 859] Referral Sales

Sec. 2.411. With respect to a consumer credit sale or consumer lease the seller or lessor may not give or offer to give a rebate or discount or otherwise pay or offer to pay value to the buyer or lessee as an inducement for a sale or lease in consideration of his giving to the seller or lessor the names of prospective purchasers or lessees, or otherwise aiding the seller or lessor in making a sale or lease to another person, if the earning of the rebate, discount or other value is contingent upon the occurrence of an event subsequent to the time the buyer or lessee agrees to buy or lease. If a buyer or lessee is induced by a violation of this section to enter into a consumer credit sale or consumer lease, the agreement is unenforceable by the seller or lessor and the buyer or lessee, at his option, may rescind the agreement or retain the goods delivered and the benefit of any services performed, without any obligation to pay for them.

[¶ 860] Notice of Assignment

Sec. 2.412. The buyer or lessee is authorized to pay the original seller or lessor until the buyer or lessee receives notification of assignment of the rights to payment pursuant to a consumer credit sale or consumer lease and that payment is to be made to the assignee. A notification which does not reasonably identify the rights assigned is ineffective. If requested by the buyer or

lessee, the assignee must seasonably furnish reasonable proof that the assignment has been made and unless he does so the buyer or lessee may pay the seller or lessor.

COMMENT

This section is derived from UCC Section 9-318(3).

[¶ 861] Attorney's Fees

Alternative A:

Sec. 2.413. With respect to a consumer sale or consumer lease the agreement may not provide for the payment by the buyer or lessee of attorney's fees. A provision in violation of this section is unenforceable.

[¶ 862] Attorney's Fees

Alternative B:

Sec. 2.413. With respect to a consumer credit sale or consumer lease the agreement may provide for the payment by the buyer or lessee of reasonable attorney's fees not in excess of 15 per cent of the unpaid debt after default and referral to an attorney not a salaried employee of the seller, or of the lessor or his assignee. A provision in violation of this section is unenforceable.

[¶ 863] Limitation on Default Charges

Sec. 2.414. Except for reasonable expenses incurred in realizing on a security interest, the agreement with respect to a consumer credit sale may not provide for any charges as a result of default by the buyer other than those authorized by this Act. A provision in violation of this section is unenforceable.

[¶ 864] Authorization to Confess Judgment Prohibited

Sec. 2.415. A buyer or lessee may not authorize any person to confess judgment on a claim arising out of a consumer credit sale or consumer lease. An authorization in violation of this section is void.

[¶ 865] Change in Terms of Revolving Charge Accounts

Sec. 2.416. (1) If a seller makes a change in the terms of a revolving charge account without complying with this section any additional cost or charge to the buyer resulting from the change is an excess charge and subject to the remedies available to debtors (Section 5.202) and to the Administrator (Section 6.113).

(2) A seller may change the terms of a revolving charge account whether or not the change is authorized by prior agreement. Except as provided in subsection (3), the seller shall give to the buyer written notice of any change at least three times, with the first notice at least six months before the effective date of the change.

(3) The notice specified in subsection (2) is not required if

(a) the buyer after receiving notice of the change agrees in writing to the change;

(b) the buyer elects to pay an amount designated on a billing statement (subsection (2) of Section 2.310) as including a new charge for a

benefit offered to the buyer when the benefit and charge constitute the charge in terms and when the billing statement also states the amount payable if the new charge is excluded;

(c) the change involves no significant cost to the buyer;

(d) the buyer has previously consented in writing to the kind of change made and notice of the change is given to the buyer in two billing cycles prior to the effective date of the change; or

(e) the change applies only to purchases made or obligations incurred after a date specified in a notice of the change given in two billing cycles prior to the effective date of the change.

(4) The notice provided for in this section is given to the buyer when mailed to him at the address used by the seller for sending periodic billing statements.

PART 5—HOME SOLICITATION SALES

[¶ 866] Definition: "Home Solicitation Sale"

Sec. 2.501. "Home solicitation sale" means a consumer credit sale of goods, other than farm equipment, or services in which the seller or a person acting for him engages in a personal solicitation of the sale at a residence of the buyer and the buyer's agreement or offer to purchase is there given to the seller or a person acting for him. It does not include a sale made pursuant to a preexisting revolving charge account, or a sale made pursuant to prior negotiations between the parties at a business establishment at a fixed location where goods or services are offered or exhibited for sale.

[¶ 867] Buyer's Right to Cancel

Sec. 2.502. (1) Except as provided in subsection (5), in addition to any right otherwise to revoke an offer, the buyer has the right to cancel a home solicitation sale until midnight of the third business day after the day on which the buyer signs an agreement or offer to purchase which complies with this Part.

(2) Cancellation occurs when the buyer gives written notice of cancellation to the seller at the address stated in the agreement or offer to purchase.

(3) Notice of cancellation, if given by mail, is given when it is deposited in a mailbox properly addressed and postage prepaid.

(4) Notice of cancellation given by the buyer need not take a particular form and is sufficient if it indicates by any form of written expression the intention of the buyer not to be bound by the home solicitation sale.

(5) The buyer may not cancel a home solicitation sale if the buyer requests the seller to provide goods or services without delay because of an emergency, and

(a) the seller in good faith makes a substantial beginning of performance of the contract before the buyer gives notice of cancellation, and

(b) in the case of goods, the goods cannot be returned to the seller in substantially as good condition as when received by the buyer.

(6) If a home solicitation sale is also subject to the provisions on debtors' right to rescind certain transactions (Section 5.204), the buyer may proceed either under those provisions or under this Part.

[¶ 868] Form of Agreement or Offer; Statement of Buyer's Rights

Sec. 2.503. (1) In a home solicitation sale, unless the buyer requests the seller to provide goods or services without delay in an emergency, the seller must present to the buyer and obtain his signature to a written agreement or offer to purchase which designates as the date of the transaction the date on which the buyer actually signs and contains a statement of the buyer's rights which complies with subsection (2).

(2) The statement must

(a) appear under the conspicuous caption: "BUYER'S RIGHT TO CANCEL", and

(b) read as follows: "If this agreement was solicited at your residence and you do not want the goods or services, you may cancel this agreement by mailing a notice to the seller. The notice must say that you do not want the goods or services and must be mailed before midnight on the third business day after you sign this agreement. The notice must be mailed to: ———————————————. If you cancel,
(insert name and mailing address of seller)
the seller may keep all or part of your cash down payment."

(3) Until the seller has complied with this section the buyer may cancel the home solicitation sale by notifying the seller in any manner and by any means of his intention to cancel.

[¶ 869] Restoration of Down Payment; Retention of Cancellation Fee

Sec. 2.504. (1) Except as provided in this section, within 10 days after a home solicitation sale has been cancelled or an offer to purchase revoked the seller must tender to the buyer any payments made by the buyer and any note or other evidence of indebtedness.

(2) If the down payment includes goods traded in, the goods must be tendered in substantially as good condition as when received by the seller. If the seller fails to tender the goods as provided by this section, the buyer may elect to recover an amount equal to the trade-in allowance stated in the agreement.

(3) The seller may retain as a cancellation fee 5 per cent of the cash price but not exceeding the amount of the cash down payment. If the seller fails to comply with an obligation imposed by this section, or if the buyer avoids the sale on any ground independent of his right to cancel provided by the provisions on the buyer's right to cancel (subsection (1) of Section 2.502) or revokes his offer to purchase, the seller is not entitled to retain a cancellation fee.

(4) Until the seller has complied with the obligations imposed by this section the buyer may retain possession of goods delivered to him by the seller and has a lien on the goods in his possession or control for any recovery to which he is entitled.

[¶ 870] Duty of Buyer; No Compensation for Services Prior to Cancellation

Sec. 2.505. (1) Except as provided by the provisions on retention of goods by the buyer (subsection (4) of Section 2.504), within a reasonable time after a home solicitation sale has been cancelled or an offer to purchase

revoked, the buyer upon demand must tender to the seller any goods delivered by the seller pursuant to the sale but he is not obligated to tender at any place other than his residence. If the seller fails to demand possession of goods within a reasonable time after cancellation or revocation, the goods become the property of the buyer without obligation to pay for them. For the purpose of this section, 40 days is presumed to be a reasonable time.

(2) The buyer has a duty to take reasonable care of the goods in his possession both before cancellation or revocation and for a reasonable time thereafter, during which time the goods are otherwise at the seller's risk.

(3) If the seller has performed any services pursuant to a home solicitation sale prior to its cancellation, the seller is entitled to no compensation except the cancellation fee provided in this Part.

PART 6—SALES OTHER THAN CONSUMER CREDIT SALES

[¶ 871] Sales Subject to Act by Agreement of Parties

Sec. 2.601. The parties to a sale other than a consumer credit sale may agree in a writing signed by the parties that the sale is subject to the provisions of this Act applying to consumer credit sales. If the parties so agree the sale is a consumer credit sale for the purposes of this Act.

[¶ 872] Definition: "Consumer Related Sale"; Rate of Credit Service Charge

Sec. 2.602. (1) A "consumer related sale" is a sale of goods, services, or an interest in land which is not subject to the provisions of this Act applying to consumer credit sales and in which the amount financed does not exceed $25,000 if

(a) the buyer is a person other than an organization; or

(b) the debt is secured primarily by a security interest in a one or two family dwelling occupied by a person related to the debtor.

(2) With respect to a consumer related sale not made pursuant to a revolving charge account, the parties may contract for the payment by the buyer of an amount comprising the amount financed and a credit service charge not in excess of 18 per cent per year calculated according to the United States rule on the unpaid balances of the amount financed.

(3) With respect to a consumer related sale made pursuant to a revolving charge account, the parties may contract for the payment of a credit service charge not in excess of that permitted by the provisions on credit service charge for revolving charge accounts (Section 2.207).

(4) The amount of $25,000 in subsection (1) is subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

COMMENT

This section imposes a rate ceiling on certain sales not subject to the rate ceilings for consumer credit sales. The principal cases covered are (1) credit sales by a seller not regularly engaged in similar credit transactions, (2) credit sales to persons for a business purpose, and (3) sales of one or two family dwellings to an organization where the dwelling is occupied by an individual related to the organization. The ceiling does not apply if the amount financed exceeds $25,000 or, except in the dwelling case, if the debtor is an organization.

[¶ 873] Applicability of Other Provisions to Consumer Related Sales

Sec. 2.603. Except for the rate of the credit service charge and the rights to prepay and to rebate upon prepayment, the provisions of Part 2 of this Article apply to a consumer related sale.

[¶ 874] Limitation on Default Charges in Consumer Related Sales

Sec. 2.604. (1) The agreement with respect to a consumer related sale may provide for only the following charges as a result of the buyer's default:

(a) reasonable attorney's fees and reasonable expenses incurred in realizing on a security interest;

(b) deferral charges not in excess of 18 per cent per year of the amount deferred for the period of deferral; and

(c) other charges that could have been made had the sale been a consumer credit sale.

(2) A provision in violation of this section is unenforceable.

[¶ 875] Credit Service Charge for Other Sales

Sec. 2.605. With respect to a sale other than a consumer credit sale or a consumer related sale, the parties may contract for the payment by the buyer of any credit service charge.

COMMENT

See Section 5.107—Extortionate Extensions of Credit.

Article 3—Loans

PART 1—GENERAL PROVISIONS

[¶ 876] Short Title

Sec. 3.101. This Article shall be known and may be cited as Uniform Consumer Credit Code—Loans.

[¶ 877] Scope

Sec. 3.102. This Article applies to consumer loans, including regulated and supervised loans; in addition Part 6 applies to consumer related loans.

[¶ 878] Definitions in Article

Sec. 3.103. The following definitions apply to this Act and appear in this Article as follows:

"Annual percentage rate"	Section 3.304(2)
"Business collateral"	Section 3.105
"Consumer loan"	Section 3.104
"Consumer related loan"	Section 3.602(1)
"Corresponding nominal annual percentage rate"	Section 3.304(3)
"Lender"	Section 3.107(1)
"Loan"	Section 3.106
"Loan finance charge"	Section 3.109
"Precomputed"	Section 3.107(2)
"Principal"	Section 3.107(3)
"Regulated lender"	Section 3.501(2)
"Regulated loan"	Section 3.501(1)
"Revolving loan account"	Section 3.108
"Supervised lender"	Section 3.501(4)
"Supervised loan"	Section 3.501(3)

[¶ 879] Definition: "Consumer Loan"

Sec. 3.104. (1) Except as provided in subsection (2), "consumer loan" is a loan made by a person regularly engaged in the business of making loans in which

(a) the debtor is a person other than an organization;

(b) the debt is incurred primarily for a personal, family, household, or agricultural purpose;

(c) either the debt is payable in instalments or a loan finance charge is made; and

(d) either the principal does not exceed $25,000 or the debt is secured by an interest in land.

(2) Unless the loan is made subject to this Act by agreement (Section 3.601), "consumer loan" does not include a loan which is secured primarily by

(a) business collateral, if at the time the loan is made the value of this collateral is substantial in relation to the amount of the loan, or,

(b) except as provided with respect to disclosure (Section 3.301) and debtors' remedies (Section 5.201), an interest in land, if at the time the loan is made the value of this collateral is substantial in relation to the amount of the loan, and the loan finance charge does not exceed 10 per cent per year calculated according to the United States rule on the unpaid balances of the principal on the assumption that the debt will be paid according to the agreed terms and will not be paid before the end of the agreed term.

(3) The amount of $25,000 in subsection (1) is subject to change pursuant to the provisions on adjustment of dollar amount (Section 1.106).

COMMENT

The purpose of subsection (2)(b) is to exclude the ordinary home mortgage from all provisions of this Act except the rate provisions; however, the Act is intended to include as a consumer loan the high rate loans which are characteristic of the second mortgage small loan business. Because the ordinary home mortgage invariably has a loan finance charge below 10 per cent, the exclusion has been based on the amount of the loan finance charge.

[¶ 880] Definition: "Business Collateral"

Sec. 3.105. "Business collateral" means an interest in land used primarily for other than a personal, family, household, or agricultural purpose, or accounts or contract rights other than earnings, business equipment, chattel paper, documents of title, instruments, inventory, or business general intangibles. Business equipment does not include farm equipment.

[¶ 881] Definition: "Loan"

Sec. 3.106. "Loan" includes

(1) the creation of debt by the lender's payment of or agreement to pay money to the debtor or to a third party for the account of the debtor;

(2) the creation of debt by a credit to an account with the lender upon which the debtor is entitled to draw immediately;

(3) the creation of debt pursuant to a lender credit card or similar arrangement; and

(4) the forbearance of debt arising from a loan.

[¶ 882] Definitions: "Lender"; "Precomputed"; "Principal"

Sec. 3.107. (1) Except as otherwise provided, "lender" includes an assignee of the lender's right to payment but use of the term does not in itself impose on an assignee any obligation of the lender with respect to events occurring before the assignment.

(2) A loan, refinancing, or consolidation is "precomputed" if the debt is expressed as a sum comprising the principal and the amount of the loan finance charge computed in advance.

(3) "Principal" of a loan means the total of

(a) the net amount paid to, receivable by, or paid or payable for the account of the debtor,

(b) the amount of any discount excluded from the loan finance charge (subsection (2) of Section 3.109), and,

(c) to the extent that payment is deferred,

(i) amounts actually paid or to be paid by the lender for registration, certificate of title, or license fees if not included in (a), and

(ii) additional charges permitted by this Article (Section 3.202).

[¶ 883] Definition: "Revolving Loan Account"

Sec. 3.108. "Revolving loan account" means an arrangement between a lender and a debtor pursuant to which (1) the lender may permit the debtor to obtain loans from time to time, (2) the unpaid balances of principal and the loan finance and other appropriate charges are debited to an account, (3) a loan finance charge if made is not precomputed but is computed on the outstanding unpaid balances of the debtor's account from time to time, and (4) the debtor has the privilege of paying the balances in instalments.

COMMENT

The usual use of the revolving loan account in consumer transactions is in connection with lender credit cards or check credit plans.

[¶ 884] Definition: "Loan Finance Charge"

Sec. 3.109. (1) "Loan finance charge" means the sum of (a) all charges payable directly or indirectly by the debtor and imposed directly or indirectly by the lender as an incident to the extension of credit, including any of the following types of charges which are applicable: interest or any amount payable under a point, discount, or other system of charges, however denominated, premium or other charge for any guarantee or insurance protecting the lender against the debtor's default or other credit loss; and (b) charges incurred for investigating the collateral or credit-worthiness of the debtor or for commissions or brokerage for obtaining the credit, irrespective of the person to whom the charges are paid or payable unless the lender had no notice of the charges when the loan was made. The term does not include charges as a result of default, additional charges (Section 3.202), delinquency charges (Section 3.203), or deferral charges (Section 3.204).

(2) If a lender makes a loan to a debtor by purchasing or satisfying obligations of the debtor pursuant to a lender credit card or similar arrangement, and the purchase or satisfaction is made at less than the face amount of the obligation, the discount is not part of the loan finance charge.

PART 2—MAXIMUM CHARGES

[¶ 885] Loan Finance Charge for Consumer Loans other than Supervised Loans

Sec. 3.201. (1) With respect to a consumer loan other than a supervised loan (Section 3.501), a lender may contract for and receive a loan finance charge, calculated according to the United States rule, not exceeding 18 per cent per year on the unpaid balances of the principal.

(2) This section does not limit or restrict the manner of contracting for the loan finance charge, whether by way of add-on, discount, or otherwise,

so long as the rate of the loan finance charge does not exceed that permitted by this section. If the loan is precomputed,

(a) the loan finance charge may be calculated on the assumption that all scheduled payments will be made when due, and

(b) the effect of prepayment is governed by the provisions on rebate upon prepayment (Section 3.210).

(3) For the purposes of this section, the term of a loan commences with the date the loan is made. Differences in the lengths of months are disregarded and a day may be counted as 1/30th of a month. Subject to classifications and differentiations the lender may reasonably establish, a part of a month in excess of 15 days may be treated as a full month if periods of 15 days or less are disregarded and if that procedure is not consistently used to obtain a greater yield than would otherwise be permitted.

(4) With respect to a consumer loan made pursuant to a revolving loan account

(a) the loan finance charge shall be deemed not to exceed 18 per cent per year if the loan finance charge contracted for and received does not exceed a charge in each monthly billing cycle which is 1½ per cent of an amount no greater than

(i) the average daily balance of the debt,

(ii) the unpaid balance of the debt on the same day of the billing cycle, or

(iii) the median amount within a specified range within which the average daily balance or the unpaid balance of the debt, on the same day of the billing cycle, is included; a charge may be made pursuant to this subparagraph only if the lender, subject to the classifications and differentiations he may reasonably establish, makes the same charge on all balances within a specified range and if the percentage when applied to the median amount within the range does not produce a charge exceeding the charge resulting from applying that percentage to the lowest amount within the range by more than 8 per cent of the charge on the median amount; for the purposes of this subparagraph and subparagraph (ii), a variation of not more than 4 days from month to month is "the same day of the billing cycle";

(b) if the billing cycle is not monthly, the loan finance charge shall be deemed not to exceed 18 per cent per year if the loan finance charge contracted for and received does not exceed a percentage which bears the same relation to 1½ per cent as the number of days in the billing cycle bears to 30; and

(c) notwithstanding subsection (1), if there is an unpaid balance on the date as of which the loan finance charge is applied, a charge not exceeding 50¢ may be made if the billing cycle is monthly or longer, or the pro rata part of 50¢ which bears the same relation to 50¢ as the number of days in the billing cycle bears to 30, if the billing cycle is shorter than monthly, but no charge may be made pursuant to this paragraph if the lender has made an annual charge for the same period as permitted by the provisions on additional charges (paragraph (c) of subsection (1) of Section 3.202) .

[¶ 886] Additional Charges

Sec. 3.202. (1) In addition to the loan finance charge permitted by this Part, a lender may contract for and receive the following additional charges in connection with a consumer loan:

(a) official fees and taxes;

(b) charges for insurance as described in subsection (2);

(c) annual charges, payable in advance, for the privilege of using a lender credit card or similar arrangement which entitles the user to purchase goods or services from at least 100 persons not related to the issuer of the lender credit card or similar arrangement, under an arrangement pursuant to which the debts resulting from the purchases are payable to the issuer; and

(d) charges for other benefits, including insurance, conferred on the debtor, if the benefits are of value to him apart from the granting of the credit, the charges are reasonable in relation to the benefits, and the Administrator has by rule determined that the charges are permissible additional charges.

(2) An additional charge may be made for insurance written in connection with the loan, other than insurance protecting the lender against the debtor's default or other credit loss,

(a) with respect to insurance against loss of or damage to property, or against liability, if the lender furnishes a clear and specific statement in writing to the debtor, setting forth the cost of the insurance if obtained from or through the lender, and stating that the debtor may choose the person through which the insurance is to be obtained; and,

(b) with respect to consumer credit insurance providing life, accident, or health coverage, if the insurance coverage is not a factor in the approval by the lender of the extension of credit, and this fact is clearly disclosed in writing to the debtor, and if in order to obtain the insurance in connection with the extension of credit, the debtor gives specific affirmative written indication of his desire to do so after written disclosure to him of the cost thereof.

(3) For the purposes of the Part on Disclosure and Advertising (Part 3), if the loan finance charge with respect to a loan primarily secured by an interest in land does not exceed 10 per cent per year (paragraph (b) of subsection (2) of Section 3.104), reasonable closing costs even though not within subsection (1) may be treated as additional charges.

COMMENT

See Comment to Section 2.202.

[¶ 887] Delinquency Charges

Sec. 3.203. (1) With respect to a precomputed consumer loan, refinancing, or consolidation, the parties may contract for a delinquency charge on any instalment not paid in full within 10 days after its scheduled due date in an amount not exceeding the greater of

(a) an amount, not exceeding $5, which is 5 per cent of the unpaid amount of the instalment, or

(b) the deferral charge (subsection (1) of Section 3.204) that would be permitted to defer the unpaid amount of the instalment for the period that it is delinquent.

(2) A delinquency charge under paragraph (a) of subsection (1) may be collected only once on an instalment however long it remains in default. No delinquency charge may be collected if the instalment has been deferred and a deferral charge (Section 3.204) has been paid or incurred. A delinquency charge may be collected at the time it accrues or at any time thereafter.

(3) No delinquency charge may be collected on an instalment which is paid in full within 10 days after its scheduled instalment due date even though an earlier maturing instalment or a delinquency charge on an earlier instalment may not have been paid in full. For purposes of this subsection payments are applied first to current instalments and then to delinquent instalments.

(4) If two instalments or parts thereof of a precomputed loan are in default for 10 days or more, the lender may elect to convert the loan from a precomputed loan to one in which the loan finance charge is based on unpaid balances. In this event he shall make a rebate pursuant to the provisions on rebate upon prepayment (Section 3.210) as of the maturity date of the first delinquent instalment, and thereafter may make a loan finance charge as authorized by the provisions on loan finance charge for consumer loans (Section 3.201) or the provisions on loan finance charge for supervised loans (Section 3.508), whichever is appropriate. The amount of the rebate shall not be reduced by the amount of any permitted minimum charge (Section 3.210). If the lender proceeds under this subsection, any delinquency or deferral charges made with respect to instalments due at or after the maturity date of the first delinquent instalment shall be rebated, and no further delinquency or deferral charges shall be made.

(5) The amount of $5 in subsection (1) is subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

COMMENT

See Comment to Section 2.203.

[¶ 886] Deferral Charges

Sec. 3.204. (1) With respect to a precomputed consumer loan, refinancing, or consolidation, the parties before or after default may agree in writing to a deferral of all or part of one or more unpaid instalments, and the lender may make and collect a charge not exceeding the rate previously stated to the debtor pursuant to the provisions on disclosure (Part 3) applied to the amount or amounts deferred for the period of deferral calculated without regard to difference in the lengths of months, but proportionally for a part of a month, counting each day as 1/30 of a month. A deferral charge may be collected at the time it is assessed or at any time thereafter.

(2) The lender may, in addition to the deferral charge, make appropriate additional charges (Section 3.202), and the amount of these charges which is not paid in cash may be added to the amount deferred for the purpose of calculating the deferral charge.

(3) The parties may agree in writing at the time of a precomputed consumer loan, refinancing, or consolidation that if an instalment is not paid within 10 days after its due date, the lender may unilaterally grant a deferral and

make charges as provided in this section. No deferral charge may be made for a period after the date that the lender elects to accelerate the maturity of the agreement.

(4) A delinquency charge made by the lender on an instalment may not be retained if a deferral charge is made pursuant to this section with respect to the period of delinquency.

[¶ 889] Loan Finance Charge on Refinancing

Sec. 3.205. With respect to a consumer loan, refinancing, or consolidation, the lender may by agreement with the debtor refinance the unpaid balance and may contract for and receive a loan finance charge based on the principal resulting from the refinancing at a rate not exceeding that permitted by the provisions on loan finance charge for consumer loans (Section 3.201) or the provisions on loan finance charge for supervised loans (Section 3.508), whichever is appropriate. For the purpose of determining the loan finance charge permitted, the principal resulting from the refinancing comprises the following:

(1) if the transaction was not precomputed, the total of the unpaid balance and the accrued charges on the date of the refinancing, or, if the transaction was precomputed, the amount which the debtor would have been required to pay upon prepayment pursuant to the provisions on rebate upon prepayment (Section 3.210) on the date of refinancing, except that for the purpose of computing this amount no minimum charge (Section 3.210) shall be allowed; and

(2) appropriate additional charges (Section 3.202), payment of which is deferred.

[¶ 890] Loan Finance Charge on Consolidation

Sec. 3.206. (1) If a debtor owes an unpaid balance to a lender with respect to a consumer loan, refinancing, or consolidation, and becomes obligated on another consumer loan, refinancing, or consolidation with the same lender, the parties may agree to a consolidation resulting in a single schedule of payments. If the previous consumer loan, refinancing, or consolidation was not precomputed, the parties may agree to add the unpaid amount of principal and accrued charges on the date of consolidation to the principal with respect to the subsequent loan. If the previous consumer loan, refinancing, or consolidation was precomputed, the parties may agree to refinance the unpaid balance pursuant to the provisions on refinancing (Section 3.205) and to consolidate the principal resulting from the refinancing by adding it to the principal with respect to the subsequent loan. In either case the lender may contract for and receive a loan finance charge based on the aggregate principal resulting from the consolidation at a rate not in excess of that permitted by the provisions on loan finance charge for consumer loans (Section 3.201) or the provisions on loan finance charge for supervised loans (Section 3.508), whichever is appropriate.

(2) The parties may agree to consolidate the unpaid balance of a consumer loan with the unpaid balance of a consumer credit sale. The parties may agree to refinance the previous unpaid balance pursuant to the provisions on refinancing sales (Section 2.205) or the provisions on refinancing loans (Section 3.205), whichever is appropriate, and to consolidate the amount

financed resulting from the refinancing or the principal resulting from the refinancing by adding it to the amount financed or principal with respect to the subsequent sale or loan. The aggregate amount resulting from the consolidation shall be deemed principal, and the creditor may contract for and receive a loan finance charge based on the principal at a rate not in excess of that permitted by the provisions on loan finance charge for consumer loans (Section 3.201) or the provisions on loan finance charge for supervised loans (Section 3.508), whichever is appropriate.

[¶ 891] Conversion to Revolving Loan Account

Sec. 3.207. The parties may agree to add to a revolving loan account the unpaid balance of a consumer loan, not made pursuant to a revolving loan account, or a refinancing, or consolidation thereof, or the unpaid balance of a consumer credit sale, refinancing or consolidation. For the purpose of this section

(1) the unpaid balance of a consumer loan, refinancing, or consolidation is an amount equal to the principal determined according to the provisions on refinancing (Section 3.205); and

(2) the unpaid balance of a consumer credit sale, refinancing, or consolidation is an amount equal to the amount financed determined according to the provisions on refinancing (Section 2.205).

[¶ 892] Advances to Perform Covenants of Debtor

Sec. 3.208. (1) If the agreement with respect to a consumer loan, refinancing, or consolidation contains covenants by the debtor to perform certain duties pertaining to insuring or preserving collateral and if the lender pursuant to the agreement pays for performance of the duties on behalf of the debtor he may add the amounts paid to the debt. Within a reasonable time after advancing any sums, he shall state to the debtor in writing the amount of the sums advanced, any charges with respect to this amount, and any revised payment schedule, and, if the duties of the debtor performed by the lender pertain to insurance, a brief description of the insurance paid for by the lender including the type and amount of coverages. No further information need be given.

(2) A loan finance charge may be made for sums advanced pursuant to subsection (1) at a rate not exceeding the rate stated to the debtor pursuant to the provisions on disclosure (Part 3) with respect to the loan, refinancing, or consolidation, except that with respect to a revolving loan account the amount of the advance may be added to the unpaid balance of the debt and the lender may make a loan finance charge not exceeding that permitted by the provisions on loan finance charge for consumer loans (Section 3.201) or for supervised loans (Section 3.508), whichever is appropriate.

[¶ 893] Right to Prepay

Sec. 3.209. Subject to the provisions on rebate upon prepayment (Section 3.210), the debtor may prepay in full the unpaid balance of a consumer loan, refinancing, or consolidation at any time without penalty.

[¶ 894] Rebate upon Prepayment

Sec. 3.210. (1) Except as provided in subsection (2), upon prepayment in full of the unpaid balance of a precomputed consumer loan, refinancing, or

consolidation, an amount not less than the unearned portion of the loan finance charge calculated according to this section shall be rebated to the debtor. If the rebate otherwise required is less than $1, no rebate need be made.

(2) Upon prepayment in full of a consumer loan, other than one pursuant to a revolving loan account, a refinancing or consolidation, whether or not precomputed, the lender may collect or retain a minimum charge within the limits stated in this subsection if the loan finance charge earned at the time of prepayment is less than any minimum charge contracted for. The minimum charge may not exceed the amount of loan finance charge contracted for, or $5 in a transaction which had a principal of $75 or less, or $7.50 in a transaction which had a principal of more than $75.

(3) Except as otherwise provided in this subsection with respect to a loan primarily secured by an interest in land, the unearned portion of the loan finance charge is a fraction of the loan finance charge of which the numerator is the sum of the periodic balances scheduled to follow the computational period in which prepayment occurs, and the denominator is the sum of all periodic balances under either the loan agreement or, if the balance owing resulted from a refinancing (Section 3.205) or a consolidation (Section 3.206), under the refinancing agreement or consolidation agreement. In the case of a loan primarily secured by an interest in land, reasonable sums actually paid or payable to persons not related to the lender for customary closing costs included in the loan finance charge are deducted from the loan finance charge before the calculation prescribed by this subsection is made.

COMMENT

Subsection (3), together with paragraph (a) of subsection (4), states the "Rule of 78" with respect to a loan, refinancing or consolidation payable in equal instalments at equal intervals from the date of the loan, refinancing or consolidation to the final scheduled payment date. In the case of such a loan, refinancing or consolidation, "computational period" may be read as "scheduled payment period", and the provisions relating to irregular payment schedules, viz., paragraphs (b), (c) and (d) of subsection (4) and subsection (5), in its entirety, may be disregarded.

(4) In this section

(a) "periodic balance" means the amount scheduled to be outstanding on the last day of a computational period before deducting the payment, if any, scheduled to be made on that day;

(b) "computational period" means one month if one-half or more of the intervals between scheduled payments under the agreement is one month or more, and otherwise means one week;

(c) the "interval" to the due date of the first scheduled instalment or the final scheduled payment date is measured from the date of a loan, refinancing, or consolidation, and includes either the first or last day of the interval;

(d) if the interval to the due date of the first scheduled instalment does not exceed one month by more than 15 days when the computational period is one month, or 11 days when the computational period is one week, the interval shall be considered as one computational period.

(5) This subsection applies only if the schedule of payments is not regular (subsection (6) of Section 3.304).

(a) If the computational period is one month and

(i) if the number of days in the interval to the due date of the first scheduled instalment is less than one month by more than 5 days, or more than one month by more than 5 but not more than 15 days, the unearned loan finance charge shall be increased by an adjustment for each day by which the interval is less than one month and, at the option of the lender, may be reduced by an adjustment for each day by which the interval is more than one month; the adjustment for each day shall be 1/30th of that part of the loan finance charge earned in the computational period prior to the due date of the first scheduled instalment assuming that period to be one month; and

(ii) if the interval to the final scheduled payment date is a number of computational periods plus an additional number of days less than a full month, the additional number of days shall be considered a computational period only if 16 days or more. This subparagraph applies whether or not subparagraph (i) applies.

(b) Notwithstanding paragraph (a), if the computational period is one month, the number of days in the interval to the due date of the first instalment exceeds one month by not more than 15 days, and the schedule of payments is otherwise regular, the lender may, at his option, exclude the extra days and the charge for the extra days in computing the unearned loan finance charge; but if he does so and a rebate is required before the due date of the first scheduled instalment, he shall compute the earned charge for each elapsed day as 1/30th of the amount the earned charge would have been if the first interval had been one month.

(c) If the computational period is one week and

(i) if the number of days in the interval to the due date of the first scheduled instalment is less than 5 days, or more than 9 days but not more than 11 days, the unearned loan finance charge shall be increased by an adjustment for each day by which the interval is less than 7 days and, at the option of the lender, may be reduced by an adjustment for each day by which the interval is more than 7 days; the adjustment for each day shall be 1/7th of that part of the loan finance charge earned in the computational period prior to the due date of the first scheduled instalment assuming that period to be one week; and

(ii) if the interval to the final scheduled payment date is a number of computational periods plus an additional number of days less than a full week, the additional number of days shall be considered a computational period only if 4 days or more. This subparagraph applies whether or not subparagraph (i) applies.

(6) If a deferral (Section 3.204) has been agreed to, the unearned portion of the loan finance charge shall be computed without regard to the deferral. The amount of deferral charge earned at the date of prepayment shall also be calculated. If the deferral charge earned is less than the deferral charge paid, the difference shall be added to the unearned portion of the loan finance charge. If any part of a deferral charge has been earned but has not been paid, that part shall be subtracted from the unearned portion of the loan finance charge, or shall be added to the unpaid balance.

(7) This section does not preclude the collection or retention by the lender of delinquency charges (Section 3.203).

(8) If the maturity is accelerated for any reason and judgment is obtained, the debtor is entitled to the same rebate as if the payment had been made on the date judgment is entered.

(9) Upon prepayment in full of a consumer loan by the proceeds of consumer credit insurance (Section 4.103), the debtor or his estate is entitled to the same rebate as though the debtor had prepaid the agreement on the date the proceeds of the insurance are paid to the lender, but no later than 10 business days after satisfactory proof of loss is furnished to the lender.

COMMENT

For examples of the application of this section, see Comment to Section 2.210.

PART 3—DISCLOSURE AND ADVERTISING

[¶ 895] Applicability; Information Required

Sec. 3.301. (1) For purposes of this Part, consumer loan includes a loan secured primarily by an interest in land without regard to the rate of the loan finance charge if the loan is otherwise a consumer loan (Section 3.104).

(2) The lender shall disclose to the debtor to whom credit is extended with respect to a consumer loan the information required by either

(a) this Part, or

(b) except with respect to a loan secured primarily by an interest in land, the Federal Consumer Credit Protection Act.

(3) For the purposes of paragraph (b) of subsection (2), information which would otherwise be required pursuant to the Federal Consumer Credit Protection Act is sufficient even though the transaction is one of a class of credit transactions exempted from that Act pursuant to a determination by the Board of Governors of the Federal Reserve System that the class of transactions is subject under the law of this State to requirements substantially similar to those imposed under that Act.

[¶ 896] General Disclosure Requirements and Provisions

Sec. 3.302. (1) The disclosures required by this Part

(a) shall be made clearly and conspicuously;

(b) shall be in writing, a copy of which shall be delivered to the debtor, but need not be contained in a single writing nor made in the order set forth in this Part;

(c) may use terminology different from that employed in this Part if it conveys substantially the same meaning;

(d) may be supplemented by additional information or explanations supplied by the lender;

(e) need be made only to the extent applicable and only as to those items for which the lender makes a separate charge to the debtor;

(f) shall be made on the assumption that all scheduled instalments are paid when due; and

(g) comply with this Part although rendered inaccurate by any act, occurrence, or agreement subsequent to the required disclosure.

(2) Except with respect to loans made by telephone or mail (Section 3.305), loans made pursuant to a binding commitment (subsection (3) of Section 3.306), and loans made pursuant to a lender credit card (Section 3.310),

(a) the disclosures required by this Part shall be made before credit is extended, but may be made in the loan, refinancing, or consolidation agreement, or other evidence of indebtedness to be signed by the debtor if set forth conspicuously therein, and need be made only to one debtor if there are more than one, and

(b) if an evidence of indebtedness is signed by the debtor, the lender shall give him a copy when the writing is signed.

(3) Except as provided with respect to rescission by a debtor (Section 5.204) and civil liability for violations of disclosure provisions (subsecton (4) of Section 5.203), written acknowledgment of receipt by a debtor to whom a statement is required to be given pursuant to this art

(a) in an action or proceeding by or against the original lender, creates a presumption that the statement was given, and

(b) in an action or proceeding by or against an assignee without knowledge to the contrary when he acquires the obligation, is conclusive proof of the delivery of the statement and, unless the violation is apparent on the face of the statement, of compliance with this Part.

[¶ 897] Overstatement

Sec. 3.303. The disclosure of an amount or percentage which is greater than the amount or percentage required to be disclosed under this Part does not in itself constitute a violation of this Part if the overstatement is not materially misleading and is not used to avoid meaningful disclosure.

[¶ 898] Calculation of Rate to Be Disclosed

Sec. 3.304. (1) Except as otherwise specifically provided, if a lender is required to give to a debtor a statement of the rate of the loan finance charge he shall state the rate in terms of an annual percentage rate as defined in subsection (2) or in terms of a corresponding nominal annual percentage rate as defined in subsection (3), whichever is appropriate.

(2) "Annual percentage rate"

(a) with respect to a consumer loan other than one made pursuant to a resolving loan account, is either

(i) that nominal annual percentage rate which, when applied to the unpaid balances of the principal calculated according to the United States rule, will yield a sum equal to the amount of the loan finance charge, or

(ii) that rate determined by any method prescribed by the Administrator as a method which materially simplifies computation while retaining reasonable accuracy as compared with the rate determined pursuant to subparagraph (i);

(b) with respect to a consumer loan made pursuant to a revolving loan account, is the quotient expressed as a percentage of the total loan finance charge for the period to which it relates divided by the amount upon which the loan finance charge for that period is based, multiplied by the number of these periods in a year; if the period is one day, the number of periods in a year is deemed to be 360.

(3) "Corresponding nominal annual percentage rate" is the percentage or percentages used to calculate the loan finance charge for one billing cycle or other period pursuant to a revolving loan account multiplied by the number of billing cycles or periods in a year; if the period is one day, the number of periods in a year is deemed to be 360.

(4) If a lender is permitted to make the same loan finance charge for all principal amounts within a specified range (subsection (4) of Section 3.201) or for all balances within a specified range (subsection (5) of Section 3.508), he shall state the annual percentage rate or corresponding nominal annual percentage rate, whichever is appropriate, as applied to the median amount of the range within which the actual principal amount or balance is included.

(5) If a debt is payable on a schedule of instalment payments which is regular except for one or more of the following irregularities:

(a) the amount of one instalment payment is not substantially equal to the amount of each of the other instalment payments;

(b) the interval between the date the credit is granted and the first instalment payment is not equal to the interval between instalment payments; or

(c) in one or more payment periods no instalment payment is due, not exceeding one-fourth of the payment periods in any year if the length of the term of the agreement is a year or more, or one-fourth of the payment periods if the length of the term of the agreement is less than a year,

the lender may, at his option, calculate the rate to be disclosed as if the debt were payable under an agreement having the same principal, the same length of term to the nearest scheduled payment period, and a regular schedule of payments having the same interval between payments as the interval between the majority of instalments as scheduled in the loan agreement.

(6) A schedule of payments is regular if (a) the instalment payments are substantially equal in amount, (b) the interval between instalment payments is one month, or the intervals between instalment payments are equal and less than one month, and (c) the interval between the date the credit is granted and the first instalment payment is equal to the interval between instalment payments.

(7) A statement of rate complies with this Part if it does not vary from the accurately computed rate by more than the following tolerances:

(a) the annual percenage rate may be rounded to the nearest quarter of 1 per cent for consumer loans payable in substantially equal instalments when a lender determines the total loan finance charge on the basis of a single add-on, discount, periodic, or other rate, and the rate is converted into an annual percentage rate under procedures prescribed by the Administrator;

(b) the Administrator may authorize the use of rate tables or charts which may provide for the disclosure of annual percentage rates which vary from the rate determined in accordance with paragraph (a) by not more than the tolerances the Administrator may allow; the Administrator may not allow a tolerance greater than 8 per cent of that rate except to simplify compliance where irregular payments are involved; and

(c) in case a lender determines the annual percentage rate in a manner other than as described in paragraph (a) or (b), the Administrator may authorize other reasonable tolerances.

COMMENT

See Comment to Section 2.304.

[¶ 899] Loans Made by Telephone or Mail

Sec. 3.305. With respect to a consumer loan, other than a loan made pursuant to a revolving loan account, if the lender receives a request for an extension of credit by mail or telephone without personal solicitation, the lender complies with this Part if the lender's printed material distributed to the public or the loan agreement or other printed material delivered to the debtor sets forth the terms of financing, including the annual percentage rate for representative amounts of credit, and if he gives the information required by this Part on or before the date the first payment is due on the loan.

[¶ 900] Consumer Loans Not Pursuant to Revolving Loan Account

Sec. 3.306. (1) This section applies to a consumer loan not made pursuant to a revolving loan account (Section 3.309).

(2) The lender shall give to the debtor the following information:

(a) net amount paid to, receivable by, or paid or payable for the account of the debtor or in the case of a loan resulting from a refinancing, the amount prescribed by the provisions on loan finance charge on refinancing (subsection (1) of Section 3.205); if any amount is paid or payable to a third person, a brief itemization, which may be contained in a separate writing or writings, shall also be given;

(b) amount paid or payable for registration, certificate of title or license fees, if not included in (a), and a description or identification of the fees;

(c) amount of official fees and taxes and a description or identification of them;

(d) brief description of insurance to be provided or paid for by the lender including the type and the amount of the coverages, and if a separate charge is made, the amount of the charge;

(e) amount of other additional charges (Section 3.202), and a brief description or identification of them;

(f) amount of principal (sum of amounts stated in paragraphs (a), (b), (c), (d), and (e));

(g) except in the case of a loan secured by a first lien on a dwelling, made to finance the purchase of that dwelling, and in which the loan finance charge does not exceed 10 per cent per year (Section 3.104), the

amount of the loan finance charge and the amount of the unpaid balance (principal plus loan finance charge);

(h) rate of the loan finance charge as applied to the principal in accordance with the provisions on calculation of rate (Section 3.304), except in the case of a loan finance charge which does not exceed $5 when the principal does not exceed $75 or $7.50 when the principal exceeds $75;

(i) number of payments, amount of each payment, due date of first payment, and the due date of subsequent payments or interval between payments;

(j) default, delinquency, or similar charges payable in the event of late payments; and

(k) description of any security interest held or to be retained or acquired by the lender in connection with the extension of credit, and a clear identification of the property to which the security interest relates.

(3) If a lender makes a binding commitment to make a consumer loan by allowing the debtor to draw on the lender and at the time the commitment is made the amount of the loan has not been determined, the lender shall then give to the debtor a statement of the terms under which the loan will be made, including the rate of the loan finance charge calculated in accordance with the provisions on calculation of rate (Section 3.304). If the rate of the loan finance charge varies according to the amount of the loan, the lender shall state the minimum and maximum annual percentage rates which would be applicable to the amounts which could be drawn pursuant to the commitment. If additional charges (Section 3.202) may be made, the lender shall also state the conditions under which the charges may be made, the amount or method of computing the charges, and a brief description or identification of the charges. Within a reasonable time after the loan is made, and in any event on or before the due date of the first instalment, the lender shall give the information required by this section.

[¶ 901] Consolidation

Sec. 3.307. If the parties to a consumer loan or consumer credit sale agree to a consolidation (Section 3.206), the creditor shall give to the debtor the information required with respect to consumer loans not pursuant to a revolving loan account (Section 3.306). To comply with those provisions (paragraph (a) of subsection (2) of Section 3.306), the amount with respect to the previous loan or sale to be consolidated shall be separately stated and shall be added to the net amount paid to, receivable by, or paid or payable for the account of the debtor in connection with the subsequent loan or sale.

[¶ 902] Deferral

Sec. 3.308. If the lender makes a deferral pursuant to the provisions on deferral charges (Section 3.204), he shall state to the debtor, at the time of or promptly after the deferral:

(1) amount deferred;

(2) any appropriate additional charges (Section 3.202);

(3) aggregate amount deferred, which is the sum of the amount in (1) and any unpaid amount included in (2);

(4) time to which payment is deferred; and

(5) amount and annual percentage rate of the deferral charge and when it is payable.

[¶ 903] Revolving Loan Acounts

Sec. 3.309. (1) Before making a consumer loan pursuant to a revolving loan account, the lender shall give to the debtor the following information:

(a) conditions under which a loan finance charge may be made, including the time period, if any, within which any credit extended may be repaid without incurring a loan finance charge;

(b) method of determining the balance upon which a loan finance charge will be computed;

(c) method of determining the amount of the loan finance charge, including the periodic percentage or percentages used to calculate the loan finance charge and the amount of any minimum loan finance charge;

(d) corresponding nominal annual percentage rate (subsection (3) of Section 3.304); if more than one corresponding nominal annual percentage rate may be used, the amount of a balance to which each corresponding nominal annual percentage rate applies shall also be stated;

(e) if the lender elects he may also state either

(i) the average effective annual percentage rate of return received from revolving loan accounts for a representative period of time; or

(ii) if circumstances are such that the computation of a rate under subparagraph (i) would not be feasible or practical, or would be misleading or meaningless, a projected rate of return to be received from revolving loan accounts; the Administrator shall prescribe rules, consistent with commonly accepted standards for accounting or statistical procedures, to carry out the purposes of this paragraph (e);

(f) conditions under which additional charges may be made and the method by which they will be determined; and

(g) conditions under which the lender may retain or acquire a security interest in property to secure the balances resulting from loans made pursuant to the revolving loan account, and a description of the interest or interests which may be retained or acquired.

(2) If there is an outstanding balance owing at the end of the billing cycle or if a loan finance charge is made with respect to the billing cycle, the lender shall give to the debtor the following information within a reasonable time after the end of the billing cycle:

(a) outstanding balance at the beginning of the billing cycle;

(b) brief description or identification of loans made during the billing cycle in a statement or in accompanying cancelled checks, memoranda or the like;

(c) amount credited to the account during the billing cycle;

(d) amount of loan finance charge and additional charges debited during the billing cycle, with an itemization or explanation to show the total amount of loan finance charge, if any, due to the application of one or more periodic percentages and the amount, if any, imposed as a minimum charge;

(e) the periodic percentage used to calculate the loan finance charge; if more than one periodic percentage is used, each percentage and the amount of the balance to which each applies;

(f) the balance on which the loan finance charge is computed and a statement of how the balance is determined; if the balance is determined without first deducting all amounts credited during the period, that fact and the amounts credited shall also be stated;

(g) if the loan finance charge for the billing cycle exceeds 50¢ for a monthly or longer billing cycle, or the pro rata part of 50¢ for a billing cycle shorter than monthly, the loan finance charge expressed as an annual percentage rate (paragraph (b) of subsection (2) of Section 3.304); if more than one periodic percentage is used to calculate the loan finance charge, the lender may, in lieu of stating a single annual percentage rate, state more than one annual percentage rate and the amount of the balance to which each annual percentage rate applies;

(h) if the loan finance charge for the billing cycle does not exceed 50¢ for a monthly or longer billing cycle, or the pro rata part of 50¢ for a billing cycle shorter than monthly, the corresponding nominal annual percentage rate (subsection (3) of Section 3.304);

(i) if the lender elects, the average effective annual percentage rate of return or the projected rate as prescribed in paragraph (e) of subsection (1);

(j) outstanding balance at the end of the billing cycle; and

(k) date by which or period within which payment must be made to avoid additional loan finance charges.

COMMENT

See Comment to Section 2.310.

[¶ 904] Loan Pursuant to Lender Credit Card or Similar Arrangement

Sec. 3.310. Before a consumer loan, other than one made pursuant to a revolving loan account, is first made pursuant to a lender credit card or similar arrangement, the lender shall give to the debtor a statement of the annual percentage rate or rates at which loans will be made to the debtor and a brief description or identification of the additional charges that may be made. The lender shall give to the debtor the information required by this Part with respect to consumer loans other than revolving loan accounts (Section 3.306) within a reasonable time after a loan is made and in any event before the due date of the first instalment.

[¶ 905] Content of Periodic Statements

Sec. 3.311. The Administrator may by rule require a creditor who transmits periodic statements in connection with any consumer loan not made pursuant to a revolving loan account to set forth in each statement each of the following items:

(1) the annual percentage rate of the loan finance charge with respect to each consumer loan to which the statement relates;

(2) the date by which or the period, if any, within which payment must be made in order to avoid further loan finance charges or other charges; and

(3) the other items set forth in the provisions on disclosure with respect to revolving loan accounts (subsection (2) of Section 3.309) appropriate to the terms and conditions under which the consumer loan is made.

COMMENT

See Comment to Section 2.312.

[¶ 906] Advertising

Sec. 3.312. (1) No lender shall engage in this State in false or misleading advertising concerning the terms or conditions of credit with respect to a consumer loan.

(2) Without limiting the generality of subsection (1), and without requiring a statement of rate of loan finance charge if the loan finance charge is not more than $5 when the principal does not exceed $75 or more than $7.50 when the principal exceeds $75, and advertisement with respect to a consumer credit loan made by the posting of a public sign, or by catalog, magazine, newspaper, radio, television, or similar mass media, is misleading if

(a) it states the rate of the loan finance charge and the rate is not stated in the form required by the provisions on calculation of rate (Section 3.304) or

(b) it states the dollar amounts of the loan finance charge or instalment payments, and does not also state the rate of any loan finance charge and the number and amount of the instalment payments.

(3) In this section a catalog or other multiple-page advertisement is considered a single advertisement if it clearly and conspicuously displays a credit terms table setting forth the information required by this section.

(4) This section imposes no liability on the owner or personnel, as such, of any medium in which an advertisement appears or through which it is disseminated.

(5) Advertising which complies with the Federal Consumer Credit Protection Act does not violate subsection (2).

PART 4.—LIMITATIONS ON AGREEMENTS AND PRACTICES

[¶ 907] Scope

Sec. 3.401. This Part applies to consumer loans.

[¶ 908] Balloon Payments

Sec. 3.402. With respect to a consumer loan, other than one primarily for an agricultural purpose or one pursuant to a revolving loan account, if any scheduled payment is more than twice as large as the average of earlier scheduled payments, the debtor has the right to refinance the amount of that payment at the time it is due without penalty. The terms of the refinancing shall be no less favorable to the debtor than the terms of the original loan. These provisions do not apply to the extent that the payment schedule is adjusted to the seasonal or irregular income of the debtor.

[¶ 909] No Assignment of Earnings

Sec. 3.403. (1) A lender may not take an assignment of earnings of the debtor for payment or as security for payment of a debt arising out of a consumer loan. An assignment of earnings in violation of this section is unenforceable by the assignee of the earnings and revocable by the debtor. This section does not prohibit an employee from authorizing deductions from his earnings if the authorization is revocable.

(2) A sale of unpaid earnings made in consideration of the payment of money to or for the account of the seller of the earnings is deemed to be a loan to him secured by an assignment of earnings.

[¶ 910] Attorney's Fees

Alternative A:

Sec. 3.404. With respect to a consumer loan the agreement may not provide for the payment by the debtor of attorney's fees. A provision in violation of this section is unenforceable.

[¶ 911] Attorney's Fees

Alternative B:

Sec. 3.404. Except as provided by the limitations on attorney's fees in certain supervised loans (Section 3.511), with respect to a consumer loan the agreement may provide for the payment by the debtor of reasonable attorney's fees not in excess of 15 per cent of the unpaid debt after default and referral to an attorney not a salaried employee of the lender. A provision in violation of this section is unenforceable.

[¶ 912] Limitation on Default Charges

Sec. 3.405. Except for reasonable expenses incurred in realizing on a security interest, the agreement with respect to a consumer loan may not provide for charges as a result of default by the debtor other than those authorized by this Act. A provision in violation of this section is unenforceable.

[¶ 913] Notice of Assignment

Sec. 3.406. The debtor is authorized to pay the original lender until he receives notification of assignment of rights to payment pursuant to a consumer loan and that payment is to be made to the assignee. A notification which does not reasonably identify the rights assigned is ineffective. If requested by the debtor, the assignee must seasonably furnish reasonable proof that the assignment has been made and unless he does so the debtor may pay the original lender.

COMMENT

This section is derived from UCC Section 9-318(3).

[¶ 914] Authorization to Confess Judgment Prohibited

Sec. 3.407. A debtor may not authorize any person to confess judgment on a claim arising out of a consumer loan. An authorization in violation of this section is void.

[¶ 915] Change in Terms of Revolving Loan Accounts

Sec. 3.408. (1) If a lender makes a change in the terms of a revolving loan account without complying with this section any additional cost or charge to the debtor resulting from the change is an excess charge and subject to the remedies available to debtors (Section 5.202) and to the Administrator (Section 6.113).

(2) A lender may change the terms of a revolving loan account whether or not the change is authorized by prior agreement. Except as provided in subsection (3), the lender shall give to the debtor written notice of any change at least three times, with the first notice at least six months before the effective date of the change.

(3) The notice specified in subsection (2) is not required if

(a) the debtor after receiving notice of the change agrees in writing to the change;

(b) the debtor elects to pay an amount designated on a billing statement (subsection (2) of Section 3.309) as including a new charge for a benefit offered to the debtor when the benefit and charge constitute the change in terms and when the billing statement also states the amount payable if the new charge is excluded;

(c) the change involves no significant cost to the debtor;

(d) the debtor has previously consented in writing to the kind of change made and notice of the change is given to the debtor in two billing cycles prior to the effective date of the change; or

(e) the change applies only to debts incurred after a date specified in a notice of the change given in two billing cycles prior to the effective date of the change.

(4) The notice provided for in this section is given to the debtor when mailed to him at the address used by the lender for sending periodic billing statements.

PART 5.—REGULATED AND SUPERVISED LOANS

[¶ 916] Definitions: "Regulated Loan"; "Regulated Lender"; "Supervised Loan"; "Supervised Lender"

Sec. 3.501. (1) "Regulated loan" means a consumer loan, including a loan made pursuant to a revolving loan account, in which the rate of the loan finance charge is in excess of 10 per cent per year calculated on the unpaid balances of the principal according to the United States rule.

(2) "Regulated lender" means a person engaged in the business of making regulated loans.

(3) "Supervised loan" means a regulated loan in which the rate of the loan finance charge exceeds 18 per cent per year as determined according to the provisions on loan finance charge for consumer loans (Section 3.201).

(4) "Supervised lender" means a person authorized to make or take assignments of supervised loans.

[¶ 917] Authority to Make Supervised Loans

Sec. 3.502. Unless a person is a supervised financial organization or has first obtained a license from the Administrator authorizing him to make supervised loans, he shall not engage in the business of

(1) making supervised loans, or

(2) taking assignments of and undertaking direct collection of payments from or enforcement of rights against debtors arising from supervised loans,

but he may collect and enforce for three months without a license if he promptly applies for a license and his application has not been denied.

COMMENT

Unlike some statutes, this section contemplates that a supervised lender needs to obtain only one license to operate one or more offices in a State. While the single license permits the supervised lender to locate offices wherever he deems them to be economically justified, he must annually notify the Administrator of the location of each office (Section 6.202). Although license fees have been viewed as a source of income for the regulatory agency, licensing of supervised lenders is not to be regarded as a source of income. Instead, income for the operations of the Administrator is to be derived from general appropriations. Annual fees are required of all persons required to file notification (Section 6.203).

Moreover, this Section does not contemplate the annual renewal of licenses; such a requirement would merely increase the administrative burdens of the Administrator and the licensee.

In this Section "person" implies no limitation on the residence of the applicant. He need not be a resident of the State in which he seeks to be licensed as a supervised lender. Even though he is not physically within the State, the licensee is bound by the laws of the State in which he makes supervised loans.

If an unlicensed assignee not in the business of making collections or enforcing rights under the paper assigned to him finds that he must undertake collection or enforcement, subsection (2) gives him a 3-month grace period during which he can operate before he obtains a license.

[¶ 918] License to Make Supervised Loans

Sec. 3.503. (1) The Administrator shall receive and act on all applications for licenses to make supervised loans under this Act. Applications shall be filed in the manner prescribed by the Administrator and shall contain such information as the Administrator may require to make an evaluation of the financial responsibility, character and fitness of the applicant.

(2) No license shall be issued unless the Administrator, upon investigation, finds that the financial responsibility, character and fitness of the applicant, and of the members thereof (if the applicant is a co-partnership or association) and of the officers and directors thereof (if the applicant is a corporation), are such as to warrant belief that the business will be operated honestly and fairly within the purposes of this Act.

(3) Upon written request, the applicant is entitled to a hearing on the question of his qualifications for a license if (a) the Administrator has notified the applicant in writing that his application has been denied, or (b) the Administrator has not issued a license within 60 days after the application for the license was filed. A request for a hearing may not be made more than 15 days after the Administrator has mailed a writing to the applicant notifying him that the application has been denied and stating in substance the Administrator's findings supporting denial of the application.

COMMENT

This section is intimately related to disclosure (Part 3 of Article 2 and Part 3 of Article 3) and to maximum charges (Part 2 of Article 2 and Part 2 of Article 3). The purpose is to facilitate entry into the cash loan field so that the resultant rate competition fostered by disclosure will generally force rates below the permitted maximum charges. Competition is further encouraged by the absence of any licensing requirements in credit sales (Article 2).

A secondary purpose is to reduce the likelihood of establishing localized monopolies in the granting of cash credit. Such monopolies tend to push rates charged to the maximum permitted levels and to establish conditions under which some share of the anticipated monopoly profits are devoted to direct or indirect pressures to obtain the license.

Since this section does not apply to supervised financial organizations, the safety of depositors' funds is not directly endangered by the competition fostered by the freedom of entry. To the extent, if any, that the increased competition causes the development of undesirable credit practices, these are directly controlled by powers to revoke or suspend a license (Section 3.504), prohibition on multiple agreements (Section 3.509), restrictions on real property security (Section 3.510), and by the provisions on remedies and penalties provided (Article 5) and the powers and functions of the Administrator (Article 6).

[¶ 919] Revocation or Suspension of License

Sec. 3.504. (1) The Administrator may issue to a person licensed to make supervised loans an order to show cause why his license should not be revoked or suspended for a period not in excess of 6 months. The order shall state the place for a hearing and set a time for the hearing that is no less than 10 days from the date of the order. After the hearing the Administrator shall revoke or suspend the license if he finds that:

(a) the licensee has repeatedly and willfully violated this Act or any rule or order lawfully made pursuant to this Act; or

(b) facts or conditions exist which would clearly have justified the Administrator in refusing to grant a license had these facts or conditions been known to exist at the time the application for the license was made.

(2) No revocation or suspension of a license is lawful unless prior to institution of proceedings by the Administrator notice is given to the licensee of the facts or conduct which warrant the intended action, and the licensee is given an opportunity to show compliance with all lawful requirements for retention of the license.

(3) If the Administrator finds that probable cause for revocation of a license exists and that enforcement of this Act requires immediate suspension of the license pending investigation, he may, after a hearing upon 5 days' written notice, enter an order suspending the license for not more than 30 days.

(4) Whenever the Administrator revokes or suspends a license, he shall enter an order to that effect and forthwith notify the licensee of the revocation or suspension. Within five days after the entry of the order he shall deliver to the licensee a copy of the order and the findings supporting the order.

(5) Any person holding a license to make supervised loans may relinquish the license by notifying the Administrator in writing of its relinquishment, but this relinquishment shall not affect his liability for acts previously committed.

(6) No revocation, suspension, or relinquishment of a license shall impair or affect the obligation of any preexisting lawful contract between the licensee and any debtor.

(7) The Administrator may reinstate a license, terminate a suspension, or grant a new license to a person whose license has been revoked or suspended if no fact or condition then exists which clearly would have justified the Administrator in refusing to grant a license.

[¶ 920] Records; Annual Reports

Sec. 3.505. (1) Every licensee shall maintain records in conformity with generally accepted accounting principles and practices in a manner that will enable the Administrator to determine whether the licensee is complying with the provisions of this Act. The record keeping system of a licensee shall be sufficient if he makes the required information reasonably available. The records need not be kept in the place of business where supervised loans are made, if the Administrator is given free access to the records wherever located. The records pertaining to any loan need not be preserved for more than two years after making the final entry relating to the loan, but in the case of a revolving loan account the two years is measured from the date of each entry.

(2) On or before April 15 each year every licensee shall file with the Administrator a composite annual report in the form prescribed by the Administrator relating to all supervised loans made by him. The Administrator shall consult with comparable officials in other states for the purpose of making the kinds of information required in annual reports uniform among the states. Information contained in annual reports shall be confidential and may be published only in composite form.

[¶ 921] Examinations and Investigations

Sec. 3.506. (1) The Administrator shall periodically examine at such intervals as he deems appropriate the loans, business, and records of every licensee. In addition, for the purpose of discovering violations of this Act or securing information lawfully required, the Administrator or the official or agency to whose supervision the organization is subject (Section 6.105) may at any time investigate the loans, business, and records of any regulated lender. For these purposes he shall have free and reasonable access to the offices, places of business, and records of the lender.

(2) If the lender's records are located outside this State, the lender shall, at his option, either make them available to the Administrator at a convenient location within this State, or pay the reasonable and necessary expenses for the Administrator or his representative to examine them at the place where they are maintained. The Administrator may designate representatives, including comparable officials of the State in which the records are located, to inspect them on his behalf.

(3) For the purposes of this section, the Administrator may administer oaths or affirmations, and upon his own motion or upon request of any party may subpoena witnesses, compel their attendance, adduce evidence, and require the production of any matter which is relevant to the investigation, including the existence, description, nature, custody, condition, and location of any books, documents, or other tangible things and the identity and location of persons having knowledge of relevant facts, or any other matter reasonably calculated to lead to the discovery of admissible evidence.

(4) Upon failure without lawful excuse to obey a subpoena or to give testimony and upon reasonable notice to all persons affected thereby, the Administrator may apply to [ ] court for an order compelling compliance.

[¶ 922] Application of [Administrative Procedure Act] [Part on Administrative Procedure and Judicial Review] to Part

Sec. 3.507. Except as otherwise provided, the [State administrative procedure act] [Part on Administrative Procedure and Judicial Review (Part 4 of the Article on Administration (Article 6))] applies to and governs all administrative action taken by the Administrator pursuant to this Part.

[¶ 923] Loan Finance Charge for Supervised Loans

Sec. 3.508. (1) With respect to a supervised loan, including a loan pursuant to a revolving loan account, a supervised lender may contract for and receive a loan finance charge not exceeding that permitted by this section.

(2) The loan finance charge, calculated according to the United States rule, may not exceed the equivalent of the greater of either of the following:

(a) the total of

(i) 36 per cent per year on that part of the unpaid balances of the principal which is $300 or less;

(ii) 21 per cent per year on that part of the unpaid balances of the principal which is more than $300 but does not exceed $1,000; and

(iii) 15 per cent per year on that part of the unpaid balances of the principal which is more than $1,000; or

(b) 18 per cent per year on the unpaid balances of the principal.

(3) This section does not limit or restrict the manner of contracting for the loan finance charge, whether by way of add-on, discount, or otherwise, so long as the rate of the loan finance charge does not exceed that permitted by this section. If the loan is precomputed,

(a) the loan finance charge may be calculated on the assumption that all scheduled payments will be made when due, and

(b) the effect of prepayment is governed by the provisions on rebate upon prepayment (Section 3.210).

(4) The term of a loan for the purposes of this section commences on the date the loan is made. Differences in the lengths of months are disregarded and a day may be counted as 1/30th of a month. Subject to classifications and differentiations the lender may reasonably establish, a part of a month in excess of 15 days may be treated as a full month if periods of 15 days or less are disregarded and if that procedure is not consistently used to obtain a greater yield than would otherwise be permitted.

(5) Subject to classifications and differentiations the lender may reasonably establish, he may make the same loan finance charge on all principal amounts within a specified range. A loan finance charge so made does not violate subsection (2) if

(a) when applied to the median amount within each range, it does not exceed the maximum permitted in subsection (2), and

(b) when applied to the lowest amount within each range, it does not produce a rate of loan finance charge exceeding the rate calculated according to paragraph (a) by more than 8 per cent of the rate calculated according to paragraph (a).

(6) The amounts of $300 and $1,000 in subsection (2) are subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

COMMENT

See Comment to Section 2.201. Since there is no basic economic difference between loans pursuant to a revolving loan account and precomputed instalments loans, which may be, and often are, refinanced or deferred, the same rate ceiling is provided for all supervised loans. Lenders are not required to use a graduated rate, but may find it more economical to use a flat monthly rate of charge, provided that it does not exceed the rate ceiling specified. Lenders offering revolving loan accounts may not levy delinquency charges (3.203), and deferral charges (3.204), or a loan finance charge on refinancing (3.205). At the same time a debtor is not entitled to rebates upon prepayment (3.210), since at the time of his prepayment there will be no prepaid, but unearned, finance charges on his revolving loan account.

[¶ 924] Use of Multiple Agreements

Sec. 3.509. With respect to a supervised loan, no lender may permit any person, or husband and wife, to become obligated in any way under more than one loan agreement with the lender or with a person related to the lender, with intent to obtain a higher rate of loan finance charge than would otherwise be permitted by the provisions on loan finance charge for supervised loans (Section 3.508) or to avoid disclosure of an annual percentage rate pursuant to the provisions on disclosure and advertising (Part 3). The excess amount of loan finance charge provided for in agreements in violation of this section are excess charges for the purposes of the provisions on effect of violations on rights of parties (Section 5.202) and the provisions on civil actions by Administrator (Section 6.113).

[¶ 925] Restrictions on Interest in Land as Security

Sec. 3.510. (1) With respect to a supervised loan in which the principal is $1,000 or less, a lender may not contract for an interest in land as security. A security interest taken in violation of this section is void.

(2) The amount of $1,000 in subsection (1) is subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

[¶ 926] [Limitation on Attorney's Fees]

[**Sec. 3.511.** (1) With respect to a supervised loan in which the principal is $1,000 or less, the agreement may not provide for the payment by the debtor of attorney's fees. A provision in violation of this section is unenforceable.

(2) The amount of $1,000 in subsection (1) is subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).]

COMMENT

If Alternative A of Section 3.404 is enacted, Section 3.511 should be omitted.

[¶ 927] Regular Schedule of Payments; Maximum Loan Term

Sec. 3.512. (1) Regulated loans payable in instalments, other than loans pursuant to a revolving loan account, in which the principal is $1,000 or less shall be repayable in substantially equal instalments which shall be payable at equal periodic intervals except to the extent that the schedule of payments is adjusted to the seasonal or irregular income of the debtor. Regulated loans payable in instalments, other than loans pursuant to a revolving loan account, in which the principal is $300 or less shall be scheduled to be payable over a period of not more than 25 months, and regulated loans in which the principal is more than $300 but does not exceed $1,000 shall be scheduled to be payable over a period of not more than 37 months.

(2) The amounts of $300 and $1,000 in subsection (1) are subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

[¶ 928] Conduct of Business Other than Making Loans

Sec. 3.513. A licensee may carry on other business at a location where he makes supervised loans unless he carries on other business for the purpose of evasion or violation of this Act.

COMMENT

A seller who makes loans must comply with Article 3 with respect to his loan operations.

[¶ 929] Application of Other Provisions

Sec. 3.514. Except as otherwise provided, all provisions of this Act applying to consumer loans apply to regulated loans.

PART 6—LOANS OTHER THAN CONSUMER LOANS

[¶ 930] Loans Subject to Act by Agreement of Parties

Sec. 3.601. The parties to a loan other than a consumer loan may agree in a writing signed by the parties that the loan is subject to the provisions of this Act applying to consumer loans. If the parties so agree, the loan is a consumer loan for the purposes of this Act.

[¶ 931] Definition: "Consumer Related Loan"; Rate of Loan Finance Charge

Sec. 3.602. (1) A "consumer related loan" is a loan which is not subject to the provisions of this Act applying to consumer loans and in which the principal does not exceed $25,000, if

(a) the debtor is a person other than an organization, or

(b) the debt is secured primarily by a security interest in a one or two family dwelling occupied by a person related to the debtor.

(2) With respect to a consumer related loan, including one made pursuant to a revolving loan account, the parties may contract for the payment

of a loan finance charge not in excess of that permitted by the provisions on loan finance charge for consumer loans other than supervised loans (Section 3.201).

(3) The amount of $25,000 in subsection (1) is subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

COMMENT

See Comment to Section 2.602.

[¶ 932] Applicability of Other Provisions to Consumer Related Loans

Sec. 3.603. Except for the rate of the loan finance charge and the rights to prepay and to rebate upon prepayment, the provisions of Part 2 of this Article apply to a consumer related loan.

[¶ 933] Limitation on Default Charges in Consumer Related Loans

Sec. 3.604. (1) The agreement with respect to a consumer related loan may provide for only the following charges as a result of the debtor's default:

(a) reasonable attorney's fees and reasonable expenses incurred in realizing on a security interest;

(b) deferral charges not in excess of 18 per cent per year of the amount deferred for the period of deferral; and

(c) other charges that could have been made had the loan been a consumer loan.

(2) A provision in violation of this section is unenforceable.

[¶ 934] Loan Finance Charge for Other Loans

Sec. 3.605. With respect to a loan other than a consumer loan or a consumer related loan, the parties may contract for the payment by the debtor of any loan finance charge.

COMMENT

See Section 5.107—Extortionate Extensions of Credit.

Article 4—Insurance

PART 1—INSURANCE IN GENERAL

[¶ 935] Short Title

Sec. 4.101. This Article shall be known and may be cited as Uniform Consumer Credit Code—Insurance.

[¶ 936] Scope [; Relation to Credit Insurance Act; Applicability to Parties]

Sec. 4.102. (1) Except as provided in subsection (2), this Article applies to insurance provided or to be provided in relation to a consumer credit sale (Section 2.104), a consumer lease (Section 2.106), or a consumer loan (Section 3.104).

(2) The provision on cancellation by a creditor (Section 4.304) applies to loans the primary purpose of which is the financing of insurance. No other provision of this Article applies to insurance so financed.

[(3) This Article supplements and does not repeal the Credit Insurance Act. The provisions of this Act concerning administrative controls, liabilities, and penalties do not apply to persons acting as insurers, and the similar provisions of the Credit Insurance Act do not apply to creditors and debtors.]

COMMENT

If the enacting State has not already enacted the NAIC Model Act for the regulation of credit life insurance and credit accident and health insurance, or similar legislation, material in brackets should be omitted.

By subsection (2) a single provision of this Article is made applicable to lenders engaged in insurance premium financing. (The borrower should be forewarned of cancellation of his insurance by the lender: Section 4.304.) Nothing else in this Article affects the practices of a lender in that business.

The Special Committee is aware that premium financing is regulated under special statutes in a number of states. It has considered the alternative courses of (1) exempting premium loans from this Act, and (2) proposing distinctive rules for premium loans as opposed to consumer loans generally. The Special Committee has concluded, after deliberation, that the provisions of this Act may appropriately be applied to insurance premium loans.

[¶ 937] Definition[s]: "Consumer Credit Insurance" [; "Credit Insurance Act"]

Sec. 4.103. In this Act [(1)] "Consumer credit insurance" means insurance, other than insurance on property, by which the satisfaction of debt in whole or in part is a benefit provided, but does not include

(a) insurance provided in relation to a credit transaction in which a payment is scheduled more than 10 years after the extension of credit;

(b) insurance issued as an isolated transaction on the part of the insurer not related to an agreement or plan for insuring debtors of the creditor; or

(c) insurance indemnifying the creditor against loss due to the debtor's default.

[(2) "Credit Insurance Act" means [NAIC Model Act, or any similar statute].]

COMMENT

If the enacting State has not already enacted the NAIC Model Act for the regulation of credit life insurance and credit accident and health insurance, or similar legislation, material in brackets should be omitted.

[¶ 938] Creditor's Provision of and Charge for Insurance; Excess Amount of Charge

Sec. 4.104. (1) Except as otherwise provided in this Article and subject to the provisions on additional charges (Section 2.202 and Section 3.202) and maximum charges (Part 2 of Article 2 and Article 3), a creditor may agree to provide insurance, and may contract for and receive a charge for insurance separate from and in addition to other charges. A creditor need not make a separate charge for insurance provided or required by him. This Act does not authorize the issuance of any insurance prohibited under any statute, or rule thereunder, governing the business of insurance.

(2) The excess amount of a charge for insurance provided for in agreements in violation of this Article is an excess charge for the purposes of the provisions of the Article on Remedies and Penalties (Article 5) as to effect of violations on rights of parties (Section 5.202) and of the provisions of the Article on Administration (Article 6) as to civil actions by the Administrator (Section 6.113).

COMMENT

Consideration has been given to the desirability of defining a "separate charge" for consumer credit insurance when the seller or lender establishes different rates of charge for sale or loan transactions predicated on whether or not consumer credit insurance is provided. The question has recently been raised by supervisory authorities in New York, where the creditors affected resolved the problem by increasing the rate of charge on transactions as to which consumer credit insurance was previously not provided to the higher rate of charge which had previously applied only to transactions as to which consumer credit insurance was provided.

It has been concluded that:

1. A definition of "separate charge" for insurance in the light of variations in credit service or loan finance charge rates depending on whether or not consumer credit insurance is provided would be futile.

2. The required disclosure of credit service charge or loan finance charge in terms of an annual percentage rate coupled with permission for exclusion from the credit service or loan finance charge and separate dollar disclosure of the charge for consumer credit insurance will encourage creditors to reduce to a minimum the disclosed rate of credit service or loan finance charge and to disclose the charge for consumer credit insurance as a separate charge not included in the credit service or loan finance charge.

[¶ 939] Conditions Applying to Insurance to Be Provided by Creditor

Sec. 4.105. If a creditor agrees with a debtor to provide insurance

(1) the insurance shall be evidenced by an individual policy or certificate of insurance delivered to the debtor, or sent to him at his address as stated by him, within 30 days after the term of the insurance commences under the agreement between the creditor and debtor; or

(2) the creditor shall promptly notify the debtor of any failure or delay in providing the insurance.

[¶ 940] Unconscionability

Sec. 4.106. (1) In applying the provisions of the Act on unconscionability (Sections 5.108 and 6.111) to a separate charge for insurance, consideration shall be given, among other factors, to

(a) potential benefits to the debtor including the satisfaction of his obligations;

(b) the creditor's need for the protection provided by the insurance; and

(c) the relation between the amount and terms of credit granted and the insurance benefits provided.

(2) If consumer credit insurance otherwise complies with this Article and other applicable law, neither the amount nor the term of the insurance nor the amount of a charge therefor is in itself unconscionable.

[¶ 941] Maximum Charge by Creditor for Insurance

Sec. 4.107. (1) Except as provided in subsection (2), if a creditor contracts for or receives a separate charge for insurance, the amount charged to the debtor for the insurance may not exceed the premium to be charged by the insurer, as computed at the time the charge to the debtor is determined, conforming to any rate filings required by law and made by the insurer with the [Commissioner] of Insurance.

(2) A creditor who provides consumer credit insurance in relation to a revolving charge account (Section 2.108) or revolving loan account (Section 3.108) may calculate the charge to the debtor in each billing cycle by applying the current premium rate to

(a) the average daily unpaid balance of the debt in the cycle;

(b) the unpaid balance of the debt or a median amount within a specified range of unpaid balances of debt on approximately the same day of the cycle. The day of the cycle need not be the day used in calculating the credit service charge (Section 2.207) or loan finance charge (Section 3.201 and Section 3.508), but the specified range shall be the range used for that purpose; or

(c) the unpaid balances of principal calculated according to the United States rule.

[¶ 942] Refund or Credit Required; Amount

Sec. 4.108. (1) Upon prepayment in full of a consumer credit sale or consumer loan by the proceeds of consumer credit insurance, the debtor or his estate is entitled to a refund of any portion of a separate charge for insurance which by reason of prepayment is retained by the creditor or returned to him by the insurer unless the charge was computed from time to time on the basis of the balances of the debtor's account.

(2) This Article does not require a creditor to grant a refund or credit to the debtor if all refunds and credits due to the debtor under this Article amount is less than $1, and except as provided in subsection (1) does not require the creditor to account to the debtor for any portion of a separate charge for insurance because

(a) the insurance is terminated by performance of the insurer's obligation;

(b) the creditor pays or accounts for premiums to the insurer in amounts and at times determined by the agreement between them; or

(c) the creditor receives directly or indirectly under any policy of insurance a gain or advantage not prohibited by law.

(3) Except as provided in subsection (2), the creditor shall promptly make or cause to be made an appropriate refund or credit to the debtor with respect to any separate charge made to him for insurance if

(a) insurance is not provided or is provided for a shorter term than that for which the charge to the debtor for insurance was computed; or

(b) the insurance terminates prior to the end of the term for which it was written because of prepayment in full or otherwise.

(4) A refund or credit required by subsection (3) is appropriate as to amount if it is computed according to a method prescribed or approved by the [Commissioner] of Insurance or a formula filed by the insurer with the [Commissioner] of Insurance at least 30 days before the debtor's right to a refund or credit becomes determinable, unless the method or formula is employed after the [Commissioner] of Insurance notifies the insurer that he disapproves it.

COMMENT

Subsection (2)(c) of Section 4.108 permits a creditor to derive from consumer credit insurance gains and advantages such as dividends and refunds resulting from favorable mortality or morbidity experience with respect to insured debtors.

The provisions of Article 4 relating to consumer credit insurance are predicated on the Special Committee's conclusions that:

1. Although the gains and advantages may be large to the creditor, they are relatively insignificant to each insured debtor and the calculating, clerical and mailing costs of returning them to insured debtors would be unreasonably disproportionate to the amounts involved.

2. The requirements of Article 4 that premiums for consumer credit insurance be reasonable in relation to benefits, if properly enforced by the State insurance commissioner or superintendent, will preclude the possibility of the use of consumer credit insurance as a device by creditors for concealing hidden charges from debtors.

[¶ 943] Existing Insurance; Choice of Insurer

Sec. 4.109. If a creditor requires insurance, upon notice to the creditor the debtor shall have the option of providing the required insurance through an existing policy of insurance owned or controlled by the debtor, or through a policy to be obtained and paid for by the debtor, but the creditor may for reasonable cause decline the insurance provided by the debtor.

[¶ 944] Charge for Insurance in Connection with a Deferral, Refinancing, or Consolidation; Duplicate Charges

Sec. 4.110. (1) A creditor may not contract for or receive a separate charge for insurance in connection with a deferral (Section 2.204 or Section 3.204), a refinancing (Section 2.205 or Section 3.205), or a consolidation (Section 2.206 or Section 3.206), unless

(a) the debtor agrees at or before the time of the deferral, refinancing, or consolidation that the charge may be made;

(b) the debtor is or is to be provided with insurance for an amount or a term, or insurance of a kind, in addition to that to which he would have been entitled had there been no deferral, refinancing, or consolidation;

(c) the debtor receives a refund or credit on account of any unexpired term of existing insurance in the amount that would be required if the insurance were terminated (Section 4.108); and

(d) the charge does not exceed the amount permitted by this Article (Section 4.107).

(2) A creditor may not contract for or receive a separate charge for insurance which duplicates insurance with respect to which the creditor has previously contracted for or received a separate charge.

[¶ 945] Cooperation Between Administrator and [Commissioner] of Insurance

Sec. 4.111. The Administrator and the [Commissioner] of Insurance are authorized and directed to consult and assist one another in maintaining compliance with this Article. They may jointly pursue investigations, prosecute suits, and take other official action, as may seem to them appropriate, if either of them is otherwise empowered to take the action. If the Administrator is informed of a violation or suspected violation by an insurer of this Article, or of the insurance laws, rules, and regulations of this State, he shall advise the [Commissioner] of Insurance of the circumstances.

[¶ 946] [Administrative Action of [Commissioner] of Insurance]

[**Sec. 4.112.** (1) To the extent that his responsibility under this Article requires, the [Commissioner] of Insurance shall issue rules with respect to insurers, and with respect to refunds (Section 4.108), forms, schedules of premium rates and charges (Section 4.203), and his approval or disapproval thereof and, in case of violation, may make an order for compliance.

(2) [The State administrative procedure act] [Each provision of the Part on Administrative Procedures and Judicial Review (Part 4) of the Article on Administration (Article 6) which applies to and governs administrative action taken by the Administrator also] applies to and governs all administrative action taken by the [Commissioner] of Insurance pursuant to this section.]

COMMENT

This section may be omitted in an enacting State in which the NAIC Model Act or any similar statute and adequate statutes applying to and governing administrative action taken by the [Commissioner] of Insurance are in force.

PART 2—CONSUMER CREDIT INSURANCE

[¶ 947] Term of Insurance

Sec. 4.201. (1) Consumer credit insurance provided by a creditor may be subject to the furnishing of evidence of insurability satisfactory to the insurer. Whether or not such evidence is required, the term of the insurance shall commence

no later than when the debtor becomes obligated to the creditor or when the debtor applies for the insurance, whichever is later, except as follows:

(a) if any required evidence of insurability is not furnished until more than 30 days after the term would otherwise commence, the term may commence on the date when the insurer determines the evidence to be satisfactory; or

(b) if the creditor provides insurance not previously provided covering debts previously created, the term may commence on the effective date of the policy.

(2) The originally scheduled term of the insurance shall extend at least until the due date of the last scheduled payment of the debt except as follows:

(a) if the insurance relates to a revolving charge account or revolving loan account, the term need extend only until the payment of the debt under the account and may be sooner terminated after at least 30 days' notice to the debtor; or

(b) if the debtor is advised in writing that the insurance will be written for a specified shorter time, the term need extend only until the end of the specified time.

(3) The term of the insurance shall not extend more than 15 days after the originally scheduled due date of the last scheduled payment of the debt unless it is extended without additional cost to the debtor or as an incident to a deferral, refinancing, or consolidation.

[¶ 948] Amount of Insurance

Sec. 4.202. (1) Except as provided in subsection (2),

(a) in the case of consumer credit insurance providing life coverage, the amount of insurance may not initially exceed the debt and, if the debt is payable in instalments, may not at any time exceed the greater of the scheduled or actual amount of the debt; or

(b) in the case of any other consumer credit insurance, the total amount of periodic benefits payable may not exceed the total of scheduled unpaid instalments of the debt, and the amount of any periodic benefit may not exceed the original amount of debt divided by the number of periodic instalments in which it is payable.

(2) If consumer credit insurance is provided in connection with a revolving charge account or revolving loan account, the amounts payable as insurance benefits may be reasonably commensurate with the amount of debt as it exists from time to time. If consumer credit insurance is provided in connection with a commitment to grant credit in the future, the amounts payable as insurance benefits may be reasonably commensurate with the total from time to time of the amount of debt and the amount of the commitment. If the debt or the commitment is primarily for an agricultural purpose, and there is no regular schedule of payments, the amounts payable as insurance benefits may equal the total of the initial amount of debt and the amount of the commitment.

[¶ 949] Filing and Approval of Rates and Forms

Sec. 4.203. (1) A creditor may not use a form, or a schedule of premium rates or charges, the filing of which is required by this section, if the [Com-

missioner] of Insurance has disapproved the form or schedule and has notified the insurer of his disapproval. A creditor may not use a form or schedule unless

(a) the form or schedule has been on file with the [Commissioner] of Insurance for 30 days, or has earlier been approved by him; and

(b) the insurer has complied with this section with respect to the insurance.

(2) Except as provided in subsection (3), all policies, certificates of insurance, notices of proposed insurance, applications for insurance, endorsements and riders relating to consumer credit insurance delivered or issued for delivery in this State, and the schedules of premium rates or charges pertaining thereto, shall be filed by the insurer with the [Commissioner] of Insurance. He shall, within 30 days after the filing of any form or schedule, disapprove it if the premium rates or charges are unreasonable in relation to the benefits provided under the form, or if the form contains provisions which are unjust, unfair, inequitable, or deceptive or encourage misrepresentation of the coverage or are contrary to any provision of the [Insurance Code] or of any rule or regulation promulgated thereunder.

(3) If a group policy has been delivered in another state, the forms to be filed by the insurer with the [Commissioner] of Insurance are the group certificates and notices of proposed insurance. He shall approve them if

(a) they provide the information that would be required if the group policy were delivered in this State; and

(b) the applicable premium rates or charges do not exceed those established by his rules or regulations.

COMMENT

Subsection (2) follows the formulation of New York Insurance Law Section 154.7, which has been upheld by the New York Court of Appeals as directing the New York Superintendent of Insurance not to approve premium rates for consumer credit insurance if they are "unreasonable in relation to the benefits provided" under the related form of policy or certificate. Some doubt has been expressed as to whether the Commissioner of Insurance has the same power under the provisions of paragraph B of Section 7 of the NAIC Model Act, which require the Commissioner to "disapprove any . . . form if the benefits provided therein are not reasonable in relation to the premium charge."

PART 3—PROPERTY AND LIABILITY INSURANCE

[¶ 950] Property Insurance

Sec. 4.301. (1) A creditor may not contract for or receive a separate charge for insurance against loss of or damage to property unless

(a) the insurance covers a substantial risk of loss of or damage to property related to the credit transaction;

(b) the amount, terms, and conditions of the insurance are reasonable in relation to the character and value of the property insured or to be insured; and

(c) the term of the insurance is reasonable in relation to the terms of credit.

(2) The term of the insurance is reasonable if it is customary and does not extend substantially beyond a scheduled maturity.

(3) A creditor may not contract for or receive a separate charge for insurance against loss of or damage to property unless the amount financed or principal exclusive of charges for the insurance is $300 or more, and the value of the property is $300 or more.

(4) The amounts of $300 in subsection (3) are subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

[¶ 951] Insurance on Creditor's Interest Only

Sec. 4.302. If a creditor contracts for or receives a separate charge for insurance against loss of or damage to property, the risk of loss or damage not willfully caused by the debtor is on the debtor only to the extent of any deficiency in the effective coverage of the insurance, even though the insurance covers only the interest of the creditor.

COMMENT

The allocation of loss under this section is not to be upset by subrogation.

[¶ 952] Liability Insurance

Sec. 4.303. A creditor may not contract for or receive a separate charge for insurance against liability unless the insurance covers a substantial risk of liability arising out of the ownership or use of property related to the credit transaction.

[¶ 953] Cancellation by Creditor

Sec. 4.304. A creditor shall not request cancellation of a policy of property or liability insurance except after the debtor's default or in accordance with a written authorization by the debtor, and in either case the cancellation does not take effect until written notice is delivered to the debtor or mailed to him at his address as stated by him. The notice shall state that the policy may be cancelled on a date not less than 10 days after the notice is delivered, or, if the notice is mailed, not less than 13 days after it is mailed.

Article 5—Remedies and Penalties

PART 1—LIMITATIONS ON CREDITORS' REMEDIES

[¶ 954] Short Title

Sec. 5.101. This Article shall be known and may be cited as Uniform Consumer Credit Code—Remedies and Penalties.

[¶ 955] Scope

Sec. 5.102. This Part applies to actions or other proceedings to enforce rights arising from consumer credit sales, consumer leases and consumer loans; and, in addition, to extortionate extensions of credit (Section 5.107).

COMMENT

Section 1.201 states the territorial applicability of this Act. Sections 2.601 and 3.601 provide for the applicability of this Act by written agreement.

[¶ 956] Restrictions on Deficiency Judgments in Consumer Credit Sales

Sec. 5.103. (1) This section applies to a consumer credit sale of goods or services.

(2) If the seller repossesses or voluntarily accepts surrender of goods which were the subject of the sale and in which he has a security interest and the cash price of the goods repossessed or surrendered was $1000 or less, the buyer is not personally liable to the seller for the unpaid balance of the debt arising from the sale of the goods, and the seller is not obligated to resell the collateral.

(3) If the seller repossesses or voluntarily accepts surrender of goods which were not the subject of the sale but in which he has a security interest to secure a debt arising from a sale of goods or services or a combined sale of goods and services and the cash price of the sale was $1000 or less, the buyer is not personally liable to the seller for the unpaid balance of the debt arising from the sale.

(4) For the purpose of determining the unpaid balance of consolidated debts or debts pursuant to revolving charge accounts, the allocation of payments to a debt shall be determined in the same manner as provided for determining the amount of debt secured by various security interests (Section 2.409).

(5) The buyer may be liable in damages to the seller if the buyer has wrongfully damaged the collateral or if, after default and demand, the buyer has wrongfully failed to make the collateral available to the seller.

(6) If the seller elects to bring an action against the buyer for a debt arising from a consumer credit sale of goods or services, when under this section he would not be entitled to a deficiency judgment if he repossessed the collateral, and obtains judgment

(a) he may not repossess the collateral, and

(b) the collateral is not subject to levy or sale on execution or similar proceedings pursuant to the judgment.

(7) The amounts of $1000 in subsection (2) and (3) are subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

[¶ 957] No Garnishment Before Judgment

Sec. 5.104. Prior to entry of judgment in an action against the debtor for debt arising from a consumer credit sale, a consumer lease, or a consumer loan, the creditor may not attach unpaid earnings of the debtor by garnishment or like proceedings.

[¶ 958] Limitation on Garnishment

Sec. 5.105. (1) For the purposes of this Part

(a) "disposable earnings" means that part of the earnings of an individual remaining after the deduction from those earnings of amounts required by law to be withheld; and

(b) "garnishment" means any legal or equitable procedure through which the earnings of an individual are required to be withheld for payment of a debt.

(2) The maximum part of the aggregate disposable earnings of an individual for any workweek which is subjected to garnishment to enforce payment of a judgment arising from a consumer credit sale, consumer lease, or consumer loan may not exceed the lesser of

(a) 25 per cent of his disposable earnings for that week, or

(b) the amount by which his disposable earnings for that week exceed forty times the Federal minimum hourly wage prescribed by Section 6 (a)(1) of the Fair Labor Standards Act of 1938, U. S. C. tit. 29, § 206(a)(1), in effect at the time the earnings are payable.

(c) In the case of earnings for a pay period other than a week, the Administrator shall by rule prescribe a multiple of the Federal minimum hourly wage equivalent in effect to that set forth in paragraph (b).

(3) No court may make, execute, or enforce an order or process in violation of this section.

COMMENT

This section is derived from CCPA Sections 302 and 303. The exemption has been increased from thirty times the minimum hourly wage to forty in the belief that the higher figure was justified in consumer transactions.

[¶ 959] No Discharge From Employment for Garnishment

Sec. 5.106. No employer shall discharge an employee for the reason that a creditor of the employee has subjected or attempted to subject unpaid earnings of the employee to garnishment or like proceedings directed to the employer for the purpose of paying a judgment arising from a consumer credit sale, consumer lease, or consumer loan.

COMMENT

The penalty for violation of this section is found in Section 5.202(6).

This Section is derived from CCPA § 304. However, it prohibits an employer from discharging an employee by reason of any garnishment (whether one or more) under a judgment arising from a consumer credit sale, consumer lease, or consumer loan.

[¶ 960] Extortionate Extensions of Credit

Sec. 5.107. (1) If it is the understanding of the creditor and the debtor at the time an extension of credit is made that delay in making repayment or failure to make repayment could result in the use of violence or other criminal means to cause harm to the person, reputation, or property of any person, the repayment of the extension of credit is unenforceable through civil judicial processes against the debtor.

(2) If it is shown that an extension of credit was made at an annual rate exceeding 45 per cent calculated according to the United States rule and that the creditor then had a reputation for the use or threat of use of violence or other criminal means to cause harm to the person, reputation, or property of any person to collect extensions of credit or to punish the nonrepayment thereof, there is prima facie evidence that the extension of credit was unenforceable under subsection (1).

COMMENT

This section is derived from CCPA Section 892.

[¶ 961] Unconscionability

Sec. 5.108. (1) With respect to a consumer credit sale, consumer lease, or consumer loan, if the court as a matter of law finds the agreement or any clause of the agreement to have been unconscionable at the time it was made the court may refuse to enforce the agreement, or it may enforce the remainder of the agreement without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.

(2) If it is claimed or appears to the court that the agreement or any clause thereof may be unconscionable the parties shall be afforded a reasonable opportunity to present evidence as to its setting, purpose, and effect to aid the court in making the determination.

(3) For the purpose of this section, a charge or practice expressly permitted by this Act is not in itself unconscionable.

COMMENT

Subsections (1) and (2) are derived from UCC Section 2-302.

PART 2—DEBTORS' REMEDIES

[¶ 962] Interests in Land

Sec. 5.201. For purposes of the provisions of this Part on civil liability for violation of disclosure provisions (Section 5.203) and on debtor's right to rescind certain transactions (Section 5.204)

(1) consumer credit sale includes a sale of an interest in land without regard to the rate of the credit service charge if the sale is otherwise a consumer credit sale (Section 2.104); and

(2) consumer loan includes a loan primarily secured by an interest in land without regard to the rate of the loan finance charge if the loan is otherwise a consumer loan (Section 3.104).

COMMENT

Sections 5.203 and 5.204 apply to transactions secured by interests in land even though the credit service charge or loan finance charge does not exceed 10%.

[¶ 963] Effect of Violations on Rights of Parties

Sec. 5.202. (1) If a creditor has violated the provisions of this Act applying to certain negotiable instruments (Section 2.403), or limitations on the schedule of payments or loan term for regulated loans (Section 3.512), the debtor is not obligated to pay the credit service charge or loan finance charge, and has a right to recover from the person violating this Act or from an assignee of that person's rights who undertakes direct collection of payments or enforcement of rights arising from the debt a penalty in an amount determined by the court not in excess of three times the amount of the credit service charge or loan finance charge. No action pursuant to this subsection may be brought more than one year after the due date of the last scheduled payment of the agreement with respect to which the violation occurred.

(2) If a creditor has violated the provisions of this Act applying to authority to make supervised loans (Section 3.502), the loan is void and the debtor is not obligated to pay either the principal or loan finance charge. If he has paid any part of the principal or of the loan finance charge, he has a right to recover the payment from the person violating this Act or from an assignee of that person's rights who undertakes direct collection of payments or enforcement of rights arising from the debt. With respect to violations arising from loans made pursuant to revolving loan accounts, no action pursuant to this subsection may be brought more than two years after the violation occurred. With respect to violations arising from other loans, no action pursuant to this subsection may be brought more than one year after the due date of the last scheduled payment of the agreement pursuant to which the charge was paid.

(3) A debtor is not obligated to pay a charge in excess of that allowed by this Act, and if he has paid an excess charge he has a right to a refund. A refund may be made by reducing the debtor's obligation by the amount of the excess charge. If the debtor has paid an amount in excess of the lawful obligation under the agreement, the debtor may recover the excess amount from the person who made the excess charge or from an assignee of that person's rights who undertakes direct collection of payments from or enforcement of rights against debtors arising from the debt.

(4) If a debtor is entitled to a refund and a person liable to the debtor refuses to make a refund within a reasonable time after demand, the debtor may recover from that person a penalty in an amount determined by a court not exceeding the greater of either the amount of the credit service or loan finance charge or ten times the amount of the excess charge. If the creditor has made an excess charge in deliberate violation of or in reckless disregard for this Act, the penalty may be recovered even though the creditor has refunded the excess charge. No penalty pursuant to this subsection may be recovered if a court has ordered a similar penalty assessed against the same person in a civil action by the Administrator (Section 6.113). With respect to excess charges arising from sales made pursuant to revolving charge accounts or from loans made pursuant to revolving loan accounts, no action pursuant to this subsection may be brought more than two years after the time the

excess charge was made. With respect to excess charges arising from other consumer credit sales or consumer loans, no action pursuant to this subsection may be brought more than one year after the due date of the last scheduled payment of the agreement pursuant to which the charge was made.

(5) Except as otherwise provided, no violation of this Act impairs rights on a debt.

(6) If an employer discharges an employee in violation of the provisions prohibiting discharge (Section 5.106), the employee may within [ ] days bring a civil action for recovery of wages lost as a result of the violation and for an order requiring the reinstatement of the employee. Damages recoverable shall not exceed lost wages for six weeks.

(7) If the creditor establishes by a preponderance of evidence that a violation is unintentional or the result of a bona fide error no liability is imposed under subsections (1), (2), and (4) and the validity of the transaction is not affected.

(8) In any case in which it is found that a creditor has violated this Act, the court may award reasonable attorney's fees incurred by the debtor.

[¶ 964] Civil Liability for Violation of Disclosure Provisions

Sec. 5.203. (1) Except as otherwise provided in this section, a creditor who, in violation of the provisions on disclosure (Part 3), other than the provisions on advertising (Sections 2.313 and 3.312), of the Article on Credit Sales (Article 2) and the Article on Loans (Article 3), fails to disclose information to a person entitled to the information under this Act is liable to that person in an amount equal to the sum of

(a) twice the amount of the credit service or loan finance charge in connection with the transaction, but the liability pursuant to this paragraph shall be not less than $100 nor more than $1000; and

(b) in the case of a successful action to enforce the liability under paragraph (a), the costs of the action together with reasonable attorney's fees as determined by the court.

(2) A creditor has no liability under this section if within 15 days after discovering an error, and prior to the institution of an action under this section or the receipt of written notice of the error, the creditor notifies the person concerned of the error and makes whatever adjustments in the appropriate account are necessary to insure that the person will not be required to pay a credit service charge or loan finance charge in excess of the amount or percentage rate actually disclosed.

(3) A creditor may not be held liable in any action brought under this section for a violation of this Act if the creditor shows by a preponderance of evidence that the violation was not intentional and resulted from a bona fide error notwithstanding the maintenance of procedures reasonably adapted to avoid the error.

(4) Any action which may be brought under this section against the original creditor in any credit transaction involving a security interest in land may be maintained against any subsequent assignee of the original creditor where the assignee, its subsidiaries, or affiliates were in a continuing business relationship with the original creditor either at the time the credit

was extended or at the time of the assignment, unless the assignment was involuntary, or the assignee shows by a preponderance of evidence that it did not have reasonable grounds to believe that the original creditor was engaged in violations of this Act and that it maintained procedures reasonably adapted to apprise it of the existence of the violations.

(5) No action pursuant to this section may be brought more than one year after the date of the occurrence of the violation.

COMMENT

This section is derived from Section 130 of the CCPA.

[¶ 965] Debtor's Right to Rescind Certain Transactions

Sec. 5.204. (1) Except as otherwise provided in this section, in the case of a consumer credit sale or consumer loan with respect to which a security interest is retained or acquired in an interest in land which is used or expected to be used as the residence of the person to whom credit is extended, the debtor shall have the right to rescind the transaction until midnight of the third business day following the consummation of the transaction or the delivery of the disclosures required under this section and all other material disclosures required by this Act, whichever is later, by notifying the creditor, in accordance with rules of the Administrator, of his intention to do so. The creditor shall clearly and conspicuously disclose, in accordance with rules of the Administrator, to the debtor in a transaction subject to this section the rights of the debtor under this section. The creditor shall also provide, in accordance with rules of the Administrator, an adequate opportunity to the obligor to exercise his right to rescind any transaction subject to this section.

(2) When a debtor exercises his right to rescind under subsection (1), he is not liable for any credit service charge, loan finance charge, or other charge, and any security interest given by the debtor becomes void upon the rescission. Within 10 days after receipt of a notice of rescission, the creditor shall return to the debtor the money or property given as earnest money, down payment, or otherwise, and shall take any action necessary or appropriate to reflect the termination of any security interest created under the transaction. If the creditor has delivered property to the debtor, the debtor may retain possession of it. Upon the performance of the creditor's obligations under this section, the debtor shall tender the property to the creditor, except that if return of the property in kind would be impractical or inequitable, the debtor shall tender its reasonable value. Tender shall be made at the location of the property or at the residence of the debtor, at the option of the debtor. If the creditor does not take possession of the property within 10 days after tender by the debtor, ownership of the property vests in the debtor without obligation on his part to pay for it.

(3) Notwithstanding any rule of evidence, written acknowledgment of receipt of any disclosure required under this Act by a person to whom a statement is required to be given pursuant to this section does no more than create a rebuttable presumption of delivery thereof.

(4) The Administrator may, if he finds that the action is necessary in order to permit homeowners to meet bona fide personal financial emergencies, prescribe rules authorizing the modification or waiver of any rights created under this section to the extent and under the circumstances set forth in those rules.

(5) This section does not apply to the creation or retention of a first lien against a dwelling to finance the acquisition of that dwelling.

COMMENT

This section is derived from CCPA Section 125.

[¶ 966] Refunds and Penalties as Set-Off to Obligation

Sec. 5.205. Refunds or penalties to which the debtor is entitled pursuant to this Part may be set off against the debtor's obligation, and may be raised as a defense to a suit on the obligation without regard to the time limitations prescribed by this Part.

PART 3—CRIMINAL PENALTIES

[¶ 967] Willful Violations

Sec. 5.301. (1) A supervised lender who willfully makes charges in excess of those permitted by the provisions of the Article on Loans (Article 3) applying to supervised loans (Part 5) is guilty of a misdemeanor and upon conviction may be [sentenced to pay a fine not exceeding $[ ], or to imprisonment not exceeding one year, or both].

(2) A person, other than a supervised financial organization, who willfully engages in the business of making supervised loans without a license in violation of the provisions of this Act applying to authority to make supervised loans (Section 3.502) is guilty of a misdemeanor and upon conviction may be [sentenced to pay a fine not exceeding $[ ], or to imprisonment not exceeding one year, or both].

(3) A person who willfully engages in the business of making consumer credit sales, consumer leases, or consumer loans, or of taking assignments of rights against debtors arising therefrom and undertakes direct collection of payments or enforcement of these rights, without complying with the provisions of this Act concerning notification (Section 6.202) or payment of fees (Section 6.203), is guilty of a misdemeanor and upon conviction may be [sentenced to pay a fine not exceeding $100].

[¶ 968] Disclosure Violations

Sec. 5.302. A person who knowingly and willfully violates the provisions on disclosure (Part 3) of the Article on Credit Sales (Article 2) or of the Article on Loans (Article 3) is guilty of a [misdemeanor] and upon conviction may be sentenced to pay a fine not exceeding $5000, or to imprisonment not exceeding one year, or both.

Article 6—Administration

PART 1—POWERS AND FUNCTIONS OF ADMINISTRATOR

[¶ 969] Short Title

Sec. 6.101. This Article shall be known and may be cited as Uniform Consumer Credit Code—Administration.

[¶ 970] Applicability

Sec. 6.102. This Part applies to persons who in this State

(1) make or solicit consumer credit sales, consumer leases, consumer loans, consumer related sales (Section 2.602) and consumer related loans (Section 3.602); or

(2) directly collect payments from or enforce rights against debtors arising from sales, leases, or loans specified in subsection (1), wherever they are made.

[¶ 971] Administrator

Sec. 6.103. "Administrator" means [ ].

COMMENT

In order to obtain the administration that is so vital to the effectiveness of the Uniform Consumer Credit Code, the National Conference recommends centralizing all powers of administration in a single official or agency. In recognition of the fact that in some States a single official or agency either is not constitutionally possible or may not be politically feasible, the Act does not attempt to identify the Administrator. The Administrator may be a single State official or department, two or more State officials or departments, or a Commission. For example in a State in which a single official (*e.g.*, Superintendent or Commissioner of Banks, Banking or Financial Institutions) or a single department (*e.g.*, Banking Department, Commerce Department or Department of Financial Institutions) presently supervises both banks and other financial institutions such as consumer finance companies and sales finance companies, it may be desirable to designate that official or department as the single Administrator. If two or more State officials or departments are to share the powers of the Administrator, the National Conference recommends that a Commission including those officials or departments be designated as Administrator, and that, unless a statutory division of areas of power and authority is provided for, the Commission be given power to prescribe the areas in which the officials or departments who are members of the Commission shall exercise the power and authority of the Administrator.

[¶ 972] Powers of Administrator; Harmony with Federal Regulations; Reliance on Rules; Duty to Report

Sec. 6.104. (1) In addition to other powers granted by this Act, the Administrator may within the limitations provided by law

(a) receive and act on complaints, take action designed to obtain voluntary compliance with this Act, or commence proceedings on his own initiative;

(b) counsel persons and groups on their rights and duties under this Act;

(c) establish programs for the education of consumers with respect to credit practices and problems;

(d) make studies appropriate to effectuate the purposes and policies of this Act and make the results available to the public; [and]

(e) adopt, amend, and repeal substantive rules when specifically authorized by this Act, and adopt, amend, and repeal procedural rules to carry out the provisions of this Act [;

(f) maintain offices within this State; and]

[(g) appoint any necessary attorneys, hearing examiners, clerks, and other employees and agents and fix their compensation, and authorize attorneys appointed under this section to appear for and represent the Administrator in court].

(2) To keep the Administrator's rules in harmony with the Federal Consumer Credit Protection Act and the regulations prescribed from time to time pursuant to that Act by the Board of Governors of the Federal Reserve System and with the rules of administrators in other jurisdictions which enact the Uniform Consumer Credit Code, the Administrator, so far as is consistent with the purposes, policies and provisions of this Act, shall

(a) before adopting, amending, and repealing rules, advise and consult with administrators in other jurisdictions which enact the Uniform Consumer Credit Code; and

(b) in adopting, amending, and repealing rules, take into consideration:

(i) the regulations so prescribed by the Board of Governors of the Federal Reserve System; and

(ii) the rules of administrators in other jurisdictions which enact the Uniform Consumer Credit Code.

(3) Except for refund of an excess charge, no liability is imposed under this Act for an act done or omitted in conformity with a rule of the Administrator notwithstanding that after the act or omission the rule may be amended or repealed or be determined by judicial or other authority to be invalid for any reason.

(4) The Administrator shall report [annually on or before January 1] to the [Governor and Legislature] on the operation of his office, on the use of consumer credit in the State, and on the problems of persons of small means obtaining credit from persons regularly engaged in extending sales or loan credit. For the purpose of making the report, the Administrator is authorized to conduct research and make appropriate studies. The report shall include a description of the examination and investigation procedures and policies of his office, a statement of policies followed in deciding whether to investigate or examine the offices of credit suppliers subject to this Act, a statement of the number and percentages of offices which are periodically investigated or examined, a statement of the types of consumer credit problems of both creditors and debtors which have come to his attention through his examinations and investigations and the disposition of them under existing law, a statement of the extent to which the rules of the Administrator pursuant to this Act are not in harmony with the regulations prescribed by the Board of Governors of the Federal Reserve System pursuant to the Federal Consumer Credit Protection Act or the rules of administrators in other jurisdictions which enact the Uniform Consumer Credit Code and the reasons for such variations, and a general

statement of the activities of his office and of others to promote the purposes of this Act. The report shall not identify the creditors against whom action is taken by the Administrator.

COMMENT

The direction to the Administrator in subsection (2) to keep his rules in harmony with the federal regulations issued pursuant to the CCPA and with the rules of administrators in other jurisdictions which enact the Uniform Consumer Credit Code is derived from the Uniform Narcotic Drug Act Section 1(14)(Alt.).

[¶ 973] Administrative Powers with Respect to Supervised Financial Organizations

Sec. 6.105. (1) With respect to supervised financial organizations, the powers of examination and investigation (Sections 3.506 and 6.106) and administrative enforcement (Section 6.108) shall be exercised by the official or agency to whose supervision the organization is subject. All other powers of the Administrator under this Act may be exercised by him with respect to a supervised financial organization.

(2) If the Administrator receives a complaint or other information concerning non-compliance with this Act by a supervised financial organization, he shall inform the official or agency having supervisory authority over the organization concerned. The Administrator may request information about supervised financial organizations from the officials or agencies supervising them.

(3) The Administrator and any official or agency of this State having supervisory authority over a supervised financial organization are authorized and directed to consult and assist one another in maintaining compliance with this Act. They may jointly pursue investigations, prosecute suits, and take other official action, as they deem appropriate, if either of them is otherwise empowered to take the action.

[¶ 974] Investigatory Powers

Sec. 6.106. (1) If the Administrator has probable cause to believe that a person has engaged in an act which is subject to action by the Administrator, he may make an investigation to determine whether the act has been committed, and, to the extent necessary for this purpose, may administer oaths or affirmations, and upon his own motion or upon request of any party may subpoena witnesses, compel their attendance, adduce evidence, and require the production of any matter which is relevant to the investigation, including the existence, description, nature, custody, condition, and location of any books, documents, or other tangible things and the identity and location of persons having knowledge of relevant facts, or any other matter reasonably calculated to lead to the discovery of admissible evidence.

(2) If the person's records are located outside this State, the person shall, at his option, either make them available to the Administrator at a convenient location within this State, or pay the reasonable and necessary expenses for the Administrator or his representative to examine them at the place where they are maintained. The Administrator may designate representatives, including comparable officials of the State in which the records are located, to inspect them on his behalf.

(3) Upon failure without lawful excuse to obey a subpoena or to give testimony and upon reasonable notice to all persons affected thereby, the Administrator may apply to [ ] court for an order compelling compliance.

(4) The Administrator shall not make public the name or identity of a person whose acts or conduct he investigates pursuant to this section or the facts disclosed in the investigation, but this subsection does not apply to disclosures in actions or enforcement proceedings pursuant to this Act.

COMMENT

Administrator under this section includes the official or agency referred to in Section 6.105(1).

A course of conduct is an act subject to action by the Administrator under subsection (1).

[¶ 975] Application of [Administrative Procedure Act] [Part on Administrative Procedure and Judicial Review]

Sec. 6.107. Except as otherwise provided, the [State administrative procedure act] [Part on Administrative Procedure and Judicial Review (Part 4) of this Article] applies to and governs all administrative action taken by the Administrator pursuant to this Article or the Part on Regulated and Supervised Loans (Part 5) of the Article on Loans (Article 3).

COMMENT

This section subjects actions of the Administrator to the State administrative procedure act, regarding, *inter alia*, adoption of rules, notice and hearing, contested cases, and judicial review. If the State does not have an adequate administrative procedure act providing equivalent procedural and judicial review protections, Part 4 of this Article should be enacted; otherwise, it may be omitted.

[¶ 976] Administrative Enforcement Orders

Sec. 6.108. (1) After notice and hearing the Administrator may order a creditor or a person acting in his behalf to cease and desist from engaging in violations of this Act. A respondent aggrieved by an order of the Administrator may obtain judicial review of the order and the Administrator may obtain an order of the court for enforcement of its order in the [ ] court. The proceeding for review or enforcement is initiated by filing a petition in the court. Copies of the petition shall be served upon all parties of record.

(2) Within 30 days after service of the petition for review upon the Administrator, or within any further time the court may allow, the Administrator shall transmit to the court the original or a certified copy of the entire record upon which the order is based, including any transcript of testimony, which need not be printed. By stipulation of all parties to the review proceeding, the record may be shortened. After hearing, the court may (a) reverse or modify the order if the findings of fact of the Administrator are clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record, (b) grant any temporary relief or restraining order it deems just, and (c) enter an order enforcing, modifying, and enforcing as modified, or setting aside in whole or in part the order of the Administrator, or remanding the case to the Administrator for further proceedings.

(3) An objection not urged at the hearing shall not be considered by the court unless the failure to urge the objection is excused for good cause shown.

A party may move the court to remand the case to the Administrator in the interest of justice for the purpose of adducing additional specified and material evidence and seeking findings thereon upon good cause shown for the failure to adduce this evidence before the Administrator.

(4) The jurisdiction of the court shall be exclusive and its final judgment or decree shall be subject to review by the [ ] court in the same manner and form and with the same effect as in appeals from a final judgment or decree in a [special proceeding]. The Administrator's copy of the testimony shall be available at reasonable times to all parties for examination without cost.

(5) A proceeding for review under this section must be initiated within 30 days after a copy of the order of the Administrator is received. If no proceeding is so initiated, the Administrator may obtain a decree of the [ ] court for enforcement of its order upon a showing that the order was issued in compliance with this section, that no proceeding for review was initiated within 30 days after copy of the order was received, and that the respondent is subject to the jurisdiction of the court.

(6) With respect to unconscionable agreements or fraudulent or unconscionable conduct by the respondent, the Administrator may not issue an order pursuant to this section but may bring a civil action for an injunction (Section 6.111).

COMMENT

If the respondent does not seek review of the Administrator's cease and desist order, this section makes that order final and allows the Administrator to obtain enforcement of it without having to support its findings with substantial evidence.

[¶ 977] Assurance of Discontinuance

Sec. 6.109. If it is claimed that a person has engaged in conduct subject to an order by the Administrator (Section 6.108) or by a court (Sections 6.110 through 6.112), the Administrator may accept an assurance in writing that the person will not engage in the conduct in the future. If a person giving an assurance of discontinuance fails to comply with its terms, the assurance is evidence that prior to the assurance he engaged in the conduct described in the assurance.

[¶ 978] Injunctions Against Violations of Act

Sec. 6.110. The Administrator may bring a civil action to restrain a person from violating this Act and for other appropriate relief.

[¶ 979] Injunctions Against Unconscionable Agreements and Fraudulent or Unconscionable Conduct

Sec. 6.111. (1) The Administrator may bring a civil action to restrain a creditor or a person acting in his behalf from engaging in a course of

(a) making or enforcing unconscionable terms or provisions of consumer credit sales, consumer leases, or consumer loans;

(b) fraudulent or unconscionable conduct in inducing debtors to enter into consumer credit sales, consumer leases, or consumer loans; or

(c) fraudulent or unconscionable conduct in the collection of debts arising from consumer credit sales, consumer leases, or consumer loans.

(2) In an action brought pursuant to this section the court may grant relief only if it finds

(a) that the respondent has made unconscionable agreements or has engaged or is likely to engage in a course of fraudulent or unconscionable conduct;

(b) that the agreements or conduct of the respondent has caused or is likely to cause injury to consumers; and

(c) that the respondent has been able to cause or will be able to cause the injury primarily because the transactions involved are credit transactions.

(3) In applying this section, consideration shall be given to each of the following factors, among others:

(a) belief by the creditor at the time consumer credit sales, consumer leases, or consumer loans are made that there was no reasonable probability of payment in full of the obligation by the debtor;

(b) in the case of consumer credit sales or consumer leases, knowledge by the seller or lessor at the time of the sale or lease of the inability of the buyer or lessee to receive substantial benefits from the property or services sold or leased;

(c) in the case of consumer credit sales or consumer leases, gross disparity between the price of the property or services sold or leased and the value of the property or services measured by the price at which similar property or services are readily obtainable in credit transactions by like buyers or lessees;

(d) the fact that the creditor contracted for or received separate charges for insurance with respect to consumer credit sales or consumer loans with the effect of making the sales or loans, considered as a whole, unconscionable; and

(e) the fact that the respondent has knowingly taken advantage of the inability of the debtor reasonably to protect his interests by reason of physical or mental infirmities, ignorance, illiteracy or inability to understand the language of the agreement, or similar factors.

(4) In an action brought pursuant to this section, a charge or practice expressly permitted by this Act is not in itself unconscionable.

COMMENT

One purpose of this section is to afford the Administrator a means of dealing with new patterns of fraudulent or unconscionable conduct unforeseen and, perhaps, unforeseeable at the writing of this Act. Another is to give him a more flexible remedy for halting reprehensible creditor practices that have been specifically and somewhat rigidly treated in previous consumer credit legislation. For instance, this Act has no specific prohibition against the creditor's allowing the debtor to sign a credit agreement containing blanks. In some situations there may be legitimate reasons for a contract to contain blanks at the time of signing. However, if the creditor deliberately leaves blanks to be filled in after the debtor's signature and without his consent, the Administrator may seek to restrain the practice as fraudulent or unconscionable conduct under this section.

[¶ 980] **Temporary Relief**

Sec. 6.112. With respect to an action brought to enjoin violations of the Act (Section 6.110) or unconscionable agreements or fraudulent or uncon-

sciensable conduct (Section 6.111), the Administrator may apply to the court for appropriate temporary relief against a respondent, pending final determination of proceedings. If the court finds after a hearing held upon notice to the respondent that there is reasonable cause to believe that the respondent is engaging in or is likely to engage in conduct sought to be restrained, it may grant any temporary relief or restraining order it deems appropriate.

[¶ 981] Civil Actions by Administrator

Sec. 6.113. (1) After demand, the Administrator may bring a civil action against a creditor for making or collecting charges in excess of those permitted by this Act. An action may relate to transactions with more than one debtor. If it is found that an excess charge has been made, the court shall order the respondent to refund to the debtor or debtors the amount of the excess charge. If a creditor has made an excess charge in deliberate violation of or in reckless disregard for this Act, or if a creditor has refused to refund an excess charge within a reasonable time after demand by the debtor or the Administrator, the court may also order the respondent to pay to the debtor or debtors a civil penalty in an amount determined by the court not in excess of the greater of either the amount of the credit service or loan finance charge or ten times the amount of the excess charge. Refunds and penalties to which the debtor is entitled pursuant to this subsection may be set off against the debtor's obligation. If a debtor brings an action against a creditor to recover an excess charge or civil penalty, an action by the Administrator to recover for the same excess charge or civil penalty shall be stayed while the debtor's action is pending and shall be dismissed if the debtor's action is dismissed with prejudice or results in a final judgment granting or denying the debtor's claim. With respect to excess charges arising from sales made pursuant to revolving charge accounts or from loans made pursuant to revolving loan accounts, no action pursuant to this subsection may be brought more than two years after the time the excess charge was made. With respect to excess charges arising from other consumer credit sales or consumer loans, no action pursuant to this subsection may be brought more than one year after the due date of the last scheduled payment of the agreement pursuant to which the charge was made. If the creditor establishes by a preponderance of evidence that a violation is unintentional or the result of a bona fide error, no liability to pay a penalty shall be imposed under this subsection.

(2) The Administrator may bring a civil action against a creditor or a person acting in his behalf to recover a civil penalty for willfully violating this Act, and if the court finds that the defendant has engaged in a course of repeated and willful violations of this Act, it may assess a civil penalty of no more than $5,000. No civil penalty pursuant to this subsection may be imposed for violations of this Act occurring more than two years before the action is brought or for making unconscionable agreements or engaging in a course of fraudulent or unconscionable conduct.

[¶ 982] Jury Trial

Sec. 6.114. In an action brought by the Administrator under this Act, he has no right to trial by jury.

[¶ 983] Debtors' Remedies Not Affected

Sec. 6.115. The grant of powers to the Administrator in this Article does not affect remedies available to debtors under this Act or under other principles of law or equity.

[¶ 984] [Venue]

[**Sec. 6.116.** The Administrator may bring actions or proceedings in a court in a county in which an act on which the action or proceeding is based occurred or in a county in which respondent resides or transacts business.]

COMMENT

This section is bracketed because it may be unnecessary in some States because of adequate venue rules in those states.

PART 2—NOTIFICATION AND FEES

[¶ 985] Applicability

Sec. 6.201. This Part applies to a person making in this State consumer credit sales, consumer leases, or consumer loans and to a person having an office or place of business in this State who takes assignments of and undertakes direct collection of payments from or enforcement of rights against debtors arising from these sales, leases, or loans.

[¶ 986] Notification

Sec. 6.202. (1) Persons subject to this Part shall file notification with the Administrator within 30 days after commencing business in this State, and, thereafter, on or before January 31 of each year. The notification shall state:

(a) name of the person;

(b) name in which business is transacted if different from (1);

(c) address of principal office, which may be outside this State;

(d) address of all offices or retail stores, if any, in this State at which consumer credit sales, consumer leases, or consumer loans are made, or in the case of a person taking assignments of obligations, the offices or places of business within this State at which business is transacted;

(e) if consumer credit sales, consumer leases, or consumer loans are made otherwise than at an office or retail store in this State, a brief description of the manner in which they are made;

(f) address of designated agent upon whom service of process may be made in this State (Section 1.203); and

(g) whether regulated or supervised loans or both are made.

(2) If information in a notification becomes inaccurate after filing, no further notification is required until the following January 31.

[¶ 987] **Fees**

Sec. 6.203. (1) A person required to file notification shall on or before January 31 of each year pay to the [Administrator] an annual fee of $10 for that year.

(2) Persons required to file notification who are sellers, lessors, or lenders shall pay an additional fee at the time and in the manner stated in subsection (1) of $10 for each $100,000, or part thereof, in excess of $100,000, of the original unpaid balances arising from consumer credit sales, consumer leases, and consumer loans made in this State within the preceding calendar year and held either by the seller, lessor, or lender for more than 30 days after the inception of the sale, lease, or loan giving rise to the obligations, or by an assignee who has not filed notification. A refinancing of a sale, lease, or loan resulting in an increase in the amount of an obligation is considered a new sale, lease, or loan to the extent of the amount of the increase.

(3) Persons required to file notification who are assignees shall pay an additional fee at the time and in the manner stated in subsection (1) of $10 for each $100,000, or part thereof, of the unpaid balances at the time of the assignment of obligations arising from consumer credit sales, consumer leases, and consumer loans made in this State taken by assignment during the preceding calendar year, but an assignee need not pay a fee with respect to an obligation on which the assignor or other person has already paid a fee.

PART 3—COUNCIL OF ADVISORS ON CONSUMER CREDIT

[¶ 988] **Council of Advisors on Consumer Credit**

Sec. 6.301. (1) There is hereby created the Council of Advisors on Consumer Credit consisting of [16] members, who shall be appointed by the Governor. One of the Advisors shall be designated by the Governor as Chairman. In appointing members of the Council, the Governor shall seek to achieve a fair representation from the various segments of the consumer credit industry and the public.

(2) The term of office of each member of the Council is [4] years. Of those members first appointed, [four] shall be appointed for a term of [1] year, [four] for a term of [2] years, [four] for a term of [3] years, and [four] for a term of [4] years. A member chosen to fill a vacancy arising otherwise than by expiration of term shall be appointed for the unexpired term of the member whom he is to succeed. A member of the Council is eligible for reappointment.

(3) Members of the Council shall serve without compensation but are entitled to reimbursement of expenses incurred in the performance of their duties.

[¶ 989] **Function of Council; Conflict of Interest**

Sec. 6.302. The Council shall advise and consult with the Administrator concerning the exercise of his powers under this Act and may make recommendations to him. Members of the Council may assist the Administrator in obtaining compliance with this Act. Since it is an objective of this Part to obtain competent representatives of creditors and the public to serve on the Council and to assist and cooperate with the Administrator in achieving the objectives of this Act, service on the Council shall not in itself constitute a conflict of interest regardless of the occupations or associations of the members.

[¶ 990] **Meetings**

Sec. 6.303. The Council and the Administrator shall meet together at a time and place designated by the Chairman at least twice each year. The Council may hold additional meetings when called by the Chairman.

[PART 4—ADMINISTRATIVE PROCEDURE AND JUDICIAL REVIEW]

[¶ 991] **[Applicability and Scope]**

[Sec. 6.401. This Part applies to the Administrator, prescribes the procedures to be observed by him in exercising his powers under this Act, and supplements the provisions of the Part on Powers and Functions of Administrator (Part 1) of this Article and of the Part on Regulated and Supervised Loans (Part 5) of the Article on Loans (Article 3).]

[¶ 992] **[Definitions in Part]**

[Sec. 6.402. In this Part (1) "Contested case" means a proceeding, including but not restricted to one pursuant to the provisions on administrative enforcement orders (subsection (1) of Section 6.108) and licensing, in which the legal rights, duties, or privileges of a party are required by law to be determined by the Administrator after an opportunity for hearing.

(2) "License" means a license authorizing a person to make supervised loans pursuant to the provisions on authority to make supervised loans (Section 3.502).

(3) "Licensing" includes the Administrator's process respecting the grant, denial, revocation, suspension, annulment, withdrawal, or amendment of a license.

(4) "Party" means the Administrator and each person named or admitted as a party, or who is aggrieved by action taken and seeks to be admitted as a party.

(5) "Rule" means each rule specifically authorized by this Act that applies generally and implements, interprets or prescribes law or policy, or each statement by the Administrator that applies generally and describes the Administrator's procedure or practice requirements or the organization of his office. The term includes the amendment or repeal of a prior rule but does not include

(a) statements concerning only the internal management of the Administrator's office and not affecting private rights or procedures available to the public;

(b) declaratory rulings issued pursuant to the provisions on declaratory rulings by Administrator (Section 6.409); or

(c) intra-office memoranda.]

COMMENT

These definitions are derived from Section 1 of the Uniform Law Commissioners' Revised Model State Administrative Procedure Act (hereinafter referred to as the "Revised Model Act").

[¶ 993] [Public Information; Adoption of Rules; Availability of Rules and Orders]

[Sec. 6.403. (1) In addition to other rule-making requirements imposed by law, the Administrator shall:

(a) adopt as a rule a description of the organization of his office, stating the general course and method of the operations of his office and the methods whereby the public may obtain information or make submissions or requests;

(b) adopt rules of practice setting forth the nature and requirements of all formal and informal procedures available, including a description of all forms and instructions used by the Administrator or his office;

(c) make available for public inspection all rules and all other written statements of policy or interpretations formulated, adopted, or used by the Administrator in the discharge of his functions:

(d) make available for public inspection all final orders, decisions, and opinions.

(2) No rule, order, or decision of the Administrator is valid or effective against any person or party, nor may it be invoked by the Administrator for any purpose, until it has been made available for public inspection as herein required. This provision is not applicable in favor of any person or party who has actual knowledge thereof.]

COMMENT

This Section is derived from Section 2 of the Revised Model Act.

[¶ 994] [Procedure for Adoption of Rules]

[Sec. 6.404. (1) Prior to the adoption, amendment, or repeal of any rule, the Administrator shall

(a) give at least 20 days' notice of his intended action. The notice shall include a statement of either the terms or substance of the intended action or a description of the subjects and issues involved, and the time when, the place where, and the manner in which interested persons may present their views thereon. The notice shall be mailed to all persons who have made timely request of the Administrator for advance notice of his rule-making proceedings and shall be published in [here insert the medium of publication appropriate for the adopting State],

(b) afford all interested persons reasonable opportunity to submit data, views, or arguments, orally or in writing. In case of substantive rules, opportunity for oral hearing must be granted if requested by 25 persons, by a governmental subdivision or agency, or by an association having not less than 25 members. The Administrator shall consider fully all written and oral submissions respecting the proposed rule. Upon adoption of a rule the Administrator, if requested to do so by an interested person either prior to adoption or within 30 days thereafter, shall issue a concise statement of the principal reasons for and against its adoption, incorporating therein his reasons for overruling the considerations urged against its adoption.

(2) No rule is valid unless adopted in substantial compliance with this section. A proceeding to contest any rule on the ground of non-compliance with the procedural requirements of this section must be commenced within 2 years from the effective date of the rule.]

COMMENT

This Section is derived from Section 3 of the Revised Model Act.

[¶ 995] [Filing and Taking Effect of Rules]

[Sec. 6.405. (1) The Administrator shall file in the office of the [Secretary of State] a certified copy of each rule adopted by him. The [Secretary of State] shall keep a permanent register of the rules open to public inspection.

(2) Each rule hereafter adopted is effective 20 days after filing, except that, if a later date is specified in the rule, the later date is the effective date.]

COMMENT

This Section is derived from Section 4 of the Revised Model Act.

[¶ 996] [Publication of Rules]

[Sec. 6.406. (1) The [Secretary of State] shall compile, index, and publish all effective rules adopted by the Administrator. Compilations shall be supplemented or revised as often as necessary.

(2) Compilations shall be made available upon request to [agencies and officials of this State] free of charge and to other persons at prices fixed by the [Secretary of State] to cover mailing and publication costs.]

COMMENT

This Section is derived from Section 5 of the Revised Model Act.

[¶ 997] [Petition for Adoption of Rules]

[Sec. 6.407. An interested person may petition the Administrator requesting the promulgation amendment, or repeal of a rule. The Administrator shall prescribe by rule the form for petitions and the procedure for their submission, consideration, and disposition. Within 30 days after submission of a petition, the Administrator either shall deny the petition in writing (stating his reasons for the denials) or shall initiate rule-making proceedings in accordance with the provisions on procedure for adoption of rules (Section 6.404).]

COMMENT

This Section is derived from Section 6 of the Revised Model Act.

[¶ 998] [Declaratory Judgment on Validity or Applicability of Rules]

[Sec. 6.408. The validity or applicability of a rule may be determined in an action for declaratory judgment in the [. . . court], if it is alleged

that the rule, or its threatened application, interferes with or impairs, or threatens to interfere with or impair, the legal rights or privileges of the plaintiff. The Administrator shall be made a party to the action. A declaratory judgment may be rendered whether or not the plaintiff has requested the Administrator to pass upon the validity or applicability of the rule in question.]

COMMENT

This Section is derived from Section 7 of the Revised Model Act.

[¶ 999] [Declaratory Rulings by Administrator]

[**Sec. 6.409.** The Administrator shall provide by rule for the filing and prompt disposition of petitions or declaratory rulings as to the applicability of any statutory provision or of any rule of the Administrator. Rulings disposing of petitions have the same status as decisions or orders in contested cases.]

COMMENT

This Section is derived from Section 8 of the Revised Model Act.

[¶ 1000] [Contested Cases; Notice; Hearing; Records]

[**Sec. 6.410.** (1) In a contested case, all parties shall be afforded an opportunity for hearing after reasonable notice.

(2) The notice shall include:

(a) a statement of the time, place, and nature of the hearing;

(b) a statement of the legal authority and jurisdiction under which the hearing is to be held;

(c) a reference to the particular provisions of the statutes and rules involved;

(d) a short and plain statement of the matters asserted. If the Administrator or other party is unable to state the matters in detail at the time the notice is served, the initial notice may be limited to a statement of the issues involved. Thereafter upon application a more definite and detailed statement shall be furnished.

(3) Opportunity shall be afforded all parties to respond and present evidence and argument on all issues involved.

(4) Unless precluded by law, informal disposition may be made of any contested case by stipulation, agreed settlement, consent order, or default.

(5) The record in a contested case shall include:

(a) all pleadings, motions, intermediate rulings;

(b) evidence received or considered;

(c) a statement of matters officially noticed;

(d) questions and offers of proof, objections, and rulings thereon;

(e) proposed findings and exceptions;

(f) any decision, opinion, or report by the officer presiding at the hearing;

(g) all staff memoranda or data submitted to the hearing officer or members of the office of the Administrator in connection with their consideration of the case.

(6) Oral proceedings or any part thereof shall be transcribed on request of any party [, but at his expense].

(7) Findings of fact shall be based exclusively on the evidence and on matters officially noticed.]

COMMENT

This Section is derived from Section 9 of the Revised Model Act.

[¶ 1001] [Rules of Evidence; Official Notice]

[**Sec. 6.411.** In contested cases:

(1) irrelevant, immaterial, or unduly repetitious evidence shall be excluded. The rules of evidence as applied in [non-jury] civil cases in the [. . . court of this State] shall be followed. When necessary to ascertain facts not reasonably susceptible of proof under those rules, evidence not admissible thereunder may be admitted (except where precluded by statute) if it is of a type commonly relied upon by reasonably prudent men in the conduct of their affairs. The Administrator shall give effect to the rules of privilege recognized by law. Objections to evidentiary offers may be made and shall be noted in the record. Subject to these requirements, when a hearing will be expedited and the interests of the parties will not be prejudiced substantially, any part of the evidence may be received in written form;

[(2) documentary evidence may be received in the form of copies or excerpts, if the original is not readily available. Upon request, parties shall be given an opportunity to compare the copy with the original;]

(3) a party may conduct cross-examinations required for a full and true disclosure of the facts;

(4) notice may be taken of judicially cognizable facts. In addition, notice may be taken of generally recognized technical or scientific facts within the Administrator's specialized knowledge. Parties shall be notified either before or during the hearing, or by reference in preliminary reports or otherwise, of the material noticed, including any staff memoranda or data, and they shall be afforded an opportunity to contest the material so noticed. The Administrator's experience, technical competence, and specialized knowledge may be utilized in the evaluation of the evidence.]

COMMENT

This Section is derived from Section 10 of the Revised Model Act.

[¶ 1002] [Decisions and Orders]

[**Sec. 6.412.** A final decision or order adverse to a party in a contested case shall be in writing or stated in the record. A final decision shall include findings of fact and conclusions of law, separately stated. Findings of fact, if set forth in statutory language, shall be accompanied by a concise and explicit statement of the underlying facts supporting the findings. If, in accordance with rules of the Administrator, a party submitted proposed findings of

fact, the decision shall include a ruling upon each proposed findings. Parties shall be notified either personally or by mail of any decision or order. Upon request a copy of the decision or order shall be delivered or mailed forthwith to each party and to his attorney of record.]

COMMENT

This Section is derived from Section 12 of the Revised Model Act.

[¶ 1003] [Licenses]

[Sec. 6.413. (1) When the grant or denial of a license is required to be preceded by notice and opportunity for hearing, the provisions of this Part concerning contested cases apply.

(2) No revocation, suspension, annulment, or withdrawal of a license is lawful unless, prior to the institution of proceedings by the Administrator, he gave notice by mail to the licensee of facts or conduct which warrant the intended action, and the licensee was given an opportunity to show compliance with all lawful requirements for the retention of the license.]

COMMENT

This Section is derived from Section 14 of the Revised Model Act.

[¶ 1004] [Judicial Review of Contested Cases]

[Sec. 6.414. (1) A person who has exhausted all administrative remedies available before the Administrator and who is aggrieved by a final decision in a contested case is entitled to judicial review under this Part. This section does not limit utilization of or the scope of judicial review available under other means of review, redress, relief, or trial de novo provided by law. A preliminary, procedural, or intermediate action or ruling of the Administrator is immediately reviewable if review of the final decision of the Administrator would not provide an adequate remedy.

(2) Proceedings for review are instituted by filing a petition in the [. . . court] within [30] days after [mailing notice of] the final decision of the Administrator or, if a rehearing is requested, within [30] days after the decision thereon. Copies of the petition shall be served upon the Administrator and all parties of record.

(3) The filing of the petition does not itself stay enforcement of the decision of the Administrator. The Administrator may grant, or the reviewing court may order, a stay upon appropriate terms.

(4) Within [30] days after the service of the petition, or within further time allowed by the court, the Administrator shall transmit to the reviewing court the original or a certified copy of the entire record of the proceeding under review. By stipulation of all parties to the review proceedings, the record may be shortened. A party unreasonably refusing to stipulate to limit the record may be taxed by the court for the additional costs. The court may require or permit subsequent corrections or additions to the record.

(5) If, before the date set for hearing, application is made to the court for leave to present additional evidence, and it is shown to the satisfaction of

the court that the additional evidence is material and that there were good reasons for failure to present it in the proceeding before the Administrator, the court may order that the additional evidence be taken before the Administrator upon conditions determined by the court. The Administrator may modify his findings and decision by reason of the additional evidence and shall file that evidence and any modifications, new findings, or decisions with the reviewing court.

(6) The review shall be conducted by the court without a jury and shall be confined to the record. In cases of alleged irregularities in procedure before the Administrator, not shown in the record, proof thereon may be taken in the court. The court, upon request, shall hear oral argument and receive written briefs.

(7) The court shall not substitute its judgment for that of the Administrator as to the weight of the evidence on questions of fact. The court may affirm the decision of the Administrator or remand the case for further proceedings. The court may reverse or modify the decision if substantial rights of the appellant have been prejudiced because the administrative findings, inferences, conclusions, or decisions are:

(a) in violation of constitutional or statutory provisions;

(b) in excess of the statutory authority of the Administrator;

(c) made upon unlawful procedure;

(d) affected by other error of law;

(e) clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record; or

(f) arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion.]

COMMENT

This Section is derived from Section 15 of the Revised Model Act.

[¶ 1005] [Appeals]

[**Sec. 6.415.** An aggrieved party may obtain a review of any final judgment of the [. . . court] under this Part by appeal to the [. . . court]. The appeal shall be taken as in other civil cases.]

Article 7.—Reserved for Future Use

Note: Provisions concerning consumer credit counseling agencies are being considered by the Special Committee and, if approved by the National Conference after 1968, will be proposed as Article 7 of the Uniform Consumer Credit Code.

Article 8.—Reserved for Future Use

Note: Provisions concerning wage earner receiverships are being considered by the Special Committee and, if approved by the National Conference after 1968, will be proposed as Article 8 of the Uniform Consumer Credit Code.

Article 9.—Effective Date and Repealer

[¶ 1006] Time of Taking Effect; Provisions for Transition

Sec. 9.101. (1) Except as otherwise provided in this section, this Act takes effect at 12:01 a. m. on [ ].

(2) To the extent appropriate to permit the Administrator to prepare for operation of this Act when it takes effect and to act on applications for licenses to make supervised loans under this Act (subsection (1) of Section 3.503), the Part on Regulated and Supervised Loans (Part 5) of the Article on Loans (Article 3) and the Article on Administration (Article 6) takes effect [ ].

Note: Insert in lieu of brackets at the end of subsection (2) either "immediately" or the earliest time possible under the constitutional or statutory requirements of the enacting State.

(3) Transactions entered into before this Act takes effect and the rights, duties, and interests flowing from them thereafter may be terminated, completed, consummated, or enforced as required or permitted by any statute, rule of law, or other law amended, repealed, or modified by this Act as though the repeal, amendment, or modification had not occurred, but this Act applies to

(a) refinancings, consolidations, and deferrals made after this Act takes effect of sales, leases, and loans whenever made;

(b) sales or loans made after this Act takes effect pursuant to revolving charge accounts (Section 2.108) and revolving loan accounts (Section 3.108) entered into, arranged, or contracted for before this Act takes effect; and

(c) all credit transactions made before this Act takes effect insofar as the article on remedies and penalties (Article 5) limits the remedies of creditors.

(4) With respect to revolving charge accounts (Section 2.108) and revolving loan accounts (Section 3.108) entered into, arranged, or contracted for before this Act takes effect, disclosure pursuant to the provisions on disclosure (Section 2.310 and Section 3.309), shall be made not later than 30 days after this Act takes effect.

COMMENT

The 30-day period in subsection (4) is derived from CCPA Section 127(c).

[¶ 1007] Continuation of Licensing

Sec. 9.102. All persons licensed or otherwise authorized under the provisions of [list statutes] on the effective date of this Act are licensed to make supervised loans under this Act pursuant to the Part on Regulated and Supervised Loans (Part 5) of the Article on Loans (Article 3), and all provisions of that Part apply to the persons so previously licensed or authorized. The Administrator may, but is not required to, deliver evidence of licensing to the persons so previously licensed or authorized.

COMMENT

This section provides automatic licensing under Article 3, Part 5, for all lenders previously licensed under the State's licensed lender statutes prior to the effective date.

No application or administrative action is required and the formal license under the prior statute, which will be repealed, will be a license under Part 5 of Article 3. The Administrator may, at such time as his new duties under the Code permit him an opportunity, substitute new licenses for those in the lenders' possession, but this is entirely a ministerial act.

[¶ 1008] Specific Repealer and Amendments

Sec. 9.103. (1) The following acts and parts of acts are repealed:

(a)

(b)

(c) [and so on]

(2) The following acts and parts of acts are amended:

(a)

(b)

(c) [and so on]

Note re Repealer and Amendatory Provisions

This Act is a comprehensive statute designed to regulate most aspects of consumer credit, maximum charges that may be made for consumer credit and rates of interest generally. Consumer credit covered includes sales credit related to the sale to consumers of goods or services, consumer loan credit, some credit related to the sale or financing of homes and some agricultural credit. All States have one or more acts regulating consumer credit and rates of interest and in many States additional provisions performing the same function appear in various other acts. To accommodate existing law to this Act, each State enacting this Act will need to repeal one or more existing acts or particular provisions in acts and may have to amend one or more other acts. The purpose of this Note is to suggest to the statutory revisor or other person preparing this Act for introduction into a particular State Legislature the acts which should be repealed or amended. To produce the uniformity which the Commissioners believe desirable, acts should be repealed or amended as recommended in this Note.

Acts to Be Totally or Substantially Repealed

Subject to other specific suggestions of this Note, certain existing acts devoted primarily to regulating consumer credit should be repealed in their entirety. The revisor or draftsman should insert in this section the appropriate statutes or provisions to be repealed. To help guide the search for these acts or provisions, a list of some of the common popular names of these acts follow, although there may be others in any particular jurisdiction:

Small loan acts, personal loan acts, consumer loan acts and acts licensing personal loan lenders, sales finance companies and consumer finance companies.

Instalment loan laws.

Retail instalment sales acts, motor vehicle instalment sales acts, all goods acts.

Revolving sales credit acts, revolving loan acts.

Truth-in-lending acts.

Home solicitation sales acts.

Home improvement sales and loan acts.

Insurance premium financing acts.

Acts Imposing Maximum Charges for Credit and General Usury Acts

Repeal of the above listed consumer credit regulatory acts will automatically repeal provisions in these acts imposing maximum charges for the types of credit dealt with in the acts. In addition, all general usury statutes and all other provisions in acts imposing maximum charges for loans, forbearance or the extension of credit should be repealed, excepting only provisions, if any, for maximum charges to be made by pawnbrokers.

Statutes providing for a "legal rate" of interest, that is, the rate to be applied for judgments, notes and other cases where

there is no agreed rate or no agreement is possible (as in a judgment) should not be repealed. If these statutes are so intertwined with maximum contract rates, *e.g.*, usury provisions, that it is difficult to separate the two types of provisions, total repeal of the usury and legal rate statute plus the addition of the following provision in this Act or elsewhere in the State statutes may be in order:

"If there is no agreement or provision of law for a different rate, the interest of money shall be at the rate of six percent per annum."

Provisions of Existing Statutes Affecting Powers of Organizations

In some States provisions relating to rates of interest are intertwined with provisions relating to powers of particular types of organizations, *e.g.*, small loan and sales finance companies, commercial banks and thrift institutions. In these cases provisions should be repealed, preserved or amended to comply with Section 1.108 of this Act. As indicated in Section 1.108, provisions relating to maximum charges should be repealed in all cases (subsection (1) of Section 1.108), provisions prescribing maximum amount or duration of any consumer credit sale or consumer loan should be repealed in statutes applicable to sellers, small loan companies consumer and sales finance companies, commercial banks and trust companies (subsection (2) of Section 1.108), and other provisions granting or limiting powers of organizations should be preserved (subsections (3) and (4) of Section 1.108).

Industrial Banks, Morris Plan Banks and the Like

As a result of evolutionary development industrial banks and Morris Plan banks made small loans at effective rates and in a manner similar to small loan companies but they also have power to receive deposits. In statutes providing for banks of this type, only those provisions prescribing maximum rates and regulations of the kind applied to small loan companies should be repealed. Provisions authorizing the organization of these banks and the receipt of deposits by them should be preserved.

THE IMPACT OF A CONSUMER CREDIT INTEREST LIMITATION LAW

WASHINGTON STATE: INITIATIVE 245

by

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CHAPTER I

INTRODUCTION

Purpose of the Study

This research was designed to determine the economic impacts of Initiative 245. The Initiative was passed by a vote of the people of the State of Washington in the general election of November 5, 1968. Its principal provision limited the interest rate (or "service charge") which could be assessed legally on various kinds of consumer credit to 12 per cent per year computed monthly at a rate of 1 per cent per month. It related to installment plans, revolving credit plans and credit cards whether these devices were used by retailers or financial institutions. The state has a basic usury law, limiting interest to 12 per cent annually, which had been amended earlier to permit a charge of 18 per cent per year (1 1/2 per cent per month) on retail credit contracts.[1] Bank credit cards were classified in an opinion by the Washington Attorney General as "retail contracts," making them eligible for the 18 per cent charge.[2] Initiative 245 reduced the maximum rate on retail credit from 18 to 12 per cent.

The Initiative did not affect the rates charged by small loan companies. They still may charge 3 per cent per month (36 per cent per year) on loans under $300, 1 1/2 per cent per month (18 per cent per year) on loans between $300 and $500, and 1 per cent per month (12 per cent per year) on loans over $500. Further, since state usury laws already limited banks to 12 per cent per year--except for credit cards which have a legal status similar to other forms of retail credit--the effect on banks was the removal of the retail credit exception to the usury laws.

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[1] R.C.W. 63.14.120.

[2] "Banks and Banking--Sale--Regulation of Bank Credit Card Transactions," Attorney General Opinion 1968, No. 6, State of Washington, Olympia, Washington, February, 1968.

Study Objectives

The study set out to determine:

1. What changes in credit policies, due to management decisions, have occurred as a result of the passage of the law.
2. What price changes, if any, are related to the new law.
3. What changes stemming from the new law have occurred in retail sales patterns (such as total retail sales and cash/credit sales relationships).
4. What effects on consumers can be inferred from the information obtained.

Procedure

There were five principal elements of the study. These were (1) a survey of the literature, (2) a field survey of retailers, banks and small-loan companies utilizing personal interviews, (3) a series of price-comparison studies in which identical items were priced in Seattle and Los Angeles to determine the extent of price movements during the second quarter of 1969 with the objective of relating price changes to the law, (4) a number of surveys of aggregative data sources as a check against questionnaire responses and intra-firm data of several kinds, and (5) certain special studies to see to what extent data on topics such as credit insurance, auto dealer pricing and gross margins, auto and appliance financing methods and sales contract registrations with county auditors could provide by way of evidence of the impact of the law.

Survey of the Literature. The literature was examined for both theoretical and empirical content.

Field Survey (personal interviews) of Retailers, Banks and Small Loan Companies. This was carried out during the third quarter of 1969. The questionnaires which were used are shown in the Appendix.

The business firms surveyed were as follows: (in some cases a complete census approach was used)

1. Census of banks.
2. Census of department stores.

3. Census of chain small loan institutions and a sample of smaller ones.
4. The largest furniture and appliance stores and a sample of smaller ones.
5. Sample of new auto dealers.
6. Sample of used auto dealers.

Responses to the questionnaires were obtained through personal interviews. The specific respondents selected, by institution, were:

1. Banks: Vice President (or other title designating chief officer) for consumer credit division
2. Department Stores: Credit Manager
3. Small Loan Companies: President or Manager
4. Large Furniture and Appliance Stores: Credit Manager
5. Small Furniture and Appliance Stores: Owner or Manager
6. Large Auto Dealers: Credit Manager
7. Small Auto Dealers: Owner or Manager

When data had been gathered from these questionnaires, they were tabulated and analyzed.

Pricing Studies of Credit Sensitive Items. Working from a list of brands (by specific model numbers) prices were recorded from price books and/or sales tags on refrigerators, washing machines, dryers, cooking ranges, and colored television sets in stores in Seattle and Los Angeles. The list was made up by the comparison shopping bureau of a large retailer. The list included descriptions, brand names, model numbers, pictures and additional identification materials. Items were "shopped" in conventional department stores, Sears Roebuck and J. C. Penney department stores, discount houses and appliance stores. This procedure, which was used in the first two price surveys (April 1969 and August 1969) was found to have the weakness that too few of specific model numbers appeared in both markets. Hence in the third price survey (January 1970) a new list of specific model numbers was prepared through field work in Seattle and which permitted the identification of 30 or more models of particular appliances in both Los Angeles and Seattle markets.

Survey of Aggregative Data Sources. To determine the extent to which published and unpublished data from secondary sources verified the survey results, data were collected, tabulated and analyzed. Relevant data were obtained from the following sources:

1. Federal Agencies. In addition to a variety of publications additional information was obtained through calls on the offices of the Federal Reserve Board and the Federal Deposit Insurance Corporation.
2. State Agencies. These included all of the agencies dealing with financial institutions, retailing institutions, insurance institutions, motor vehicles and general economic information. Existing publications of the agencies were supplemented with special tabulations available from computer storage but not yet published.
3. Relevant trade associations.

The kinds of data were quite varied and in addition to the verification purpose mentioned above, were used to determine changes in local economic conditions and, for purposes of comparison, the state economy with the national economy.

Special Studies. In addition to data from the State Insurance Commissioner and insurance trade associations, data were obtained from private insurance companies involved in credit insurance. We were thus provided with data on all of the credit insurance business done in the state for 1968 and 1969.

Since two large automobile dealers were willing to open their records, a detailed study of auto dealer sales contracts was made for the periods 1968 and 1969 to determine changes that had occurred in types of credit employed, credit criteria and the credit roles of the firms involved.

One large national manufacturer of automobiles provided complete records for the state necessary to determine dealer pricing and gross margin changes. It also provided similar information on the State of Oregon which does not have a credit limitation law.

A complete tabulation of installment sale registrations was made from the records of the King County (which includes Seattle) Auditor's records. The

periods covered were the twelve months prior to December 5, 1968 (before the law took effect) and the twelve months following. These data showed the types of financial institutions involved and the firms from which purchases were made This was followed by a re-survey of the institutions making the registrations to determine the extent to which management policies were responsible for observable trends.

Economic Environment of the Study

Ideally, for purposes of investigating the impacts of Initiative 245, the study would have been conducted in an environment in which all other economic factors would have remained somewhat equal. Unfortunately, this was not the case. Attempts to verify the statements of businessmen obtained in field interviews through analyzing external or aggregative data were made difficult by the changes in the economy other than the Initiative and its effects. The impacts which might have been expected from the change in the law were in the same direction as impacts which might be expected from the tightness and cost of money, economic recession in the area, and inflation. The first two (interest rates and recession) were strongly influenced by federal monetary policy, and the third--inflation--seemed beyond the reach of federal monetary policy during the period of the study. Hence, it is important at this point to describe the economic environment pertaining at the time of the research for this report.

There is ample evidence available on the behavior of the Washington state and the United States economies since January of 1968 to suggest that a number of highly adverse economic influences have prevailed. That is, from the point of view of the businesses in the state all costs of doing business have continued to spiral on the supply side and the growth of revenues has noticeably slackened in most sectors on the demand side.

The behavior of these elements in the economy is affected by many economic variables which add to the results from the reduction of business revenues with the imposition of a 12 per cent interest rate ceiling. Needless to say, it is difficult to sort out, quantify, and measure the pure effects of rate ceiling change when other economic factors introduce high degrees of variability.

It is the purpose of this section then to point out the behavior of several of the more indicative and influential macro-economic factors at work in the environment during the period in which this study analyzed the impacts from Initiative 245.

On the supply side the wholesale price index nationally for durables continued to climb. In January 1968 it was 103.0 for furniture and household durables and by January of 1969 it had risen to 105.3, up 2.3 points. As of June 1970, it was 108.6, up 5.6 from the beginning of the time period under study.

By the same token, the lowest possible cost of money to business (the prime rate) rose from 6.0 per cent in November 1967 to 7.0 per cent by January 1969, and to the high of 8.5 per cent on June 19, 1969. (See Table I-1.)

TABLE I-1

THE PRIME RATE

Date	Prime Rate
November 20, 1967	6.00%
April 19, 1968	6.50
September 25, 1968	6.00-6.25
November 13, 1968	6.25
December 18, 1968	6.75
January 7, 1969	7.00
March 17, 1969	7.50
June 19, 1969	8.50
March 25, 1970	8.00
September 25, 1970*	7.50

*Prediction as of September 23, 1970.

Source: Manufactures Hanover Trust Special Report, June 1970.

This represents an increase of at least 2.5 per cent in the cost to businesses of financing inventories, trade credit and consumer credit during the study period.

On the demand side the economic indicators are as equally bleak. Tables I-2, I-3 and I-4 clearly indicate a substantial decline in buying power both at the state and national level with above average increases in the unemployment rate occurring at the state level. While the unemployment rate increased through 1969 at the state level it remained quite stable through 1969 at the national level. When both 1968-1969 and 1969-1970 changes are compared for Washington state it is found that while the unemployment rate in 1969 was only 4.09 in January of 1968, it was 4.65 in 1969 and continued to rise to 5.29 in January of 1970.

There is evidence that unemployment rates might be worse if businessmen reacted more strongly to their problems. The Seattle-First National Bank Newsletter in mid-1970 stated:

> Everyone talks about higher costs (labor) and the squeeze on profits; inventories are being closely controlled and staff has been reduced here and there; quite a number of retail establishments have absorbed cost increases; the consumer is getting a break.[1]

Since the beginning of the study the state unemployment rate has always been higher and climbing at a faster rate than that of the national average. Hence, the impact on demand of goods and services could conceivably be quite large.

The Consumer Price Index (Tables I-5, I-6 and I-7) reflect the behavior of prices in the Seattle area when compared with the U.S. average. Traditionally, Seattle indices are higher than national averages. As demand slackens it is to be expected that the state and national indices will more nearly equate and that occurred in early 1970 (see Table I-5). Throughout the period of the study the Seattle consumer price index for all goods has declined relative to U.S. averages to reflect the depressed demand situation that faces state businesses.

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[1]Seattle-First National Bank, *Summary of Pacific Northwest Industries*, July, 1970, p. 4.

TABLE I-2

WAGE AND SALARY EMPLOYMENT
WASHINGTON AND UNITED STATES

Month	1968		1969			1970			
	Wash.	U.S.**	Wash.	Per Cent Change Over 1968	U.S.**	Per Cent Change Over 1968	Wash.	Per Cent Change Over 1969	U.S.**	Per Cent Change Over 1969
January	1086.5	66720	1113.8	+2.5	69199	+3.7	1138.7	+2.2	70992	+2.6
February	1088.6	67165	1114.4	+2.4	69487	+3.5	1131.8	+1.6	71135	+2.4
March	1089.9	67286	1123.6	+3.1	69710	+3.6	1114.3	-0.8	71256	+2.2
April	1086.8	67466	1125.2	+3.5	69992	+3.7	1108.0	-1.5	71163	+1.7
May	1092.0	67550	1128.5	+3.3	70172	+3.9	1097.4	-2.8	70852	+1.0
June	1094.6	67816	1128.8	+3.1	70347	+3.7	1086.8	-3.7	70598	+0.4
July	1102.7	67945	1126.2	+2.1	70400	+3.6	1082.3	-3.9	70455	+0.1
August	1108.6	68088	1123.9	+1.4	70497	+3.5	n.a.		n.a.	
September	1105.9	68195	1127.0	+1.9	70567	+3.5	n.a.		n.a.	
October	1109.7	68427	1129.0	+1.7	70836	+3.5	n.a.		n.a.	
November	1112.2	68664	1129.0	+1.5	70808	+3.1	n.a.		n.a.	
December	1116.1	68875	1128.8	+1.1	70842	+2.9	n.a.		n.a.	

*Thousands of persons

**Adjusted

Source: Washington: Washington State Employment Security Department. United States: *Economic Indicators*, Dates.

TABLE I-3

UNEMPLOYMENT*
WASHINGTON AND UNITED STATES

Month	1968		1969				1970			
	Wash.	U.S.	Wash.	Per Cent Change Over 1968	U.S.	Per Cent Change Over 1968	Wash.	Per Cent Change Over 1969	U.S.	Per Cent Change Over 1969
January	55.4	2795	64.7	+16.8	2645	-5.4	75.6	+16.8	3172	+19.9
February	55.2	2929	66.5	+20.5	2627	-10.3	80.6	+21.2	3427	+30.5
March	57.4	2881	62.0	+8.0	2728	-5.3	97.8	+57.7	3657	+34.1
April	59.4	2774	61.2	+3.0	2845	+2.6	98.2	+60.5	3948	+38.8
May	59.8	2810	62.7	+4.8	2809	+0.0	117.7	+87.7	4106	+46.2
June	61.4	2914	63.7	+3.7	2763	-5.2	119.3	+87.3	3900	+41.2
July	59.7	2897	65.1	+9.0	2858	-1.3	129.8	+99.4	n.a.	
August	58.8	2776	69.3	+17.9	2846	+2.5	n.a.		n.a.	
September	59.3	2847	72.4	+22.1	3131	+10.0	n.a.		n.a.	
October	59.4	2798	74.6	+25.6	3078	+10.0	n.a.		n.a.	
November	60.8	2654	77.8	+28.0	2851	+7.4	n.a.		n.a.	
December	59.0	2603	76.5	+29.7	2846	+9.3	n.a.		n.a.	

*Thousands of persons, seasonally adjusted.

Source: Washington: Washington State Employment Security Department. United States: *Economic Indicators*, Dates.

TABLE I-4

UNEMPLOYMENT RATE*
WASHINGTON AND UNITED STATES

	1968		1969				1970			
	Wash.	U.S.	Wash.	Change	U.S.	Change	Wash.	Change	U.S.	Change
January	4.09	3.5	4.65	+0.56	3.4	-0.1	5.29	+0.64	3.9	+0.5
February	4.06	3.8	4.77	+0.71	3.3	-0.5	5.64	+0.87	4.2	+0.9
March	4.21	3.7	4.43	+0.22	3.4	-0.3	6.86	+2.43	4.4	+1.0
April	4.35	3.5	4.35	+0.00	3.5	+0.0	6.95	+2.60	4.8	+1.3
May	4.38	3.6	4.47	+0.09	3.5	-0.1	8.36	+3.89	5.0	+1.5
June	4.46	3.7	4.55	+0.09	3.4	-0.3	8.53	+3.98	4.7	+1.3
July	4.36	3.7	4.66	+0.30	3.5	-0.2	9.19	+4.53	5.0	+1.5
August	4.29	3.5	4.93	+0.64	3.5	0.0	n.a.		5.1	+1.6
September	4.31	3.5	5.14	+0.83	3.8	+0.3	n.a.		n.a.	
October	4.31	3.5	5.29	+0.98	3.8	+0.3	n.a.		n.a.	
November	4.39	3.4	5.49	+1.10	3.5	+0.1	n.a.		n.a.	
December	4.26	3.3	5.39	+1.13	3.5	+0.2	n.a.		n.a.	

*Seasonally adjusted.

Source: Washington: State Employment Security Department. United States: Bureau of Labor Statistics.

TABLE I-5

CONSUMER PRICE INDEX--
WASHINGTON AND UNITED STATES

	1968		1969		1970	
	Seattle	U.S.	Seattle	U.S.	Seattle	U.S.
February	120.2	119.0	125.9	124.6	132.2	132.5
May	121.1	120.3	127.6	126.8	133.9	134.6
August	123.2	121.9	129.5	128.7	n.a.	n.a.
November	124.5	123.4	130.0	130.5	n.a.	n.a.

Source: U.S. Department of Labor, Bureau of Labor Statistics, The Consumer Price Index 1968, 1969, 1970.

TABLE I-6

CPI--HOUSEHOLD FURNISHINGS AND OPERATION*
SEATTLE AND UNITED STATES

	1968		1969		1970	
	Seattle	U.S.	Seattle	U.S.	Seattle	U.S.
February	109.4	111.2	112.7	115.8	116.3	120.8
May	110.9	112.5	113.3	117.4	117.4	122.5
August	110.5	113.3	113.2	118.5	n.a.	n.a.
November	112.0	114.8	114.5	119.6	n.a.	n.a.

*The household furnishings and operation category of the CPI includes the following items: Household furnishings (textiles, furniture and bedding, floor coverings, appliances, housekeeping supplies and services).

Source: U.S. Department of Labor, Bureau of Labor Statistics, The Consumer Price Index 1968, 1969, 1970.

TABLE I-7

CPI--PRIVATE TRANSPORTATION *
SEATTLE AND UNITED STATES

	1968		1969		1970	
	Seattle	U.S.	Seattle	U.S.	Seattle	U.S.
February	119.2	116.4	121.1	119.3	123.3	123.3
May	118.4	116.8	120.0	121.2	124.0	125.9
August	120.7	117.7	121.8	121.3	n.a.	n.a.
November	121.1	118.9	119.3	122.7	n.a.	n.a.

*The private transportation category of the C.P.I. includes new and used autos, gasoline, tires, oil, repairs, insurance, registration, parking fees.

Source: U.S. Department of Labor, Bureau of Labor Statistics, The Consumer Price Index 1968, 1969, 1970.

TABLE I-8

GENERAL ECONOMIC INDICATORS
WASHINGTON VS. UNITED STATES

		1968		1969		1968 vs. 1969 Per Cent Change		1970		1969 vs. 1970 Per Cent Change	
		Wash.	U.S.	Wash.	U.S.	Wash.	U.S.	Wash.	U.S.	Wash.	U.S.
Bank Loans	1st Qtr	2675	233570	3089	264970	+15.5	+13.4	3321	288230	+7.5	+8.8
(Millions $)	2nd Qtr	2759	244580	3179	283850	+15.2	+16.1	3314	293280	+4.2	+3.3
	3rd Qtr	2886	251920	3184	284300	+10.3	+12.9				
	4th Qtr	2972	265259	3222	295547	+8.4	+11.4				
Bank Debits	1st Qtr	58058.0	7218700	67446.3	8723500	+16.2	+20.8	69979.3	9842900	+3.8	+12.8
(Millions $)	2nd Qtr	57974.8	7948500	76666.7	9384800	+32.2	+18.1	69650.6	10143900	-9.2	+8.1
	3rd Qtr	62831.1	8368400	83657.8	9737200	+33.1	+16.4				
	4th Qtr	67118.1	8755800	73561.4	9560400	+ 9.6	+ 9.2				
Demand Deposits	1st Qtr	2091	168420	2139	180610	+ 2.3	+ 7.2	2209	189230	+3.3	+4.8
(Millions $)	2nd Qtr	2055	182807	2190	199426	+ 0.5	+ 9.1	2109	190110	-3.7	-4.7
	3rd Qtr	2111	179020	2137	188160	+ 1.2	+ 5.1				
	4th Qtr	2200	204911	2169	212760	- 1.4	+ 3.8				
Time Deposits	1st Qtr	2157	n.a.	2342	n.a.	+ 8.6		2340	n.a.	-0.1	
(Millions $)	2nd Qtr	2190	n.a.	2362	n.a.	+ 7.9		2439	n.a.	+3.3	
	3rd Qtr	2265	n.a.	2320	n.a.	+ 2.4					
	4th Qtr	2317	n.a.	2313	n.a.	- 0.2					
Personal	1st Qtr	968	55195	1062	59948	+ 9.7	+ 8.6	1120	64168	+5.5	+7.0
Income	2nd Qtr	1013	57236	1110	62263	+ 9.6	+ 8.8	1140	65000	+2.7	+4.4
(Millions $)									(est.)		(est.)
	3rd Qtr	1045	58455	1137	62290	+ 8.8	+ 6.6				
	4th Qtr	1058	59755	1136	64032	+ 7.4	+ 7.2				

TABLE I-8 (Continued)

		1968		1969				1970			
						1968 vs. 1969 Per Cent Change				1969 vs. 1970 Per Cent Change	
		Wash.	U.S.	Wash.	U.S.	Wash.	U.S.	Wash.	U.S.	Wash.	U.S.
Help Wanted	1st Qtr	208	194	218	231	+ 4.8		186	194	-14.7	
Index-Seattle	2nd Qtr	182	197	235	228	+29.1		186	175	-20.9	
vs. U.S.	3rd Qtr	207	218	204	235	- 1.4					
1957-59 = 100	4th Qtr	220	225	199	217	- 9.5					
Building Permit	1st Qtr	99.1		80.2		-19.1		68.2		-15.0	
Seattle-King	2nd Qtr	102.0		108.2		+ 6.1		64.5		-40.4	
County Only	3rd Qtr	99.4		78.6		-20.9					
(Millions $)	4th Qtr	98.6		79.7		-19.2					
Mortgages	1st Qtr	8698		7709		-11.4		4698		-39.1	
Recorded	2nd Qtr	10785		9013		-16.4		5127		-43.1	
King County	3rd Qtr	9688		7051		-27.2					
(by number)	4th Qtr	8864		6054		-31.7					
Deeds Recorded	1st Qtr	10601		12328		+16.3		10054		-18.4	
King County	2nd Qtr	11906		14613		+22.7		10526		-28.0	
(by number)	3rd Qtr	12771		13346		+ 4.5					
	4th Qtr	13950		11678		-16.3					

Source: Economic Research Department, Seattle First National Bank, Economic Indicators, Federal Reserve.

Table I-8, which lists a variety of indicators, further supports the decline in demand proposition and in a number of instances where the U.S. rates are up substantially the state rate is significantly declining. A case in point is demand deposits where in March of 1969 deposits had increased 2.3 per cent in Washington and 7.2 per cent for the U.S. In December of 1969 demand deposits had declined to 1.4 per cent below that of 1968 and the national figure remained 3.8 per cent above demand deposit levels in 1968.

A basic problem in utilizing financial data such as appear on Table I-8 is that some of the adjustments which have been made by businessmen have been in the form of what might be called "credit portfolio adjustments." That is, businessmen in many cases changed internally the relative proportions of various types of credit business (such as open book, installment credit, revolving credit, and credit card sales). Such changes may not be visible in general economic data. For example, the recorded figures for volumes of business done by banks and/or consumer finance companies might show little change in total, even though relatively drastic measures affecting consumers might have been taken by the financial institutions. Financial institutions have tightened up on credit-granting procedures, which has taken certain consumers out of the market for some intended purchases. At the same time, the efforts of retailers to decrease their credit costs might have shifted more credit business to the financial institutions, thus keeping up the volume of loans made by financial institutions. These counter-balancing actions on the part of the two groups of businessmen might result in a fairly stable aggregative figure for loans from financial institutions even though there may have been some serious effects on consumers who happened to be marginal credit risks. By the same token, an increase or a decline in aggregative volume would not necessarily warrant conclusions that any such changes resulted from Initiative 245, because:

1. The portfolio adjustments might be invisible,
2. The portfolio adjustments and other responses might have been in reaction to money supply or interest rate increases, or
3. The portfolio adjustments (which in the current period would tend to diminish volumes of loans by financial institutions)

might be counterbalanced by shifting of the credit burden from retailers to financial institutions or--to some extent--by the shifting of the credit burden from one financial institution to another (e.g., from banks to consumer finance companies).

Table I-8 points out many other such declines that are indicators of the behavior of the marketplace which directly or indirectly affect the ability of businessmen to perform in their economic environment. Further, the impacts of these economic changes are bound to be felt throughout the state economy.

In summary, the general economic environment has contributed many complexities and introduced a number of barriers to the drawing of firm conclusions from available external economic data concerning Initiative 245. Whereas, the nation moved into a recession during the period of the study, full-blown depression struck at the state of Washington. The anomaly of a depression at a time of inflation and high interest rates wiped out the neat condition of "all other things being equal" which economists like to see when studying specific issues.

Hypotheses

Based on the theoretical knowledge of the researchers, supplemented with a consideration for theoretical and empirical research into credit limitation laws, the following hypotheses were developed for the original study. As a result of the credit limitation law it was hypothesized that:

Prices of merchandise frequently sold on a credit basis have gone up.

Leasing of similar merchandise has increased.

Banks and merchants are doing less business on a credit basis.

Lenders are diverting business to the most profitable types of loans or credit arrangements.

Small-loan companies are doing more business.

Credit losses have decreased.

Different products and businesses have been affected in different ways by the new laws.

More poor people have been affected by the new law than middle or upper income people.

Marginal credit standing has been redefined to exclude some higher risks.

Some people have not been able to buy such products as used cars because of the law (sales have been adversely affected).

Financing charges other than interest rates have increased.

Businessmen have become more strict in the application of rules on delinquent accounts.

Organization of the Report

The balance of this report is divided into four chapters. Chapter II is a summary of the findings. Chapter III presents the relevant prior research. Chapter IV deals with the credit implications of the law and Chapter V covers the product related impact of the law. Following a brief concluding chapter, the Appendix includes a definition of terms and the questionnaires used in the field interviewing program.

CHAPTER II

SUMMARY OF FINDINGS

Scope of This Summary

This summary reports on findings from the survey of retailers, financial institutions and secondary sources of information.

The retail survey included the sixty-five retailers in the State which do the vast majority of business in credit-sensitive ("big-ticket") merchandise. The survey also covered all of the chain banking units in the state, banks in cities of 10,000 or more population, a sample of single-unit banks in smaller towns, all chain consumer finance companies and a sample of smaller firms, a sample of other financial institutions, a sample of auto dealers selling both new and used cars, and a sample of auto dealers selling only used cars. The managements of these institutions were interviewed as to the actions that they had taken in response to Initiative 245.

The implications for consumers are drawn from the changes businessmen made. The feasibility of surveying consumers was tested, but the results indicated that useful information could not be readily or easily obtained from this source. An opportunity existed to determine the accuracy of the consumer responses that were obtained and it was found that these responses were grossly undependable.

In addition to the survey of businessmen, the research involved the study of secondary sources of information in an attempt to verify or negate the kinds of conclusions which might be drawn from the survey. Data were gathered from federal, state and local governments, national finance and merchandise firms operating in the state, individual firms which volunteered to provide information, and previous studies. The government data of course covered all units (for example, all commercial banks, all savings institutions, all credit unions, all consumer finance companies and all retailers including auto dealers).

Based on the field interview results, the verification studies, and the analysis of the information available from all sources, certain conclusions

seem warranted. For purposes of exposition, the brief statements of this summary are organized under the following headings:

Availability of credit

Price of credit

Price of products and services

The conclusions take the form of series of statements concerning impacts and changes occurring after the passage of Initiative 245 followed by selections from the research data which support the statements.

Availability of Credit

Since Initiative 245 reduced the income retailing and financial institutions could achieve from credit charges, they could be expected to make up their loss of income by either reducing costs related to retail credit transactions or by developing new sources of income to compensate for the loss--or some combination of these actions. A prime potential for reducing a retailer's costs is to reduce risk through restricting his own credit granting, by switching consumers from more expensive (for the retailer) to less costly types of credit, and by sending consumers to some other source of credit. There is evidence of all three forms of risk and cost reduction and the net effect of these actions appears to have been a reduction in the availability of retail credit.

Consumers considered "marginal" or "slow pay" credit risks are increasingly being rejected when they apply for retail credit financing

Sixty-six per cent of the sample of retailers report that they now must reject applicants whom they would have accepted prior to Initiative 245.

Credit application rejection rates of retailers increased by an average of 9 per cent in 1969 as compared with 1968.

The increase in rejection rates for bank credit card applicants was 4.1 per cent for 1969, but the increase was much higher in the last half of the year, averaging 8.6 per cent and reaching 13 per cent in December.

Forty-two per cent of the auto dealers reported an increase of 14 per cent in the rejection rate (on both new and used cars) of credit applications in 1969 over 1968.

New customers for bank credit cards are given lower credit lines than those granted prior to Initiative 245.

Credit lines represent lower percentages of consumers' incomes. Acceptance criteria (such as length of time on the job, or in the city) have also been strengthened.

Many customers, who might have obtained "open book" (or free) credit prior to Initiative 245 now are unable to get such credit and must use revolving or instalment forms of credit instead.

Of 47 retailers offering open book credit prior to Initiative 245, 17 per cent have eliminated this form of credit.

An additional 13 per cent have cut 60- and 90-day open-book accounts to 30 days, after which maximum interest is ch ed.

Of the total 65 retailers, 43 per cent have encouraged consumers to switch from one type of credit to another. Over 50 per cent of furniture and appliance dealers have encouraged consumers to switch from using their credit to cash sales.

Consumers are often being asked by retailers to get outside financing for their purchases of durables.

Financing from outside sources become cash sales for retailers. The sources to which consumers are turning include credit unions, banks, and small loan companies.

Among auto dealers, 13 per cent report advising consumers to arrange their own financing. They reported an increase in the practice of "mousing" (consumers putting together multiple small loans either to make a downpayment or pay in full to the dealers).

Retailers in the sample show an average decrease of 3.8 per cent in the ratio of credit to total sales in 1969 as compared with 1968 (first quarter). Changes in the ratio of credit to total sales were reported by 26.2 per cent of the retail merchants in the sample. Of these 7.7 per cent reported an average increase in the ratio of 6.8 per cent, with a range of +1 to +20 per cent increase. However, 18.5 per cent reported an average decline of 13.4 per cent, with a range of -1 to -30 per cent decline.

Some marginal credit risk consumers, formerly able to get credit, now must forego making purchases of products that require loans.

These consumers have been taken out of the market because of an inability to borrow from any source on terms that would permit them to handle repayments out of future income.

The Price of Credit

Some of the ways in which retailers can reduce their risks or recover the credit income losses incurred with the passage of Initiative 245 can involve higher costs to consumers. The switch from open book to revolving credit can mean a consumer pays interest charges which he did not pay before. If a consumer must go to a small loan company, he will pay as high as 36 per cent annual interest, as opposed to the 12 per cent he would pay if he received retail or bank credit, or the 18 per cent he might have paid for revolving credit prior to Initiative 245. If a consumer must pay a higher downpayment, and/or if loan maturities are shortened, he may be forced to forego purchases he otherwise could afford. If fees other than interest charges are raised, and if consumers must pay charges (such as filing fees and insurance premiums) not required prior to Initiative 245, the finance-related costs to him may increase despite the attempt of the law to reduce interest charges.

Some low risk consumers are paying more for purchases made on credit.

By means of switching customers from open book to revolving credit plans retailers have passed on higher credit costs to low-risk customers who were previously being subsidized by cash customers and users of other credit plans (instalment and revolving).

Consumers now pay an increased minimum service fee on revolving accounts.

In some cases consumers are charged the minimum revolving credit fee of one dollar on a purchase if their balances are less than $50 and greater than $2.

In a number of cases, retailers and banks have instituted minimum service fees or increased existing fees since passage of Initiative 245. (The law allows a service charge of $10 as an alternative to computing the 1 per cent per month on balances.)

Some creditworthy consumers who bought on credit before and after the passage of the Initiative may have benefited from the law.

To the extent that price adjustments on merchandise usually bought on credit may not have been large enough to balance the consumers' savings in interest payments due to the reduction from 18 per cent to 12 per cent per year in the cost of credit, credit customers may have gained.

Price adjustments which were made were not necessarily made on the specific merchandise sold on credit. In fact, the majority of

respondents to the interview survey reported that they raised prices on all merchandise. By this means they could recover losses in credit income without raising prices just on those items frequently sold on a credit basis. This could provide creditworthy customers a net reduction in total cost (including interest costs) for goods bought on credit.

To the extent that retailers may have become more efficient in response to credit income losses, consumers in general may have benefited.

The reduction in gross profit margins due to the reduction in interest rates has also probably worked to the advantage of consumers by encouraging businessmen to strive for greater efficiency in their operations.

Businessmen have to some extent improved procedures and reduced waste in order to achieve cost reductions and thereby re-establish the gross profit margins in effect prior to the passage of the law.

Cash customers of stores selling credit items are in all likelihood paying somewhat higher prices but receiving no benefits.

The actions of retailers to raise prices, to institute new or higher charges for ancillary services, and to increase gross margins through adjustments in merchandise offerings will increase net costs to cash customers. Those persons who were on open book accounts prior to the passage of the law and who are still in the same category have been effected in essentially the same manner as have cash customers.

Consumers considered to be marginal credit risks may now pay more for money that they borrow.

Banks and merchants will no longer grant credit or, in effect, lend to them at the new lower rates, hence they may have to obtain funds from small loan companies (at rates up to 36 per cent) or from illegal lenders (at unlimited rates).

Retailers have moved to shorten maturities to reduce risks and the costs of selling sales contracts.

In selling paper, retailers have had their situation change from 2 per cent participation to 2 per cent discount per year on the average. They shorten maturities to lessen discount costs.

Among auto dealers, 18 per cent reported shortening maturities by an average of six months.

Consumers are having to pay higher downpayments on durable goods purchases.

Sixty per cent of auto dealers reported an average increase of downpayments on new cars of 11 per cent and 15 per cent for marginal credit risk buyers.

Sixty-nine per cent of the used car dealers surveyed increased downpayments an average of 21 per cent, but downpayments for marginal risk buyers were raised 31 per cent.

More consumers who make instalment contracts are being asked to purchase credit life and credit health and accident insurance.

There was an increase of 20 per cent in the number of retailers requiring credit insurance.

Retailers and banks not only reduce their risk with credit insurance, but they derive revenue from premiums amounting to 40 per cent of the premium as well.

Thirty-five per cent of the auto dealers state they have been "pushing credit insurance harder" since Initiative 245 became law.

Price of Products

The most direct means for retailers to recover the credit earnings lost due to Initiative 245 is to raise prices on the products usually bought on credit. If the market permits, this approach probably also is easiest of the various alternatives open to them. Another approach is to raise the prices on all merchandise in a store. The effective net price of the product to the consumer may also be raised by raising the price for ancillary services, or instituting charges for services which formerly were free. A third method of raising the net price to the consumer is to lower the discounts given for trade-ins in businesses where trade-ins are appropriate. Evidence of all of these approaches to increasing revenue were found in the study.

In one form or another consumers are paying higher prices for merchandise as a result of Initiative 245.

The majority (56 per cent) of retailers said that they raised prices on all merchandise on the average of 5 per cent in response to the passage of Initiative 245.

Sixty-four per cent of furniture and appliance dealers said that they raised prices on "credit-sensitive" items. Thirty-one per cent of department stores said that they did the same.

Several retailers stated that they were adjusting their merchandise offerings to obtain higher ave age mark-ups than existed prior to Initiative 245.

Forty-three per cent of auto dealers reported raising prices (net realized price) on new cars. Those that reported the magnitude had increases averaging 5.3 per cent.

Forty-one per cent of used car dealers reported raising prices. The average increase of those reporting the magnitude of increase was 11 per cent. Checking auction prices showed that wholesale prices of one-year old cars increased by 5 per cent in 1969 compared with 1968 in both Seattle and Denver. Six-year-old cars, however, are significantly lower priced in Seattle than in 1968--and are significantly lower than prices in Denver. This suggests that dealer margins increased percentage-wise on older used cars.

A special compilation of dealer margins covering 15 per cent of used cars sold in Washington in 1968 and 1969 (entire years) showed an increase of dealer gross margins of 13 per cent in 1969 over margins received in 1968.

Some retailers have instituted fees for services which were given to the consumers free of charge prior to Initiative 245.

The product-related fees for services formerly furnished free of charge have been assessed on check cashing, wrapping and packaging, lay-away, parking (in some cases parking fees were simply increased), delivery and product installation.

Tentative Conclusions

On the basis of the evidence that we have gathered, a number of conclusions appear warranted.

The low-income people who are marginal credit risks seem to have suffered the most so far from the enactment of Initiative 245. Since prices have been raised, customers who pay cash have suffered. At the time of the surveys (summer, 1969), the burden of supplying a service (credit), the cost of which may exceed the price that can be charged for it, seemed to have fallen on the merchants and possibly the banks. The merchants and banks had taken some steps to maximize their revenue, given the constraints under which they must work,

but they did not have a great deal of leeway. They also appeared to have made efforts to reduce their costs, but once again there appear to be significant limits to what can be done along these lines. The merchants and banks seem to be placing their main hope in raising the rate that they can charge. If this does not materialize, it seems to us that the banks and merchants will have to take what might be called drastic actions and these actions would, in all likelihood, have an adverse affect on a significant number of borrowers and cash buyers. We anticipate that these drastic steps would involve price rises, tighter restrictions and decisions not to do business on a credit basis for small sums (i.e., something less than $200, $300 or $500 per transaction or per year). Buyers in this category would be encouraged to borrow directly from personal finance companies, credit unions or other financial institutions. In fact, merchants might very well decide to get into the small-loan business, since it can be handled profitably.

It seems unlikely that merchants will be able to institute dramatic price increases in order to make up for the revenues lost as a result of the imposition of the 12 per cent rate ceiling. If they were to do this, they would put themselves at a disadvantage on readily comparable merchandise vis-a-vis those merchants who stress cash sales, which, of course, could be consumated at lower prices. Rather, it is likely that merchants will opt for a combination of moves including some price raises, adjustment of credit portfolios and merchandise assortments, tightening credit-granting criteria and raising charges or instituting new charges on ancillary services.

It seems to come down to this: the resolution of the banks and merchants' dilemma calls for drastic action on their part in the face of the very substantial decline in the interest rates (service charges) that they are allowed to charge their customers. Banks and merchants have taken many of the small steps that can be taken but their basic problem is still unresolved because its solution requires more than that. Some consumers (notably, the credit-worthy) may be benefiting as a result of the inertia that banks and merchants have displayed since Initiative 245 became law. One of two things has to happen. The rate ceiling will have to be raised or banks and merchants will have to reduce costs and/or increase revenues from other sources.

CHAPTER III

RELEVANT PRIOR RESEARCH

The General Importance of Interest Rates

Economists always have favored a free market for money or credit as well as for products and services. As Milton Friedman has said: (commenting on the writings of Jeremy Bentham in 1787 in which Bentham opposed interest limitation laws)

> I know of no economist of any standing from that time to this who has favored a legal limit on the rate of interest that borrowers could pay or lenders receive--though there must have been some. I know of no country that does not limit by law the rates of interest--and I doubt that there are any.[1]

This quotation highlights a problem that is basic to this study. Economists regard interest rates as a regulating mechanism in a free market economy and think they should be free to respond to market forces; government bodies, on the other hand (even those which strive for free market prices in general), tend to set legal limits on the price (interest rate) which may be paid or received on money or credit. These limits are set for political and generally non-economic reasons although justification of such acts are usually couched in economic terms.

The theoretical essence of the economic issue involved in legal limitations on interest is rather simple and straightforward. It is that regulating the price of one key component in a market economy inevitably causes dislocations in the system and results in misallocations of resources.

The importance of the role of interest rates in an economy can be seen in macro economics (i.e., economics of the total economy) where there is general agreement that interest rates affect not only the monetary system, but the rest

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[1]Milton Friedman, "On Defense of Usury," *Newsweek*, April 6, 1970, p. 79.

of the economy as well. The usual measure of the status of a total economy is the Gross National Product for the nation. On the expenditure side, it includes consumption (which usually accounts for nearly two-thirds of GNP), business investment (plant and equipment plus net change in inventories--called "Gross Private Domestic Investment"), government expenditures (federal, state and local) and net exports (exports minus imports). The first "general theory" to describe the total economic system was that of J. M. Keynes. Although arguments have raged concerning Keynesian economics, if certain additional factors (such as stocks of money and real assets and varying employment levels) are added to the Keynesian system, it is quite compatible with classical economics. In simplified form, Keynes related key factors in an economy as follows:

With the supply of money given:

> Money Supply is equal to the Demand for Money (Liquidity Preference) applied to the Interest Rate and Income. (Money Supply and Demand for Money in relation to each other determine the Interest Rate.)
>
> Consumption is a function of Income and the Interest Rate.
>
> Investment is a function of the Interest Rate and Consumption.
>
> Consumption plus Investment equals Income.

In practical terms, this means that consumption expenditures can be increased by decreases in the rate of interest or decreased by increases in the rate of interest that consumers must pay, all other things being equal. Since the total economy really revolves around consumption expenditures, and business investment is derived from consumption spending (i.e., businessmen raise or lower investment according to their perceptions as to whether the markets for their goods and services are going up or down), it is clear that interest rates can affect the total economy through inducing gains or declines in consumer buying activity. Likewise, in a free market, declines in expenditures induced through high interest rates tend toward reducing interest rates. The lower interest rates then induce higher expenditures. Thus, interest rates can play an adjustment, or equilibrating, role in the economy.

In practical terms, low interest rates also induce business investment. A businessman who has determined that there is an additional market for his products will evaluate the desirability of additional investment to handle this market. He will try to estimate the "marginal efficiency of capital," or the return on investment, and if there is a chance that the estimated return will be negated or seriously reduced by the cost of the money necessary for making the investment, the investment will not be made.

The Purpose of Interest Limitation Laws

Each law or regulation on interest strives to favor one side of, or one party to, a financial transaction. For example, the typical usury law is intended to benefit the borrower (or, in the case of consumer credit, the purchaser of goods and services). Since such a law usually takes the form of setting a fixed interest percentage rate, or fixed scale of rates, it necessarily disregards the overall supply of, and demand for, money or credit. Further, it disregards the cost of money to the lenders and the non-interest costs (such as higher prices and extra charges) to borrowers. A usury law in one state cannot control rates in other states and, even more important, it does not control prices of goods and services. Since money is mobile, it can move to other states at the expense of businesses and consumers in the state with the usury law in question. And since prices of goods and services are, in general, not controlled, they can be adjusted to make up for the costs or losses due to limitations on interest on credit--again at the expense of businesses and consumers in the state with particular laws.

As in the case of laws, limits on interest which are set by regulation have similar weaknesses. The current Federal Reserve regulation which limits the interest commercial banks can pay for deposits to 4½ per cent for small savers and 7 per cent for $100,000 depositors disregards supply, demand and costs (although the higher rate for large deposits presumably is based on economies of scale). Such limits may tend to favor banks by restraining competition for funds, but a bank which needs funds and can afford to pay depositors higher rates is unable to do so. In a market where potential bank depositors can earn much more through other forms of employment of their funds, the Federal Reserve regulations may impair the banks' supply of money. Further,

the interest limitation on savings is at the expense of the depositor, particularly the small saver who does not have feasible alternatives for earning a better return on his funds, and contributes to inflation by discouraging saving. One economist has commented on this problem as follows:

> Controls on rates payable by financial agencies ignores the welfare of savers who invest through these agencies. Such savers perform a vital function in the economy. Rate controls deny many low income savers the right to a competitive loanable funds market. High income savers can bypass the controlled market by investing in equities, etc., but if rate controls cause them to divert funds or to lose interest income, their contribution to economic product is reduced.[1]

The Effectiveness of Interest Limitation

But the most serious limitation of the powers of interest limitation laws or regulations is that none of them, nor all of them together, really can control the price of money or credit. Taken individually, they control only a portion of particular transactions: the portion which formally states an interest rate. But in any such transaction, the true price of money or credit can exceed the legal limit one way or another. For example, in a mortgage transaction, the lender can capture a higher rate than specified by government regulation by means of "discounting" the loan. In a commercial loan, the bank can insist on a "reserve" (or compensating balance) on a loan which effectively raises the rate on the money actually received by the borrower. On a consumer credit purchase, the seller can raise the price of goods or services, he can increase the charges for peripheral services and/or add new charges, he can reduce the allowance on trade-ins where trade-ins are accepted, he can change his assortments of goods to increase his average gross margin, and he can insist on life and/or disability insurance which raises the cost of credit to the consumer and increases the "credit" earnings of the seller. If the interest limitation causes the seller to refuse any longer to deal in credit, or to refuse credit to increased proportions of "marginal credit risks,"

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[1]Clifton B. Luttrell, "Interest Rate Controls--Perspective, Purpose and Problems," Review-Federal Reserve Bank of St. Louis, September, 1968, Reprint Series No. 32.

consumers may be sent by suggestion or necessity to a financial institution to negotiate a direct loan. Since some of these institutions, for example, can legally charge up to 36 per cent annual interest, the consumer protection motive of the interest limitation law is thwarted and the consumer may end up paying higher interest than he paid prior to the interest limitation law or regulation.

Paul A. Samuelson has pointed out that in setting ceilings too low on small loan interest rates, funds for the poor may even become unavailable or are supplied by loan sharks at very high interest rates:

> The concern for the consumer and for the less affluent is well taken. But often it has been expressed in a form that has done the consumer more harm than good. For fifty years the Russel Sage Foundation and others have demonstrated that setting too low ceilings on small loan interest rates will result in drying up legitimate funds to the poor who need it most and will send them into the hands of the illegal loan sharks. History is replete with cases where loan sharks have lobbied in legislatures for unrealistic minimum rates, knowing that such meaningless ceilings would permit them to charge much higher rates.[1]

Since questions might be raised concerning the setting of a relatively high rate ceiling as would be the case under the Uniform Consumer Credit Code, or allowing the market to set its own rate, it is significant that a study of actual rates charged by two large finance companies operating in several states suggested that the high ceiling would not necessarily cause rates all to move to that ceiling. Robert Johnson reported that:

> In states where the ceiling rates were $6 per $100 of unpaid balance per year, almost 18 per cent of the contracts were at the ceiling. In contrast, where the ceiling was $9 per $100 per year, less than 2/10ths of one per cent of the contracts were at the ceiling.[2]

Blitz and Long point out that historically there have been three objectives of usury legislation: " . . . protecting the small borrower

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[1]Paul A. Samuelson, statement in *Major Statements in Support of the Uniform Credit Code Filed with the Massachusetts Committee on the Judiciary, January 29, 1969* (Boston: National Conference of Commissioners on Uniform State Laws, Chicago, Illinois, 1969), p. 32.

[2]Robert W. Johnson, "Why Rate Ceilings in the U.C.C.C.?" *Industrial Banker*, March, 1969, p. 18.

. . . curbing the monopoly power of the creditor . . . and regulating the allocation of resources. . ."[1] They conclude that on the first issue ". . . it is not possible to determine a priori which group of borrowers will be the main beneficiaries. . ." On the second, they argue that usury legislation is "not particularly effective" in control of a credit monpolist "when the monopolist is free to discriminate in a nonhomogeneous market."[2] On the allocation of resources issue, they feel that capital markets are affected by interest regulation in a manner that is "mostly other than intended and frequently adverse." On the question of resource allocation they point out:

> A well-functioning capital market is likely to promote change, while a capital market encumbered by an enforced interest rate of zero is more in keeping with stagnation. In the latter system there is no interest-rate differential to attract capital to the more dynamic sectors of the economy. . . Recognizing that usury legislation may be aimed toward other goals, we would still point out that, in periods of rapid change, restraints on the price system, such as a ceiling interest rate, are likely to be a barrier to the efficient allocation of resources and to growth.[3]

The nature of the inefficiency is brought out by Clifton B. Luttrell in this quotation from an article in the *Review* of the Federal Reserve Bank of St. Louis:

> All ceilings which alter normal flows of funds retard economic growth. Low usury ceilings prohibit the higher rates necessary to offset the higher risks of business and individual innovators. Credit tends to be channeled into well-established, low-risk functions. Low ceilings on rates payable by financial agencies tend to restrict the flow of funds through usual credit channels. Loan funds supplies are thereby reduced, affecting borrowers adversely. . .[4]

Michael Kawaja, in an analytical essay on the economics of statutory ceilings on consumer credit, dealt with fixed rates (which set the exact rate

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[1]Rudolph C. Blitz and Millard F. Long, "The Economics of Usury Legislation," *Journal of Political Economy*, December, 1965, p. 609.

[2]*Ibid.*

[3]*Ibid.*, p. 619.

[4]Luttrell, *op. cit.*

to be charged) and ceilings (which are set as outer limits to rates). He suggested that the usual goals of usury legislation can be better achieved by less direct methods:

> The main findings of this analysis follow. First, there are no demands or cost-entry conditions inherent in the consumer industry that would justify rate fixing. Second, rate ceilings may serve worthwhile purposes in those segments of the credit market in which there are entry restrictions, but even in these cases they have serious drawbacks. Third, the disadvantages of ceilings on finance rates in competitive credit markets outweigh their advantages. And, fourth, the goal of rate ceilings in competitive credit markets is ill-defined and does not provide a basis for selecting the level of the rate ceiling or judging its efficacy. These conclusions point to the possibility and desirability of making the consumer credit industry more competitive and substituting the market mechanism for price ceilings. Therefore, all regulatory efforts should now be focused upon bringing about the conditions requisite to the development of effective competition in the industry.[1]

Thus, the general conclusions from the literature on effectiveness of interest limitation are that it has certain noble purposes, that these purposes are not achieved, and that undesirable effects may be incurred by individual consumers and by society in general.

The Effects of Interest Limitations on Buyers and Sellers

To some extent the effects of interest limitation laws on buyers and sellers can be anticipated on a priori grounds. For example R. W. Johnson has pointed out the differences between cash credit and vendor credit:

> If legislation is properly drawn, the cash lender has no place to conceal his finance charge and no source of additional income for his credit services. In contrast, the vendor offering both a time price and a cash price may juggle these prices any way he chooses.[2]

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[1]Michael Kawaja, "The Economics of Statutory Ceilings on Consumer Credit Charges," *Western Economic Journal*, March, 1967, p. 167.

[2]Robert W. Johnson, "Regulation of Finance Charges on Consumer Installment Credit," *The Michigan Law Review*, Vol. 66, No. 81 (November 1967), p. 98.

In a footnote to this comment, he explains some of the implications of this relationship as follows:

> This adjustment, however, is not made without cost either to the retailer or his customers. The demand for credit is derived from the demand for goods and services financed. Since the finance charge is a relatively small portion of the total time price and monthly payment, consumers are probably not as sensitive to changes in the price of credit as they are to changes in the cash price of goods or services financed. In economic terminology, the demand for credit is probably less elastic than is the demand for the good or service.
>
> Assume that without rate ceilings a retailer has achieved his optimum market strategy by allocation of the total time price between the cash price and finance charge. An imposition of rate ceilings forces him to redistribute a portion of the finance charge to the cash price. Because the demand for the good is more elastic than the demand for credit, this shift will reduce the number of cash sales by an amount greater than any resultant increase in credit sales. Thus, not only are total sales likely to be less, but also the credit sales gained are more costly to service than the cash sales lost. The resultant reduction in profits will force some marginal retailers out of the market.[1]

Although the majority of the authors in the field of credit limitations favor either a free market for interest rates or a ceiling much above the market rates, proponents of credit limitation such as William Warren, point out that this relative insensitivity to credit costs poses a hazard for the consumer:

> The danger of ceding to the dealer the choice of financing agency lies in the fact that a dealer, in exercising his choice, is likely to be more influenced by the size of the finance-charge rebate accruing to him than by the reasonableness of the charge which the buyer will have to pay.[2]

Maurice B. Goudzwaard, in an article on the impact of rate ceilings on the availability of credit, provides empirical evidence that in states having the highest small loan rates, credit loss rates are higher than in states with intermediate or low small loan rates. He concludes as follows:

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[1] *Ibid.*, pp. 98-99.

[2] William D. Warren, "Regulation of Finance Charges in Retail Installment Sales," *The Yale Law Journal*, Vol. 68, No. 5 (April, 1959), p. 846.

> Lenders appear more willing to accept higher credit losses and more marginal credit risks if their rate is sufficient to compensate for bad debt, investigation, and collection expenses. In effect, higher rate ceilings enlarge credit availability to poorer risks and allow lenders to adjust credit standards to accommodate rate ceilings. Since lenders have no control over price, low ceilings force them to reduce costs and restrict lending to the better risk classes, thereby discriminating against the less creditworthy and significantly reducing their credit opportunities. . . But the analysis does demonstrate that any rate ceiling will very likely affect consumer credit allocation and that price controls have important economic and credit rationing effects on credit availability at consumer finance companies.[1]

Since a knowledge of theory and a minimum of observation would suggest a hypothesis that the incidence of impact from credit limitation laws would vary between classes of consumer borrowers, it is logical to anticipate differences based on the relative creditworthiness of consumers. It would seem reasonable to expect that a credit rate limitation set below the charges in existence before a law took effect would have a marked effect on persons at the margin of acceptable creditworthiness. The effect on the marginal credit risk would, of course, be negative. At the same time, it might be reasonable to expect that the initial effects of such a law on the fully creditworthy consumer would be positive--that, until the full impact of the law struck home with businessmen, and they adjusted to it, the creditworthy person would benefit from a reduced interest cost.

There are of course many facets of the question over and above the mere interest rate which can create benefit or injury to all classes of consumers. F. Thomas Juster presented the argument that consumers are not "economic men" in their use of credit, which leads to the inference that less creditworthy consumers may use monthly payments as the principal criterion regardless of interest rates. If such consumers do look principally to the monthly payment amount, then it follows that they could incur an unreasonably high rate of interest. On the other hand, the people who could obtain the credit they want could afford to select sources of credit on the basis of interest rates. Juster concludes that:

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[1]Maurice B. Goudzwaard, "Price Ceilings and Credit Rationing," *Journal of Finance*, March, 1968, pp. 183-185.

> Thus the model predicts that the minimum available monthly payment is a highly relevant proxy for the "real" cost of credit in an economy where all consumers are rationed [able to borrow less than they would prefer] in the sense just described. But in an economy where all consumers are unrationed [actual and preferred borrowings equal], monthly payments are irrelevant and finance rate is the relevant price. Thus the marginal borrowing cost model predicts that consumer response to finance rates will depend on the relative importance of unrationed consumers in the population.[1]

Although questions have been raised concerning the nature of Professor Juster's research, the concept of differing attitudes toward interest by different classes ("rationed" and "unrationed") of consumers is important because of its implications which are outlined in the following quotation:

> These results suggest the necessity for qualification of the widely held view that consumers are unresponsive to changes in the finance rates on installment credit contracts. Most consumers are in fact unresponsive, but only because they are constrained to accept shorter contract maturities than they would prefer. . . consumers appear to be unresponsive to finance rates because they do not have access to anything like a perfectly competitive capital market. The closer capital markets come to this analytical ideal, the more sensitive will consumers be to the cost of funds.[2]

On the business side, Paul Douglas points out that the apparent behavior of finance company lenders is such that raising and lowering finance rates may not bring about increases or declines in their profit:

> Higher or lower rate ceilings do not raise or lower finance company profits but rather, determine credit availability. The higher the ceiling, the more marginal risk borrowers can be accommodated. This is confirmed by data showing a high positive correlation between the rate ceiling and bad debt charge-offs. The higher the ceiling, the riskier the loans and the higher the incidence of bad debts.[3]

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[1]F. Thomas Juster, "Consumer Sensitivity to the Price of Credit," *Journal of Finance*, May, 1964, p. 227.

[2]*Ibid.*, p. 233.

[3]Paul H. Douglas, statement in *Major Statements in Support of the Uniform Consumer Credit Code Filed with the Massachusetts Committee on the Judiciary January 29, 1969* (Boston: National Conference of Commissioners on Uniform State Laws, Chicago, Illinois, 1969), p. 11. Douglas footnotes this comment

The real question to any business is the relationship between costs, revenues and volumes, so that for consumer credit institutions costs of money must be related to allowable interest rates. If the ceilings are relatively low, or the costs of money relatively high, consumer finance companies and others can adjust their profits by changing credit granting criteria. Profits could literally be increased as long as there is a margin between costs and revenues by making credit less available to people most likely to cause losses. Thus it is possible for finance companies to increase profits in the face of low interest rate ceilings and tight money.

Several other empirical studies have concluded that credit rate limitations create real problems for grantors of consumer credit and that these problems are passed along to the consumers.

Jan Robert Williams who studied the Arkansas situation found that the Arkansas constitutional 10 per cent limitation on credit charges has caused serious problems for both businessmen and consumers. From an examination of cost-revenue relationships of retailers, Williams concluded:

> Credit costs are greater than credit revenues generated by maximum legal service charges. This condition has a profound influence on the general store operations of retailers and the customers purchasing merchandise both on credit and for cash.[1]

Williams reports that retailers limited their credit business, even though they saw credit as a device to increase sales. One form of limiting credit business was to set rigid standards for credit granting which made it impossible for many marginal credit applicants to obtain credit. In this regard, he points out that:

> These would-be purchasers either are unable to purchase or they must seek borrowed funds under conditions which may allow lenders to take advantage of the borrower's situation.[2]

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with a reference to Robert P. Shay, "State Regulation and the Provision of Small Loans," in John M. Chapman and Robert P. Shay (eds.), *Consumer Finance Industry* (New York: Columbia University Press, 1967), p. 100.

[1]Jan Robert Williams, *An Analysis of Retail Credit Costs of Selected Retail Stores in Arkansas* (Unpublished Doctoral Dissertation, University of Arkansas, 1970), p. 125.

[2]*Ibid.*, p. 126.

The merchants were hurt by having to "receive undesirable terms in the financing of installment accounts with banks and other financial institutions. These terms included high rates of discount, large compensating balances, and full recourse arrangements."[1]

One of the worst effects of the Arkansas rate limitation was the "credit subsidy," described by Williams as follows:

> The credit subsidy is perhaps the greatest inequity caused by the 10 per cent limit on service charges in the State. Simply stated, the cash price of goods must be increased in order to cover losses on credit operations which result when credit costs exceed credit revenues. . . The credit subsidy, which is equal to the increase in the cash price to cover credit losses, is paid by the cash buyer and received by the credit customer.[2]

Williams also concludes that the credit limitation law had restrained economic development in the state, particularly in border areas. Firms were discouraged from entering business in Arkansas and the law also "hurt the further expansion of stores already located in Arkansas."

Gene C. Lynch also studied the Arkansas case and had similar conclusions relative to the retailers' costs of credit. He also discussed the problems of financial institutions and provided evidence that credit availability was restricted in Arkansas. In addition, he did a survey of prices on major appliances in Little Rock, Arkansas, and cities in states in the "Arkansas Region" (including Texarkana, Texas, Monroe, Louisiana, Greenville, Mississippi, Memphis, Springfield, Missouri, Tulsa and Denver). He found that if Little Rock were given an index of $100, the indexes of the other cities ranged from about $93 to $97.[3] Lynch suggests that these and other price data show the retailers' response to credit rate limitation:

> The only factor that can logically account for the higher cash prices in Arkansas is the ten per cent usury limitation. The cause of higher prices is not higher absolute costs, but

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[1] *Ibid.*

[2] Williams, *op. cit.*, pp. 126-127.

[3] Gene C. Lynch, *Consumer Credit at Ten Per Cent Simple: The Arkansas Case* (Fayetteville, Arkansas: College of Business, University of Arkansas, 1969), p. 16.

> lower revenues from credit sales. The legal finance charge differential between Arkansas and surrounding states is too great not to have an effect on store pricing policies.[1]

In the Lynch study, prices were found to be higher in the state (Arkansas) with the lowest limit on credit charges in the region, although questions might be raised as to whether a causal relationship between the interest rate limitation and product prices had been established.

A number of studies have been made of the credit cost-revenue relationships for retailers and financial institutions. The basic conclusion is that consumer credit is not a very profitable business even in the absence of low rate ceilings on credit charges. The Federal Reserve Bank studies show that there are economies of scale in loans and that breakeven loan sizes decrease with the length of maturity and increase as interest rates decline. It is rather obvious that as the cost of money rises the break-even size of loans increases considerably at any given rate of interest charged. When this situation is capped by a credit limitation law at a relatively low figure (12 per cent per year) as is true in Washington there is a cost-price squeeze on the credit-granting institutions.

The best-known study of retail credit costs and revenues is that sponsored by the National Retail Merchants Association, a department store trade group. In 1963 and again in 1968, the accounting firm of Touche, Ross, Bailey and Smart gathered credit operating data from department stores, and in the 1968 study an economic analysis of the data was provided by Robert W. Johnson.[2] The study showed that the stores lost money on all three forms of credit (30-day charge account, revolving credit and installment accounts). Conclusions included:

> Study findings indicate that providing credit in the department store field was a costly undertaking. . . It is clear, therefore, that credit must be justified economically by the department store

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[1] *Ibid.*, p. 26.

[2] Robert W. Johnson, "Economic Analysis of Credit Revenues and Costs in Department Stores," in Touche, Ross, Bailey and Smart, *Economic Characteristics of Department Store Credit* (New York: National Retail Merchants Association, 1969).

> as a selling tool--not as a separate business venture. . . The small stores had greater deficiencies of revenue over costs.[1]

An unpublished study by Touche, Ross, Bailey and Smart on costs in stores in the state of Washington for the fiscal year ending January 31, 1966 also found that there were losses in all forms of credit.[2]

The importance of credit to furniture and home appliance retailers was stressed in an empirical study which included the city of Spokane, Washington. The study, which covered Boise, Idaho as well, was published in 1963 and reported the following:

> All of the furniture and appliance retailers in the two cities granted credit to their customers. All of the retailers sold merchandise under conditional sales contracts. All but two retailers gave credit on open account. In approximately one-third of the establishments the credit business was a major enterprise both from the volume of credit and the income from the credit business, which was treated as a separate department in a few instances. An analysis of opinions expressed by retailers indicates that essentially all of the retailers realize that credit operations are very important to their overall operations and may be important even as a separate enterprise.[3]

The study was made at a time when the most common rates charged by the banks for short-term borrowings by retailers was 6 per cent and the range was from 5 to 8 per cent per annum. On paper carried by financial institutions, the rates charged by banks averaged 14.5 per cent and that carried by consumer finance companies averaged 22.3 per cent. Bank rates ranged from 8 to 23 per cent and finance company rates ranged from 11 to 40 per cent and "there were isolated cases beyond these limits."[4] If the average bank rate of 14.5 per cent, or 8½ per cent above the "most common" short-term rate to retailers, was

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[1] *Ibid.*, pp. 50-51.

[2] Touche, Ross, Bailey and Smart, "Study of Consumer Credit Costs in Retail Stores in Washington (Unpublished report to Washington Retail Council, 1966).

[3] Norman Nyhroten, Ralph H. Farmer, Russel L. Chrysler and Paul O. Groke, *Credit Practices of Retailers and Financers of Furniture and Home Appliances in Two Northwest Cities* (Moscow, Idaho: University of Idaho, May, 1963), p. 75.

[4] *Ibid.*, p. 82.

based on reasonable net earnings for the banks, then reasonable net earnings for banks in 1970 would require an average rate of at least 18 per cent or more. Hence, it is logical to assume that the rate ceiling of 12 per cent per year imposed by Initiative 245 provides additional evidence that it is unlikely that credit grantors in general can provide consumer credit without incurring operating losses.

Summary

In summarizing the concepts from extant literature, it should be kept in mind that the issue of rate ceilings, or any particular form of ceiling, is controversial. It seems to the researchers in this study, however, that the weight of opinion favors certain key concepts:

1. The objectives of credit rate limitation by law or regulation usually are to protect the small borrower (assumed to lack power and/or knowledge to handle his own financial affairs), to limit the monopoly power of creditors and lenders (assumed to have a bargaining advantage in dealing with borrowers), and to foster a more rational and equitable allocation of resources than would occur without regulation. The majority opinion seems to be that legal rate limitations fail in all three objectives.
2. Economists generally see the interest rate as an equilibrating mechanism which should function in a manner resembling the free markets preferred for goods and services. They consider restrictions on the free money market as a source of maladjustment and misallocation of economic resources.
3. Rate restrictions tend toward restrictions on the availability of credit, particularly for small, less creditworthy borrowers and also tend to lead to increases in rates for small borrowers when their only alternatives are consumer finance companies (with higher legal rates) or illegal lenders (who can charge what the traffic will bear).
4. Low rate ceilings cause creditors and lenders to try to make up for loss of interest income through other means. For example,

the retailer who is faced with rates too low to cover his costs (or with a decline in interest income whatever his cost) tends to recoup his losses by raising prices on merchandise, raising charges on ancillary services, or by shifting the consumer to outside sources of credit.

5. Where interest ceilings are to be used, economists favor setting the ceilings distinctly higher than ordinary market rates of interest, so that a relatively free market can operate without reaching the ceilings.

Empirically, it has been shown that retailers probably lose money (in terms of cost/revenue relationships) on all forms of credit, even where the rate charged is higher than 12 per cent per year. It is evident, moreover, that financial institutions suffer from a cost-price squeeze, particularly in this period of high interest rates and tight money. The break-even size of loans for banks is much above the amount needed for purchases of virtually any durables except housing and automobiles.

The cash customer may be forced to provide a subsidy for credit customers through paying higher prices on goods and services.

Creditworthy consumers who bought on credit before and after the passage of the Initiative may have benefited through a net reduction in interest costs. The benefits could derive from the possibility that the stores from which they made purchases may not have adjusted completely to the Initiative, or from the possibility that the stores may have been trying to recover credit income losses through a combination of reducing costs (including credit granting costs) or by raising prices on all items, or on items not ordinarily bought on credit. The raising of prices on all items, or on items not ordinarily bought on credit, would tend to subsidize the credit customers at the expense of cash customers by giving them a net reduction in total cost (including interest) on goods purchased.

CHAPTER IV

CREDIT RELATED EFFECTS

Credit Related Hypotheses

The credit related hypotheses established at the outset of this study were as follows:

Banks and merchants are doing less business on a credit basis.

Lenders are diverting business to the most profitable types of loans or credit arrangements.

Small loan companies are doing more business.

Credit losses have decreased.

More poor people have been affected by the new law than middle- or upper-income people and marginal standing from a credit standpoint has been redefined to exclude some individuals classified as higher risks.

Financing charges other than interest rates have increased.

Businessmen have become more strict in the application of rules on delinquent accounts.

The passage of Initiative 245 resulted in a number of changes in the manner in which a large number of firms do business on a credit basis with their customers. These effects were felt primarily in three major areas:

1. The volume of sales done on a credit basis by retailers and financial institutions.

2. The charges imposed by retailers and financial institutions as well as the costs of providing credit services for customers.

3. The credit-related effects of the new law on consumers generally.

Each of these three major headings will be discussed in this chapter.

The Volume of Business

The 12 per cent interest ceiling which became effective with the enactment of Initiative 245 does not apply to direct consumer loans obtained from consumer finance, or "small loan" companies, as they are sometimes called. Automobile finance companies such as GMAC are restricted to the 12 per cent interest limit. The latter organization and its counterparts in the auto and appliance fields are also sometimes called "captive" or sales finance companies.

The volume of business that banks and consumer finance companies are doing in indirect loans to consumers that originate with retail merchants has, as might be expected, declined. Sixteen out of 23 retailers made changes tending to diminish indirect loans and Table 4 shows an overall decline in indirect loans. This decline is attributable primarily to a falling off in the volume of business done between financial institutions and furniture and home appliance retailers. A sample representing a substantial proportion of the total indirect dealer paper purchased by the state and national banks in Washington revealed a 41 per cent decline in the number of appliance and home furnishings contracts purchased in 1969 when compared to 1968. The total dollar volume decline amounted to 33 per cent. Indirect dealer paper in automobiles declined 10 per cent in the number of contracts and 5 per cent in dollar volume. Indirect marine (boat and motor) paper declined 6 per cent in number of contracts, but increased 25 per cent in dollar volume. In all three categories, the number of contracts declined by 15.5 per cent and the dollar volume by 5.8 per cent and the average size of contract increased. That these events can probably be attributed to Initiative 245 also seems to be indicated by the fact that the experience of the banks and finance companies in Washington State apparently runs counter to the experience of similar institutions in the rest of the country. The extent of this divergence is shown below in Tables 1, 2 and 3. A survey representing approximately 60 per cent of bank consumer loans in the State of Washington in 1968 and 1969 is summarized in Tables 4 and 5.

There was also a decline of 15 per cent in filings of retail installment contracts in King county in 1969 compared to 1968. Table 6 shows in the last six months of 1969 an even sharper 25 per cent decline in filings by retailers and 33 per cent by banks. Small loan companies, however, showed a decline of only 12 per cent, which was less than the total or average decline. This

TABLE IV-1

COMMERCIAL BANKS, CONSUMER FINANCE AND SALES FINANCE COMPANIES

INDIRECT LOANS -- 1968 and 1969
(millions of dollars)

	EXTENDED			OUTSTANDING (Dec. 31)		
	1968	1969	% Change	1968	1969	% Change
Washington	$203.9[a]	$192.3[a]	-5.7	$172.4	$182.0	+5.6
United States	$13,313*	$14,272*	+7.2	$39,907	$42,567	+6.7

[a]Does not include consumer finance company data for state.

*Includes all finance companies.
(Commercial banks are omitted--data unavailable)

Sources: Washington: Division of Banking, Sales Finance Companies, Commercial banks. United States: Federal Reserve

TABLE IV-2

ALL FINANCE COMPANIES

INDIRECT LOANS -- 1968 and 1969
(millions of dollars)

	EXTENDED			OUTSTANDING (Dec. 31)		
	1968	1969	% Change	1968	1969	% Change
Washington	n.a.	n.a.		$34.9	$35.6	+2.0
United States	$13,313	$14,272	+7.2	$15,794	$17,030	+7.8

Sources: Washington: Sales Finance Companies, Supervisor of Banking Report (Consumer Finance Companies). United States: Federal Reserve.

TABLE IV-3

SALES FINANCE COMPANIES

INDIRECT LOANS -- 1968 and 1969
(millions of dollars)

	1968	1969	% Change	1968	1969	% Change
Washington	$16.4	$15.8	-3.7	$14.0	$14.5	+3.7
United States	$12,011	$12,942	+7.8	$14,835	$16,049	+8.2

Sources: Washington: Sales Finance Companies. United States: Federal Reserve.

TABLE IV-4

NEW CONSUMER LOANS MADE BY SELECTED
BANKS IN THE STATE OF WASHINGTON
1968-1969

	1968		1969		Per Cent Change 1969 over 1968		
	No.	$ (000)	No.	$ (000)	No. (%)	$ Volume (%)	Average Loan Size (%)
Direct							
Auto	36,166	69,389	31,916	63,399	-11.8	-8.6	+3.5
Personal	62,753	54,577	47,061	47,558	-25.0	-12.9	+16.2
Total Direct	98,919	123,966	78,977	110,957	-20.2	-10.5	
Indirect							
Auto	78,514	170,826	70,781	161,900	-10.0	-5.0	+5.1
Appliance	18,334	10,688	10,837	7,157	-40.9	-33.0	+13.3
Marine	2,679	5,973	2,521	7,485	-6.0	+25.0	+33.1
Total Indirect	99,527	187,487	84,139	176,542	-15.5	-5.8	

Source: Survey of Banks in Washington State.

TABLE IV-5

CONSUMER LOANS OUTSTANDING IN SELECTED
BANKS IN THE STATE OF WASHINGTON
1968-1969

	1968		1969		Per Cent Change 1969 over 1968		
	No.	$ (000)	No.	$ (000)	No. (%)	$ Volume (%)	Average Loan Size (%)
Direct							
Auto	48,556	65,883	45,742	63,358	-5.8	-3.8	+2.1
Personal	50,182	50,063	40,784	45,314	-18.7	-9.5	+11.3
Total Direct	98,738	115,946	86,526	108,672	-12.4	-6.3	
Indirect							
Auto	80,994	123,023	84,725	131,546	+4.6	+6.9	+2.2
Appliance	17,771	7,908	14,098	6,620	-20.7	-16.3	+5.5
Marine	3,425	6,485	3,703	8,223	+8.1	+26.8	+17.3
Total Indirect	102,190	137,416	102,526	146,389	+.3	+6.5	

Source: Survey of Banks in Washington State.

TABLE IV-6

KING COUNTY U.C.C. FILINGS[a]
1968 vs. 1969

	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.	Total (Last 6 mos.)	Total (Annual)
Finance:														
1968	2690	2651	2441	2603	2690	2519	2772	2580	1791	2255	2026	3126	14550	30144
1969	2402	2402	2349	2349	2193	2240	2183	2132	1962	2065	1786	2717	12845	26780
													(-12%)	(-11%)
Banks:														
1968	210	206	244	286	310	244	329	213	221	254	195	167	1379	2879
1969	159	184	253	303	271	262	203	174	133	160	134	125	929	2361
													(-33%)	**(-18%)**
Retail:														
1968	843	706	781	738	754	800	883	841	777	926	773	884	5084	9706
1969:	602	763	719	860	820	729	691	562	597	708	659	604	3821	8314
													(-25%)	(-15%)
Credit Union:														
1968	132	145	150	129	163	158	170	159	157	147	105	143	881	1758
1969	91	129	121	139	140	159	115	126	150	99	96	105	691	1470
													(-22%)	(-17%)
Savings & Loan:														
1968	13	17	20	13	14	9	8	10	10	9	13	16	66	152
1969	29	18	19	13	26	18	12	13	16	20	10	16	87	210
													(+32%)	(+38%)
Other[b]														
1968	114	101	111	115	155	122	163	138	95	124	105	182	807	1525
1969	151	116	123	168	168	207	142	118	169	144	118	184	875	1808
													(+ 8%)	(+18%)
Total: 1968	4002	3826	3747	3884	4086	3852	4325	3941	3051	3715	3217	4518	22767	46164
1969	3434	3612	3584	3832	3618	3615	3346	3125	3027	3196	2803	3751	19248	40943
	-14%	-6%	-5%	-2%	-12%	-6%	-33%	-21%	-1%	-14%	-13%	-17%	-15.5%	-12%

[a]Contracts on sales of untitled goods--"FS" only. [b]Other category includes mortgage companies.
Source: King County Records.

combination of percentages suggests a relative shift of installment credit business from banks and retailers to small loan companies.

The decline in the total of installment credit financing, and particularly the greater decline in bank and retailer business in this field, appear related to Initiative 245. Since state records do not show a decline in retail sales for the 1969 period covered in Table IV-6, and since a resurvey of firms which filed contracts revealed no change in policy regarding filings in 1969 versus 1968, it is obvious that many purchases which might have been financed through installment credit in 1968 were financed by other means in 1969. Of the twenty-eight retailers who said that they encouraged consumers to switch from one form of credit to another, eleven reported that they now ask the customer to arrange his own financing. Another stopped granting extended credit and required his customers to pay cash in thirty days. In all twelve of these cases, some customers were undoubtedly getting direct loans from credit unions and small loan companies which had no connection with the merchandise purchases, and were using the loan proceeds to make "cash" purchases at the retail stores. In other cases, even where there was no effort to suggest alternative forms of credit, people considered marginal credit risks were turned down for credit by banks and retailers and had to obtain the funds for "cash" purchases from small loan companies. Further, although the interviews with retailers did not turn up a trend toward switching people from installment credit to bank credit cards, later research suggested that many retailers did shift other forms of credit to bank credit cards.

Further, the price that the banks and finance companies charge the dealers with whom they do business is not controlled by law and it has gone up, reflecting the rising cost of money to these financial institutions. (See Table IV-7.) Instead of paying dealers "participation," a practice which involved having the bank share the interest proceeds received from the consumer loan with the merchant, the financial institutions began instead to discount dealer paper. In the case of auto dealers, for example, 19 out of the 24 dealers who responded to a question on participation stated that at the time of the survey (summer, 1969) they had lost an average of two per cent in revenues on indirect paper. In other words, if they had been receiving one per cent participation (or "commission") on the business they took to banks and finance companies, by the

TABLE IV-7

MARKET INTEREST RATES AND THE PRIME RATES

	Prime Rate	3 Mos. Treasury Bill	Finance Paper (3-6 Mos.)	Daily Av. Bkers. Accepts. (90 Day)	Federal Funds
Jan., 1964	4.50	3.52	3.82	3.70	3.48
Dec. 6, 1965	5.00	4.37	4.60	4.55	4.32
Mar. 10, 1966	5.50	4.58	5.02	4.96	4.65
June 29, 1966	5.75	4.50	5.39	5.39	5.17
Aug. 16, 1966	6.00	4.95	5.63	5.67	5.53
Jan. 26-27, 1967	5.50-5.75	4.72	5.50	5.23	4.94
Mar. 27, 1967	5.50	4.26	5.01	4.68	4.53
Nov. 20, 1967	6.00	4.72	5.17	4.98	4.12
April 19, 1968	6.50	5.37	5.60	5.75	5.76
Sept. 25, 1968	6.00-6.25	5.20	5.61	5.63	5.78
Nov. 13, 1968	6.25	5.45	5.75	5.97	5.81
Dec. 18, 1968	6.75	5.94	5.86	6.20	6.02
Jan. 7, 1969	7.00	6.13	6.14	6.46	6.30
Mar. 17, 1969	7.50	6.01	6.38	6.66	6.79
June 19, 1969	8.50	6.43	7.25	7.99	8.90
Mar. 25-6, 1970	8.00	6.63	7.68	7.60	7.76

Source: "How Interest Rates Got So High," *Special Report* by Manufacturers' Hanover Trust Company, June, 1970.

summer of 1969 they were paying a 1 per cent discount on this indirect paper. Both the participation prior to Initiative 245 and the discounts charged after the Act took effect tended to vary between dealers. At the time of the survey, small used-car dealers reported paying discounts as high as 5 per cent.

The principal reason for this shift in policy on the part of the financial institutions was that the paper generated as a result of credit transactions between consumers and retail dealers now carried an interest rate of only 12 per cent. Prior to the enactment of Initiative 245 on December 5, 1968, retail credit contracts could have been written with up to 18 per cent per annum. Thus the dealers were being forced to assume the burden of the mandatory reduction through the discounting of the contracts. Understandably the net result has been a decline in the volume and number of new indirect loans through the consumer and sales finance companies and commercial banks.

In addition to the reluctance of retail merchants to pay so much for money that they suffer losses on credit, some of them have also been affected by changes in the lending policies of the banks with whom they do business. These modifications are not uniform throughout the banking system but, for example, many banks will no longer handle indirect loans for older model automobiles, particularly those five years of age and older. When older model cars are still financed on an indirect basis, it is because the automobile dealers involved are especially important customers of the bank. A small number of banks no longer make indirect loans for amounts of less than $500 average loan size. This particular policy change affects furniture and appliance dealers primarily. One large bank with several branches is no longer handling any indirect paper from any household goods dealer in the state and another bank no longer handles consumer paper emanating from any appliance dealer. A third bank has cut out indirect paper originating with the hospitals in its community. Still another will handle only indirect paper when it originates with an individual who is also a depositor of the banks as well as a customer of the merchants.

The foregoing observations imply that the volume of business that banks do, both directly and indirectly, with consumers has been adversely affected except perhaps for credit cards. As mentioned earlier, indirect loans primarily for furniture and home appliances declined significantly (40.9 per cent for appliances) even though such loans have risen substantially on the national

level. The total volume of automobile loans in 1969 handled by Washington banks through automobile dealers declined 10 per cent in number and 5 per cent in volume below the level that it was prior to the enactment of Initiative 245. At the national level, however, indirect bank auto loans outstanding rose by 5.6 per cent in volume. (See Table IV-1.)

Direct consumer loans made by major Washington banks declined in 1969 relative to 1968. Direct auto loans declined 11.8 per cent in number of contracts and 8.6 per cent in dollar volume. Personal loans declined 25 per cent in number and 12.9 per cent in dollar volume. The total of direct bank consumer loans declined 20.2 per cent in number of loans and 10.5 per cent in dollar volume in 1969 relative to 1968. There were similar, though less pronounced, declines in the amount of consumer loans outstanding in 1969 relative to 1968. The total outstanding consumer loans declined 12.4 per cent in number and 6.3 per cent in dollar volume. In all of the above categories of loans, there was an increase in the average loan size. Although the average size of auto loans increased only 3.5 per cent, the average size of personal loans increased 16.2 per cent due largely to the setting of higher minimum loan sizes and a shift toward more affluent customers.

The dollar volume of new indirect consumer loans made by commercial banks, consumer finance companies and sales finance companies combined in 1969 was 5.7 per cent less than in 1968. There was a slight increase in indirect loans by consumer finance companies, but not enough to materially affect the above figure.

Information obtained about the first quarter of 1969 from interviews with automobile dealers throughout the state during the third quarter of 1969 led us to believe that there had been a significant movement toward the financing of automobiles through consumer finance companies, especially in the case of older used cars because of the difficulty encountered in financing these automobiles through banks. Some corroborating evidence was uncovered when it was observed that a number of automobile dealers said that they had experienced an increase in the number of cars sold for cash. It would appear reasonable to assume that in those instances where this was observed or encouraged by the dealers, direct loans from small loan companies were the most probable source of funds, although credit unions and banks may have been involved.

TABLE IV-8

UNITED STATES CONSUMER INSTALMENT CREDIT OUTSTANDING BY TYPE AND BY HOLDER, 1969 BY MONTHS
(in millions of dollars)

	All Finance Companies Combined	Commercial Banks	Other Financial Institutions	Automobile Dealers	Total
Automobile Paper					
December (1968)	10,124	19,318	4,368	320	34,130
January (1969)	10,087	19,268	4,339	319	34,013
February	10,098	19,270	4,366	319	34,053
March	10,124	19,392	4,426	320	34,262
April	10,232	19,661	4,515	325	34,733
May	10,384	19,908	4,609	329	35,230
June	10,577	20,184	4,710	333	35,804
July	10,673	20,315	4,758	335	36,081
August	10,703	20,372	4,834	336	36,245
September	10,687	20,407	4,891	336	36,321
October	10,822	20,511	4,928	338	36,599
November	10,854	20,591	4,958	337	36,650
December	10,866	20,704	4,996	336	36,602

Source: National Consumer Finance Association, April 6, 1970, p. 49.

On the other hand, an examination of the operating results of small loan companies in the state for the entire year did not reveal any appreciable growth in the dollar total of loans made during the year. This was a somewhat surprising finding. There is, of course, evidence of a relative shift in available consumer credit business toward consumer finance companies as compared with retailer and bank financing. The installment contract filings referred to earlier in the chapter showed that total installment filings declined, but that the decline in consumer finance filings was less than the average decline and that the decline in retailer and bank filings were much above average. In the face of an increased opportunity it was expected there would be an increase in the volume of business that these small loan companies would transact. Instead, the small loan companies appear to have taken advantage of the opportunity to improve the risk quality of their loan portfolios. Net earnings before interest on borrowed funds was up by more than 10 times the average increase during the previous three years and the change in the number and amount of loans charged off was up by about 11 per cent and 14 per cent respectively. A five year summary of the small loan company operating results in Washington in shown in Table IV-9.

Charges and Costs

The retail businessmen and financial institutions have, as expected, tried to reduce the costs associated with credit transactions and loans and to the extent possible to maximize the potential revenue obtainable under the law. Since these affected businessmen have been unable to do much on the revenue producing side, they have understandably enough devoted their primary efforts to cost reduction, at least as far as the strictly financial side of the matter is concerned. The major emphasis in trying to achieve an upward revision of revenues has taken place in the area of product price adjustments. This activity is discussed in the following chapter.

One of the ways in which commercial banks have made an effort to reduce costs is in the handling of loans for small amounts, i.e. under $500. Such loans have been made on their credit card systems whenever possible. The main reason for this development appears to be the lower cost of handling loan transactions of that size in this manner. Service charges and other fees such

TABLE IV-9

FIVE-YEAR ANALYSIS OF SMALL LOAN COMPANIES

	1965	1966	1967	1968	1969
Number of Licensed Offices	252	258	265	271	286
Number of Offices Reporting	251	258	265	271	286
Total Loans Made	185,255	175,608	176,680	184,940	186,552
Amount of Loans Made	$ 98,648,377	$ 93,602,730	$ 97,139,667	$103,979,909	$109,101,461
Total Loans Outstanding	164,665	171,447	174,503	181,524	189,058
Amount of Loans Outstanding	$ 76,498,429	$ 79,276,833	$ 82,160,588	$ 87,557,136	$ 92,704,367
Number of Contracts (Indirect)	32,011	39,984	41,795	64,153	68,339
Amount of Contracts (Indirect)	$ 7,170,699	$ 11,252,947	$ 13,037,682	$ 20,994,248	$ 21,128,176
Number of Other Loans (Indirect)	5,899	7,288	8,683	8,487	7,023
Amount of Other Loans (Indirect) (12% loans, i.e., over $500)	$ 12,138,211	$ 13,529,029	$ 15,542,635	$ 15,499,419	$ 12,031,459
Total Assets	$119,244,126	$128,316,772	$135,970,123	$146,718,231	$149,694,907
Net Earnings Before Interest on Borrowed Funds	$ 5,154,839	$ 5,208,337	$ 5,273,576	$ 5,350,203	$ 6,124,868
Monthly Rate Collected	2.13%	2.08%	2.10%	2.13%	2.11%
Number of Loans Charged Off	5,819	6,074	6,286	6,719	7,440
Amount of Loans Charged Off	$ 2,138,160	$ 2,329,656	$ 2,463,840	$ 2,687,767	$ 3,059,731

Source: Supervisor of Banks, State of Washington.

as those for late payment have also b en either raised or instituted wherever they are allowed and have not heretofore been in effect.

Banks have also attempted to lower their costs of doing business by making qualitative changes in their consumer loan portfolio. Virtually all financial institutions and retailers have tightened their lending policies in one or more of the following areas:

1. Down payment requirements have been increased.
2. Maturities on loans have been shortened.
3. The discretion of local lending officers to waive requirements on consumer loans such as minimum uncommitted monthly income, minimum residence, and minimum length of time on the job has been substantially curtailed.

The impact of these policy changes has been reflected in operating results. One bank reported that their bad debt losses, for example, had been reduced by one-third.

Additional evidence concerning the efforts of businessmen to increase the monetary size of credit transactions is also furnished from a review of the installment sales contracts filed in King County. The average size of these contracts increased from $589 in 1968 to $670 in 1969. These data may also be an indication of the success that banks have had in switching consumers to bank cards which, as we pointed out before, appear to be a form of credit which is less expensive administratively from the lending institutions point of view.

Retailers as well as financial institutions appear to have made a serious attempt to reduce the time period over which they are willing to do business on a credit basis. Eight auto dealers reduced maturities by six months, and one reduced maturities for marginal buyers from a possible 36 months to spans of 2-6 months. By doing so they are able to reduce the dollar amount of the discount on the paper that they sell to financial institutions.

In addition to the reduction in the amount of interest permitted, retailers have also had to contend with a reduced service charge ceiling on consumer loans. The amount allowed prior to the enactment of the law was $15; this was reduced to $10 or 1 per cent per month on the unpaid balance. On the other hand, according to our survey, many banks and retailers have apparently

instituted such charges for the first time in their efforts to generate additional revenues. In this connection it may also be noted that some retailers have raised their interest charges to 12 per cent in those cases where they had been charging consumers less.

Most large-scale retailers have not found it feasible to eliminate the free credit granted to a significant portion of their retail customers as a result of a tradition of open-book accounts. What has happened, however, is that the time period granted to customers on open-book accounts has been reduced. Merchants who were offering 90-day open book accounts say they have cut this to 60 days and the 60-day accounts have been cut to 30. Regular accounts as well as slow pay accounts have been encouraged to switch to sales contracts, revolving accounts or bank cards.

Retailers, and particularly the automobile dealers, have also compensated for their decline in income on credit transactions by selling more of their customers credit life and credit health and accident insurance policies. Around one-third of the auto dealers reported that they were pushing much harder to sell credit insurance, and in some cases began to require customers to purchase the insurance after the passage of the Initiative. The consumer who purchases either a health and accident and/or life insurance contract incurs an additional cost to himself that is determined by the amount of the loan that he has negotiated and the applicable rate for the coverage involved. The maximum legal rate established for credit life insurance in Washington is 60 cents per $100 per year. The rate for health and accident insurance coverage on credit transactions varies with the benefits offered in the particular policy.

In addition to a desire to increase their revenues (through receiving 40 per cent of the premiums), there are other reasons why retailers have emphasized the sale of these types of insurance. First of all in the event of sickness or disability on the part of the consumer his payments are made by the insurance company. Second, the contract between the merchant and the consumer is also more salable if credit insurance is associated with it. Many finance companies will either reject the paper or discount it an additional point if the purchaser is not insured.

About one-third of the automobile dealers interviewed reported that they increased their emphasis on credit insurance in connection with the sale of automobiles. Secondary sources of information representing about 90 per cent of the auto credit insurance transactions in the state also substantiate these dealer responses. The evidence is even more convincing when Washington and the neighboring border states of Oregon and Idaho are compared. As may be seen from an examination of Table IV-10 the amount of life and health insurance premiums on automobile sales in Washington increased by 23 per cent in 1969 while there was only a negligible increase in both Oregon and Idaho. Table IV-11 shows the changes between 1968 and 1969 in total credit insurance. Table IV-12 provides data on northwest states and the United States for credit life insurance in force in the years 1958 through 1969.

TABLE IV-10

CREDIT LIFE AND HEALTH INSURANCE PREMIUMS ON AUTOS

(in thousands of dollars)

	1968	1969	Per Cent Change
Washington	$1666	$2056	23%
Oregon	$ 739	$ 741	0%
Idaho	$ 272	$ 273	0.4%

Source: Major insurance companies specializing in automobile credit insurance.

TABLE IV-11

NEW CREDIT INSURANCE BUSINESS
STATE OF WASHINGTON
1968 AND 1969

Type	1968	1969	Per Cent Change
Individual Life	$ 205,067	$ 135,534	-43.9%
Group Life	$8,902,190	$9,384,760	+ 5.4
Total Life	$9,107,257	$9,520,294	+ 4.5
Group A & H	$2,732,741	$3,438,749	+25.8
Other A & H	$ 141,097	$ 12,095	--
Total A & H	$2,873,838	$3,450,844	+20.0
Total Credit Insurance	$11,981,095	$12,971,138	+ 8.3

Source: Life insurance company annual reports.

TABLE IV-12

CREDIT LIFE INSURANCE IN FORCE
1958-1969

	1969	1968	1967	1966	1965	1964	1963	1962	1961	1960	1959	1958
Washington												
Number (000)	954	865	759	772	688	637	559	516	526	504	440	337
$ Amount (000,000)	927	855	740	717	583	526	443	391	364	337	286	212
Oregon												
Number (000)	793	707	582	697	646	505	443	413	389	441	377	326
$ Amount (000,000)	1202	1077	941	934	877	790	680	621	532	478	393	289
Idaho												
Number (000)	292	275	259	205	177	189	170	133	106	105	126	96
$ Amount (000,000)	326	304	267	231	205	204	191	154	121	116	113	80
United States												
Number (000)	79,372	75,860	71,183	70,090	63,178	58,017	52,856	47,620	45,262	43,479	39,422	35,004
$ Amount (000,000)	83,788	75,881	66,952	62,672	56,993	49,933	43,555	38,011	33,493	31,183	26,680	21,474
Per Cent Change in dollars		+13.3	+6.80	+10.0	+14.1	+14.6	+14.6			+17.0	+24.0	+9.0
Per Cent Change in number											+13.0	+13.0

Source: Life Insurance Factbook 1969-1958 (New York: Institute of Life Insurance).

At the time of the interviewing program, there was little indication of changes in other credit-related fees and charges.

One concluding remark on the behavior of the businessmen with reference to the issue of cost and revenue adjustments seems warranted. The evidence at hand suggests that their reaction to the passage of Initiative 245 did not necessarily take place immediately after the law went into effect, although there was a great deal of talk about it at the time. The adjustments which have taken place appear to have gone on throughout the year and it is quite possible that some adjustments still remain to be made. This seems to be due in part to the fact that many businessmen, particularly in the smaller firms, were unable to ascertain the precise effect of the law on their operations while others were unable to reach a decision about what to do in the face of the effect of the law on their operations. The survival of all of the firms studied however may well require an adjustment to the changed environment.

In spite of the imposition of fees and charges and the potential cost savings involved in the processing of loan transactions, personal loans for small amounts, no matter how small the risk associated with them, are not very profitable for banks in the face of current high money costs. The maximum rates the banks are allowed to charge under existing state laws is 12 per cent simple interest. The usury law has prevented banks from raising their interest rates above 12 per cent on direct merchandise loans and Initiative 245 holds bank credit cards to 12 per cent in the face of a rapid and substantial increase in their cost of money. Whether the banks actually would raise their rates if they had the opportunity to do so is a question. The evidence at hand strongly suggests that they would have raised their rates if they had been able to do so. If the present high cost of money persists and the 12 per cent revenue ceiling remains in effect, it is quite possible that some banks might drop bank credit cards if net income from this source of business is not forthcoming. One possibility for additional bank revenue would involve a direct annual charge to the consumer for the privilege of using the bank credit card services.

Credit cards are still in use because of the very substantial investment that the sponsoring banks have made in them, because of hopes that either the price of money will come down and/or the interest ceiling will be revised

upward and because of a feeling among bankers that credit cards are going to grow in importance in the future. In the long-run, however, banks may be unwilling to bear the burden of supplying a service the costs of which equal or almost equal and, which may ultimately exceed, the price that can be charged for it.

It is also reasonably apparent that the retail merchants are either not making money or actually losing money on that part of their business that they do on a credit rather than on a cash basis. However, it seems even less likely that the affected retailers will be able to dispense with loan arrangements between themselves and their customers, even in the face of this lack of profitability or outright loss. The merchants have by now done many of the things they can do to maximize their credit revenue and reduce their credit costs. Additional adjustments will have to be made in the area of product price increases or product cost and service reductions. The sale of automobiles and, to a slightly lesser extent, household furnishings and major appliances, depend heavily on purchasers who must borrow in order to buy. Borrowing money for a good reason is now a socially accepted practice in the United States; it is an absolute necessity for the survival for some types of businesses. It is no exaggeration to suggest that the whole American economy would be seriously shaken and many of the largest firms in the automotive, furniture, and appliance industries forced into bankruptcy along with thousands of retailers if no loans were available to consumers for the purpose of purchasing these items. The cost of credit sales will simply have to be absorbed in one way or another by the ultimate consumer. This is not to suggest that it is a matter of indifference how this burden is borne nor is it meant to suggest that it will be borne equally by all consumers.

Effects on Consumers

Positive effects. The primary effect of Initiative 245 insofar as individual consumers are concerned is that the cost of direct or indirect merchandise loans, the use of bank credit cards and interest charged by merchants has been either held at or reduced to 12 per cent per annum. In view of the rapid and substantial increase in the cost of money (the prime rate increased from 6.25 per cent in December, 1968 to 8.50 per cent in June, 1969) and the costs of

operating a credit card service and a credit department, it seems quite likely that the banks would have increased their charges above 12 per cent on direct merchandise loans and stayed at--or raised to--a charge of 18 per cent on bank credit cards. Further, most retail merchants would have kept finance charges at or raised them to 18 per cent. The evidence for this statement is, of course, largely circumstantial but it appears quite convincing.

The reduction in gross profit margins due to the reduction in interest rates has also probably worked to the advantage of consumers by encouraging businessmen to strive for greater efficiency in their operations in order to achieve cost reductions and thereby re-establish the gross profit margins in effect prior to the passage of Initiative 245. On the other hand, there is no assurance that if businessmen could achieve greater profitability through efficiencies that they would pass on the benefits to their customers.

Negative effects. The effect of the law is, however, uneven and there appear to be groups of consumers who have suffered adversely from the effects of the law. Cash customers, for example, have received no benefits and, on the other hand, they are in all likelihood paying somewhat higher prices. Those persons who were on open book accounts prior to the passage of the law and who are still in the same category have been affected in essentially the same manner a have cash customers although they are still being subsidized by cash customers to some extent.

There are those who must now pay more for the money that they borrow because banks and merchants will no longer lend to them at the new lower rates. Also included in the category of persons adversely affected are those who were on open book accounts prior to the passage of the law and who are now on revolving credit accounts or some other basis which requires them to pay 12 per cent interest.

Finally, there are those who must forego making purchases of products that require loans because of an inability to borrow from any source on terms that would permit the buyer to handle repayment of a loan out of future income.

Credit eligibility problems. After the passage of Initiative 245, retailers and financial institutions tightened up on the granting of credit to reduce potential losses in the form of bad debts and credit and collection expenses. First, there were some retailers who went out of the business of financing

their own customers. Eleven of the 63 general merchandise, furniture and appliance retailers who responded to the question stated that they changed to a policy of making the customer arrange his own financing. This meant essentially that none of their previous credit customers were eligible for credit. Similarly, of 37 retailers who offered 90-day open book credit prior to the initiative, 5 cancelled the plan entirely, 6 more reduced the time period from 90 to 30 days, and two others reduced the time period to 60 days.

Of the 30 auto dealers who sold new cars, 22 reported tightening the eligibility rules for credit, and of the 46 dealers handling used cars (including dealers selling both new and used) 36 tightened up on eligibility rules. For seven of the dealers this meant cancelling out whole categories of people who might have received credit prior to the Initiative. Two-thirds of the other retailers reported that they were rejecting applicants whom they would have accepted prior to the passage of the law. This was also borne out by the fact that all of the merchants interviewed showed a 9 per cent increase in credit application rejection rates during the second quarter of 1969. New and used auto dealers reported even higher rejection rates. Whether a credit eligibility criterion was income, length of residence, time on a job or repayment history, it was likely to be made tougher after passage of Initiative 245.

There are also indications that bank credit cards are being issued in a more discriminating manner. Based on a survey representing 95 per cent of the bank credit card business in the state, Table IV-13 shows that rejection rates on new applications for major bank cards were up sharply in the last six months of 1969. The rejection rate was significantly higher in each of these months over that of the same month in 1968. The increase in 1969 over 1968 was 2.2 per cent in July, 11.4 per cent in August, 8.4 per cent in September, 10.7 per cent in October, 6.1 per cent in November and 13.0 per cent in December. Although the rejection rates were lower in 1969 than 1968 for each of the first six months, the total rejection rate for the year was 4.1 per cent higher in 1969.

Shortened maturities. The specific effects of all of the policy changes that have been made by banks, retailers and finance companies in connection with indirect loans can be inferred from the nature of the changes that have been instituted. The effect of the shortening of the loan repayment time

TABLE IV-13

BANKCARD APPLICATIONS RECEIVED AND DECLINED--WASHINGTON, 1968 & 1969

	1968 Applications			1969 Applications		
	Number Received	Number Declined	Per Cent Declined	Number Received	Number Declined	Per Cent Declined
Total	60,860	23,758	39.0%	132,595	57,203	43.1
January	3917	1597	40.7	6612	2459	37.2
February	3140	1370	43.6	5387	2100	39.0
March	3074	1342	43.7	7525	2685	35.7
April	4435	1961	44.2	9160	3622	39.5
May	4103	1757	42.8	9982	4064	40.7
June	4512	1845	40.9	16770	6717	40.1
July	5084	2097	41.2	12801	5559	43.4
August	5372	2042	38.0	12132	5993	49.4
September	5997	2242	37.4	13108	6005	45.8
October	8831	2784	31.5	12857	5430	42.2
November	5931	2396	40.4	12126	5636	46.5
December	6464	2325	36.0	14135	6933	49.0

period, for example, has been to increase the size of the consumer's monthly payment. This means that most consumers are able to borrow less than they were able to prior to the enactment of the law. The reported increase in downpayment requirements also serves to inhibit the sale of products sold on credit in much the same way--by shortening maturities.

The question of the size of the consumer's monthly payment is important because it is one of the credit related variables that the consumer frequently determines by choice. As pointed out before, this choice is constrained by the consumer's ability to repay the loan. The size of the monthly payment on a given purchase has been shown to be the key decision variable considered by some classes of consumers. Juster and Shay point out that financial institutions establish normative maturity limitations and the tendency is for some consumers to seek the longest contract maturities.

Notwithstanding the desire for long maturities on the part of many consumers and the opportunity that it represents to increase borrowing power, the desire of the merchants to minimize their costs of doing business on a credit basis and the income constraint both work to the disadvantage of lower income members of the community.

A consumer faced with purchasing a product requiring higher monthly payments and if these monthly payments are more than he can manage, can seek an adjustment in product quality level that may effectively reduce the total price of the merchandise and loan with the objective of reducing his monthly payments.

Increased down payments. There are several forces at work expanding downpayment requirements. First, retailers have made a conscious attempt to shorten maturities in order to reduce the amount of the discount that they must contend with on indirect paper sold to financial institutions and to improve their credit turnover. Second, higher downpayments serve to minimize high risk customer transactions. While customers who can afford large downpayments are not always better credit risks than those who can afford only a small downpayment, merchants believe, with some justification, that by following this procedure their risks are minimized. Twenty five per cent of the non-automotive retailers indicated that they had increased their downpayment requirements on credit purchases by an average of 15 per cent subsequent to the enactment of Initiative 245. Many retailers no longer offer "no downpayment" credit

arrangements. A number of retailers indicated that they required an additional 15 to 20 per cent down from those buyers whom they regarded as marginal risks. It also seems inevitable under these circumstances that at least some consumers would try to meet the retailer's downpayment requirements as well as the financing of the balance from small loan companies at rates higher than those offered by the retail merchants prior to the enactment of the law.

"Mousing." An illustration of the manner in which these changes in lending policies affect low income consumers is the practice of "mousing." If the consumer does not have enough money to meet the downpayment requirements for an automobile, for example, he may be obliged to borrow from one or more consumer finance companies using such items as his furniture as collateral for the loan. Then, if he is unable to obtain financing from a bank directly or indirectly for the balance of the purchase price, he may go to a finance company and use the auto for collateral to obtain a loan to cover the balance. Since these small loan companies are not limited by the 12 per cent restriction, and since the rate of interest they charge the consumer is inversely related to the size of the loan, the buyer who has to go through this practice of mousing ends up paying a larger sum of interest than he would if he obtained the loan in a single transaction from the dealer, a bank or through a sales finance company.

Several automobile dealers in the field survey indicated that "mousing" was more frequent after the passage of Initiative 245 than it was before. The records of one of the dealers surveyed showed that in his case at least increased downpayment requirements had apparently led to an increase in mousing. While the proportion of automobile buyers in this category is still small, i.e. less than 5 per cent, the proportion of automobile purchasers utilizing small loan companies for at least a part of their loan requirements exceeded 50 per cent in the case of this particular dealer.

The following quotation suggests that this is not an isolated example. "The squeeze is especially apparent in used cars . . . auto dealers have to guarantee repayment of the loans they submit to lending agencies . . . dealers are now telling purchasers of older used cars that the customer must finance the cars through small loan companies."[1]

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[1]*Seattle Times*, December 18, 1969.

Role of banks. There has been, for a number of reasons, a definite reluctance on the part of banks to take over auto dealer paper in 1969 as compared with 1968. Banks typically had a policy of full recourse prior to the passage of Initiative 245, with some exceptions for "quality" paper. The banks might insist that dealers had to repurchase cars which were repossessed by banks. The losses to the bank were recovered from the dealers reserve account. Repurchase agreements are limited as to time (90 days, for example) so that if a bank fails to repossess within the time limit, the dealer is no longer obligated. Six dealers reported a tightening on recourse, usually by extending the time limit on repurchase agreements from 90 to 120 days. This, in turn has encouraged auto dealers to screen their credit sales customers more carefully. Naturally, some credit customers will suffer from this selective procedure. Although the volume of auto dealer paper decreased in 1969, the average value of each loan increased by about $100.

In comparing 1969 with 1968, it is seen that new direct bank auto loans decreased 11.8 per cent in number and 8.6 per cent in volume. Yet the average loan size increased by 3.5 per cent. New indirect bank auto loans declined 10 per cent in number and 5 per cent in volume. Average loan size increased 5.1 per cent. Personal secured and unsecured direct bank loans declined 25 per cent in number and 12.9 per cent in volume. Direct personal loans increased 16.2 per cent in average size. New indirect bank loans for appliance, home equipment and home furnishings purchases declined 40.9 per cent in number and 33 per cent in volume. The average size increased by 13.3 per cent. New indirect loans for marine boats and motors declined 6 per cent in number and increased 25 per cent in volume. The average size of bank loan for this purpose increased 33.1 per cent. This suggests that the decrease in the number of loans was not across the board but the cutoff was made at the lower tail of the distribution of loans by size resulting in a fewer number of loans but loans with a larger average size. This phenomenon is even more apparent in the case of direct loans.

Direct loans from banks to consumers for the purpose of an automobile purchase also decreased in number in 1969 when compared with 1968 while the average size of a loan in 1969 increased by almost $200. This indicates that banks have become even more selective in screening borrowers who come to them directly.

The rising cost of money to the lending institutions has undoubtedly intensified the effect of restricting the price that these same institutions can charge for the money that the lend.

In general, it is obvious that a low ceiling on the amount that can be charged for loans has encouraged lenders to reduce their risks by discriminating against those borrowers who are viewed as less creditworthy.

Summary

In sum it appears that people who are new in the community and are new on their jobs with relatively limited incomes and who wish to buy major appliances or older automobiles are being hit hardest by the law. In spite of what appear to be reasonable expectations to the contrary these people have also experienced difficulty borrowing money, at least in the short run, from relatively higher cost, higher risk-bearing financial institutions such as small loan companies.

The first hypothesis relative to credit was, "Banks and merchants are doing less business on a credit basis." All evidence is that credit declined both absolutely and relatively. Direct consumer loans declined and indirect consumer loans through banks and finance companies have declined because the financial institutions are less willing to loan at the new price ceiling. Increases in the lenders' cost of doing business, particularly in the cost of money, has intensified the problem. The net result has struck with special severity at furniture, appliance and used auto retailers.

The second hypothesis was, "Lenders are diverting business to the most profitable types of loans or credit arrangements." Banks have switched more credit to their bank credit cards, which are considered more profitable than instalment or direct merchandise loans, and have raised the minimum size of loan they will grant. Retailers have switched customers from instalment to revolving credit, they have shortened their open-book time periods and/or have divested themselves of some or all of their credit business by switching customers to bank credit cards or to other forms of outside credit.

The third hypothesis was "Small loan companies are doing more business." This does not appear to hold in absolute terms, since total volume has declined. In relative terms, however, there appears to be a shift toward

small-loan companies since in a totally declining market they declined less than the average whereas bank and retailer credit declined much more than the average. It is possible that they too became more selective in granting credit, because they showed a sharp increase in profitability in 1969 relative to any recent year.

The fourth hypothesis was, "Credit losses have decreased." Because businessmen's records on costs tend to be sketchy and because they often were reluctant to reveal what they regard as proprietary information about their operations, it was difficult to ascertain the extent to which lenders have been able to reduce their costs of transacting business on a credit basis. There were some cases of substantial reductions in costs, but their number was insufficient to warrant conclusions. The evidence gathered suggests that there are limits on the extent to which businessmen can seek relief from the loss in credit revenues by means of cost reductions. Most credit grantors, particularly large retailers and financial institutions, appear to have embarked on cost-cutting programs and have engaged in efforts to maximize credit income to the extent permitted by law.

A fifth hypothesis was, "More poor people have been affected by the new law than middle or upper-income people, and marginal standing from a credit standpoint has been redefined to exclude some individuals classified as higher risks." It is possible that creditworthy consumers have benefited from a decrease in allowable interest charges from 18 to 12 per cent per annum on consumer credit. The actions taken by financial institutions and retailers, however, tend to be at the expense of the lower income people, particularly those considered marginal credit risks. The tightening of credit granting criteria, the raising of the minimum amount eligible for credit, the increasing of downpayment requirements and the shortening of maturities all strike hardest at poor people. Those most affected are the people who were literally excluded from markets and those who were shunted off to small loan companies by retailers. The legal interest schedules of small loan companies, as high as 36 per cent per year, worked a hardship on consumers formerly able to get regular retail or bank credit.

The sixth hypothesis was, "Financing charges other than interest rates have increased." Although the new law reduced the basic service charge from

$15 to $10 or 1 per cent per month, some firms have instituted minimum service charges where before there were none. The charge for overdraft plans on credit cards has increased--in one case it was doubled. The increased requirement that consumers take out credit insurance has raised the effective costs of borrowing well above the 12 per cent prescribed by law. Retailers now pay a discount on indirect paper (cases were reported of discounts as high as 5 per cent) where before they received a commission ("participation"). Such costs must eventually be paid by the consumer in some way.

The final hypothesis was, "Businessmen have become more strict in the application of rules on delinquent accounts." Whereas these rules were often not utilized prior to the passage of the Initiative, they were brought to bear as a cost-cutting measure after the law took effect. Some consumers receiving credit, or eligible for credit, prior to the law were dropped. These effects were part of the result of the general tightening of credit availability in response to the law but the increases in levels of wholesale interest rates also contributed.

In sum, credit has become less available, it may cost less in terms of interest on revolving and instalment credit for creditworthy consumers, it costs more for creditworthy customers whose open-book privileges have been cancelled or reduced, it costs more for many low-income marginal-risk consumers, it has been denied to some poor people who formerly were eligible for credit and in retail stores it was being subsidized by cash customers at the time of the field work for this study.

CHAPTER V

PRODUCT RELATED IMPACTS

Product Related Hypotheses

The product-related hypotheses established at the outset of this study were as follows:

Prices of merchandise frequently sold on credit have gone up.

Different products and different businesses have been affected in different ways by the new law.

Leasing of merchandise frequently sold on credit has increased.

The passage of Initiative 245 imposed direct limitations upon the credit related policies of retailers. Secondary and somewhat indirect effects were also imposed upon the product related decisions of retailers. That is, the credit related policy restrictions were, in effect, imposed on the retailer by law, and he therefore adjusted his business operations to the new situation using the balance of his marketing options--his product related policies. For example, changes were made in pricing and service policies to compensate for changes in the credit area.

The imposition of a price ceiling on all credit customers had two important effects on retailers. First, it represented a potential 33 1/3 per cent decrease in finance income in some transactions. In many cases this represented a substantial portion of the firm's total gross and net profits. Second, with such a decrease in income it became imperative for the retailers to attempt to reduce costs, increase total revenues, or both.

Product Related Decisions: Prices

Essentially a retailer places a price on his service, product and credit terms. Each represents a revenue-generating and cost-incurring activity. When the contribution of one component is restricted, the burden of adjustment rests

on the other components. When credit income is significantly reduced by legislation the businessman's response can be expected to be in the form of cost reductions and an attempt to increase the revenue-generating capacity of the other activities in his business. Hence, prices may be increased on products and services. Within the context of such adjustments, attempts may also be made to reduce costs as well. In the matter of product price, per se, prices may be raised on items usually sold on a credit basis, on all items, or on some selection of credit-sensitive and/or non-credit-sensitive items.

In this study, retailers are divided into two major groups: auto dealers and others. The "others" include general merchandise retailers (department stores), and furniture and appliance retailers. The "other" retailers are covered first in this report.

The majority (56 per cent) of retailers (other than auto dealers) included in the sample of Washington retailers indicated that they raised prices on all merchandise on the average of 5 per cent in response to the passage of Initiative 245. A somewhat larger majority (64 per cent) of furniture and appliance dealers stated that they raised prices on items usually sold on credit. Thirty-one per cent of the department stores also raised prices for products usually sold on credit.

In a response which was less direct, but which had the net effect of raising prices to consumers, retailers stated that they were adjusting their merchandise offerings to obtain higher average mark-ups than existed prior to Initiative 245. Such adjustments can be brought about by changing to suppliers whose suggested retail prices include a higher percentage of gross margin for retailers, by obtaining suppliers whose wholesale prices permit a higher gross margin at accepted local retail price lines, or by replacing stocks with items whose unit prices are higher than those of prior offerings. This last approach will increase the gross margin per unit in dollars without raising the percentage of gross margin realized. Gross margins, of course, are affected by both cost and revenue factors. For example, increased efficiency in buying brought about by tighter controls, better inventory information, or more accurate selection can increase realized gross margin with no change in initial price mark-on rates. The greater efficiency in buying reduces losses from

markdowns in price that are made necessary by slow rates of turnover such as occur from overbuying or from errors in the selection of merchandise.

In general, it appears that there was no single pattern of response among retailers but price increases came mostly in the form of general price increases rather than singling out specific products. A retail sale may now require a trade-in whereas prior to Initiative 245 no trade-in was required. Or, in the case of pricing trade-ins, the retailer may now offer less for the used item. A few of the price increases noted above were in the form of changes in such product related charges.

Some retailers instituted charges for services which were provided for consumers free of charge prior to Initiative 245. Product-related charges for services formerly furnished free of charge have been assessed on check cashing, wrapping and packaging, lay-away, delivery, product installation, product service contracts and parking. In some cases, where charges had existed on such services, the charges were increased. In parking, for example, some stores ceased validating parking tickets so that the consumer had to pay the regular parking charge rather than obtaining it free through validation. In other cases, the charges for parking which was under the control of retailers were increased. Some stores placed substantial charges on product installation, where this service had been free. The new charges may not actually have covered the installation costs to the store, but they represented net price increases to consumers.

Implications for the Consumer. If price increases in product and product related services just compensate for the revenue cost by reducing the interest ceiling on credit extension then the typical credit customer has not been affected appreciably. However, those who pay cash for their products and services may now pay more.

The consumer who trades in a used appliance may well expect to receive less for it because of a change in trade-in policies by retailers. As mentioned above some consumers can now expect to pay for services that were provided by the retailer without charge prior to Initiative 245. Quite probably all consumers are paying totally a higher price for products and services as the passage of the Initiative appears to have encouraged price increases.

These price changes were also very probably facilitated by the then recent growth in the state's economy and the generally high level of employment prevailing at the time the law was enacted.

Product Price Decision Verification: Appliances

In an attempt to gather concrete evidence on whether or not retailers were raising prices as they said they were in response to Initiative 245, three surveys of prices on major appliances were conducted. They took place in April and August 1969, and January, 1970. Stores in Seattle, Spokane, Portland and Los Angeles were included in the first two surveys, but the January survey covered only Los Angeles and Seattle. Seattle was considered sufficiently representative of the state of Washington that it was deemed unnecessary to include Spokane. Portland, Oregon was included initially on the theory that its location in another state and at some distance (around 170 miles) from Seattle would provide an independent market for comparison purposes. Executives of chain retailing organizations were of the opinion, however, that Portland prices were strongly influenced by Seattle prices and that they might tend to follow Seattle trends regardless of the reason for the Seattle price trends.

The surveys were made in eight to ten large department and appliance stores in each of the cities visited, and the same stores were used in all surveys. The purpose of the surveys was to obtain the prices on six types of major appliances in order to compare the trends of these prices during the 9-month period in question. Working from a list of model numbers and descriptions provided by the comparison shopping bureaus of large stores, the prices were obtained by inspecting price books of major appliance departments and checking price tags on the merchandise or, in the few cases where price books were not made available, by inspecting the price tags alone. This method was modified for the third survey as described below.

Important difficulties were encountered because of several uncontrollable variables facing the price shoppers which made the task of locating identical models difficult. One major difference in the Seattle and Los Angeles markets was the dominance of electric appliances in some categories (cooking ranges and clothes dryers) in the former, and gas appliances in the latter. Another major

problem was that of model changes. Some appliances that were priced in April, for instance, did not exist in August, or if they did exist, they were placed on sale because of newer models in the market. This limited the usefulness of price comparisons from quarter to quarter, and reduced the number of identical models to a point where no statistical tests for price changes could be applied.

The initial survey in April used the comparison shopping list as a guide in the selection of appliance models. In August, an attempt was made to duplicate exactly the April survey by visiting the same stores and pricing the same models. However, because of the obstacles mentioned above, this met with only partial success. In an attempt to overcome this weakness in January, as many appliance models as possible were obtained in both Seattle and Los Angeles. This "shotgun" approach proved much bett r than the use of the comparison shopping list with respect to the number of comparable models in both cities. In the last survey, the number of identical models for most appliances was increased significantly. However, since most of the January models were different from the two earlier surveys, no statistically significant price trend analysis of particular appliances is possible with the available data.

In analyzing the available prices of identical models that could be found during each survey, the average price of each type of appliance is shown for Los Angeles and Seattle in Table V-1.

The models recorded in each appliance category for Los Angeles and Seattle were exactly the same for the first two surveys. Unfortunately, although in the January survey it was possible to obt in a much larger number of identical models in the two cities, these models were not the same as thos obtained during the April and August surveys. This hampers comparing price trends for the 9-month period.

Since the trends of retail sales volumes might be expected to influence price trends, retail sales data are provided here as economic background. In a declining market, price competition might be expected to lower prices, and vice versa. The retail furniture and appliance sales trends from 1968 to 1969 in the state of Washington and the United States are shown in Table V-2. Table V-3 presents a month-by-month comparison of department store sales in selected western cities.

TABLE V-1

AVERAGE PRICES OF MAJOR APPLIANCES
LOS ANGELES AND SEATTLE

Item	April, 1969			August, 1969			January, 1970		
	N	L.A.	Seattle	N	L.A.	Seattle	N	L.A.	Seattle
Dishwashers	4	$197	$198	4	$193	$194	9	$209	$218
Ranges	1	200	210	1	190	198	4	262	265
Washers	4	210	223	4	213	228	26	227	236
Dryers	2	182	162	2	183	173	12	194	204
T.V.	2	400	415	2	410	425	30	353	375
Refrigerator	6	363	371	6	362	372	34	354	359

Source: Field surveys.

TABLE V-2

FURNITURE AND APPLIANCE GROUP SALES[a]
WASHINGTON STATE vs. NATIONAL
(in millions of dollars)

	United States			Washington		
	1968	1969	Per Cent Change	1968	1969	Per Cent Change
1st Quarter	3663	3774	+3.0	62.8	62.5	- .6
2nd Quarter	3884	4084	+5.1	61.9	64.9	+5.0
3rd Quarter	4284	4144	-3.3	69.1	67.7	-2.0
4th Quarter	4709	4712	+.06	77.7	75.4	-3.0
Totals	16540	16714	+1.1	271.5	270.5	- .4

[a]Unadjusted for seasonal variation.

Source: Washington: Department of Revenue, Olympia. United States: Department of Commerce, "Survey of Monthly Retail Trade."

TABLE V-3

DEPARTMENT STORE SALES IN SELECTED AREAS (TABLE 10-UNADJUSTED
(Department of Commerce Monthly Sample Data)
(all numbers in thousands)

SMSA's	12 months 68 vs. 67	Dec. 68 Dec. 67	Jan. 68 Jan. 69	Feb. 68 Feb. 69	6 months Jan.-June 1968-1969	(1st Qtr.) Mar. 68 Mar. 69	April 68 April 69	May 68 May 69	(2nd Qtr.) June 68 June 69	July 68 July 69	Aug. 68 Aug. 69	(3rd Qtr.) Sept. 68 Sept. 69	Oct. 68 Oct. 69	(4th Qtr.) Nov. 68 Nov. 69	Dec. 68 Dec. 69	1968 vs. ANNUAL 1969
1. Los Angeles-Long Beach (Los Angeles County)	+5%	+6%	102260 106239 (+4%)	93174 96550 (+4%)	+6%	108874 116192	118717 127107	123908 130884	121142 130024 (+7%)	124955 137946	127015 139714	119502 131508	124276 134192	150256 160657	241784 269542	+8%
2. Eugene, Oregon (Lane County)	+7%	-3%	1777 1587 (-11%)	1745 1691 (-3%)	-2%	2183 2094	2137 2231	2287 2357	2357 2317 (-2%)	2390 2365	3015 2746	2541 2499	2268 2350	2556 2436	4137 4308	-1%
3. Salem, Oregon (Marion & Polk Counties)	+5%	-5%	1759 (+3%)	1648 (-4%)		2018 2064	2234 2259	2235 2313	2258 2260 (0)	2442 2405	3134 2847	2411 2429	2377 2486	2509 2533	4065 4228	+1%
4. Portland, Ore.-Wash. (3 Oregon Counties Clark County, Wn.)	+6%	+1%	10511 10806 (+3%)	10326 10204 (-1%)	+5%	12241 13212	12766 13957	13509 14659	13812 14115 (+2%)	13065 13752	16166 15888	13329 14297	14075 15378	16547 16523	25739 27813	+5%
5. Seattle-Everett, Wash. (King & Snohomish Counties)	+17%	+6%	21601 23166 (+7%)	20394 22753 (+7%)	+8%	25297 27604	26080 27839	28871 30859	27431 29793 (+9%)	27073 29397	35067	28891 30503	31128 32267	35816 36935	56398 62822	+7%
6. Spokane, Wash. (Spokane, County)	+10%	+19%	4426 4866 (+4%)	5016 4982 (-7%)	+9%	5693 6264	5795 6601	5996 7141	6583 6900 (+5%)	6160 6688	7676 7802	6797 6967	7789 8061	7734 7884	12578 13283	+6%
7. Tacoma, Wash. (Pierce County)	+19%	+1%	5661 5849 (+3%)	5956 5893 (-1%)	+6%	6790 7290	6954 7319	7925 8333	7233 8178 (+13%)	7484 7923	9059 9627	7704 8023	7957 8013	9527 9731	14966 15971	+5%
II. CITIES																
1. Bellingham, Wash.	+29%	+72%	(+40%) 390 545	(+31%) 391 511	+53%	487 744	525 757	558 910	510 907 (+78%)	529 848	663 1068	542 904	565 915	1069 1051	1522 1794	+41%
2. Seattle, Wash.	+11%	-4%	(+2%) 14001 14235	(-4%) 13177 12997	0	15676 15801	15739 15782	17482 17399	16242 16446 (+1%)	16404 16719	19964	16997 17562	18480 18602	20715 20580	31910 34196	+2%
3. Walla Walla, Wash.	+3%	-8%	(-2%) 309 302	(-5%) 322 306	+1%	433 406	425 441	439 458	420 431 (+7%)	432 420	489 484	412 406	428 423	460 412	687 701	-1%
4. Yakima, Wash.	+5%	(-2%)	(-4%) 1285 1239	(-7%) 1363 1266	+2%	1681 1736	1641 1725	1876 1875	1794 1913 (+8%)	1781 1834	2217 2174	1802 1957	2047 2136	2240 2178	3243 3430	+2%

Source: U.S. Department of Commerce: Current Business Reports--Monthly Retail Trade
(1968 and 1969—monthly issue)

As a general rule, price levels in the Seattle area seem to be somewhat higher than the Los Angeles area. This holds fairly consistently for all three periods, but it would be difficult to conclude increases have been more pronounced in Seattle during the 9-month period than in Los Angeles. One exception to this is dryers. There was about 1.5 per cent increase in August from April in Seattle, while the price remained unchanged in Los Angeles. Another exception is that dryers are the only appliance that showed a lower price level in the Seattle area during April and August. However, with only two identical models to compare, very little can be said about this difference. The January, 1970 survey conveys a greater confidence in the average price levels because of the larger number of identical appliances. Here, the price level still shows a trend similar to the two earlier surveys for all appliances.

Since our interest is in the general price level, a second approach to the collected data was the use of some kind of an aggregate price index of all appliances for the two cities. In combining all appliances, we obtained the following:

TABLE V-4

AGGREGATE PRICES OF MAJOR APPLIANCES
LOS ANGELES AND SEATTLE

	April		August		January	
	L.A.	Seattle	L.A.	Seattle	L.A.	Seattle
Total Price	$5166	$5274	$5172	$5314	$32785	$34062
Number of identical models	19	19	19	19	115	115
Average price per model	$ 273	$ 277	$ 273	$ 280	$ 285	$ 296
Seattle price as a percentage using L.A. as a base, each period	100	101	100	102.5	100	104
Percentage price change, using both cities as base	0%	0%	0%	1%	4%	7%
CPI--all items, nationally		126.4		128.7		131.3
CPI for household furnishings, nationally		116.9		118.5		120.0

Source: Field surveys.

The table above shows that prices in the Seattle area for appliances in general have increased at a somewhat higher rate than Los Angeles and the national average. This may be a matter of speculation, but there is no economic reason that would suggest a higher rate. In fact, economic conditions in Seattle should force an opposite trend since there was substantial unemployment in the Puget Sound area in January 1970. But with this type of limited information, we cannot conclude that Initiative 245 has been the cause of the price increase in the Seattle area. The difference is not significantly large enough for drawing such a conclusion. On the other hand, the relatively higher prices for appliances in Seattle does tend to corroborate the survey responses of the appliance retailers.

Auto Retailer Pricing

Since there are some characteristics of auto retailing which differ from those of other types of retailing, and because auto purchases are usually the second-largest single purchase items for consumers (purchase of a house is larger, of course, and for non-home-owners rent payments are normally higher than car payments), auto prices are considered separately. Further, it was possible to obtain certain kinds of data on autos not available for other forms of merchandise.

Tables V-5 and V-6 summarize the findings relative to auto price changes by dealers interviewed in our sample. These reflect changes that were said to have taken place during the first three months of 1969.

TABLE V-5

NEW CAR PRICE CHANGES
WASHINGTON STATE, FIRST QUARTER 1969

Type of Dealer	Amount Given	Average Increase of 5.3%	Average Increase of $56.-	Total Dealers	Per Cent
New car dealers				30	100%
Increased price	3	6	4	13	43
No price increase				17	57

TABLE V-6

USED CAR PRICE CHANGES
WASHINGTON STATE, FIRST QUARTER 1969

Type of Dealer	No Specific Amount Given	Average Increase of 11%	Average Increase of $64.0	Total Dealers	Per Cent
Used car dealers				46	100%
Increased price	5	9	5	19	41
No price change				27	59

Note: A new-and-used car dealer's response is recorded in Table V-5 with respect to his new cars, and in Table V-6 with respect to his used cars.

Almost one-half of the dealers in each category indicated price increases on the autos that were sold. The dealers apparently did not attempt to increase their revenue by means of increasing prices on other products or services. Only 4 out of 39 respondents indicated that they had done so. Three new-car dealers increased delivery charges by an average of $30 and one dealer increased his service contract charge by $2. For used cars, the change was primarily a price increase in the car purchased because some of the services offered to new car buyers are not usually offered to used car buyers. Four used car dealers (10 per cent) did reduce their warranty liability on service contracts by shortening their commitment time period or by changing service terms. However, an indirect price increase for both categories was levied by means of offering the prospective buyer a lower trade-in allowance for his old car. This practice was expressly mentioned by 4 or 5 dealers in our sample.

A more comprehensive investigation of price changes was made using secondary source data. Data were recorded for all the Chevrolet, Ford, and Plymouth models that were sold at the Seattle Auction during the periods January through August of 1968 and 1969. For purposes of comparison the same kind of data were secured from Denver, Colorado, where the 12 per cent interest restriction does not exist. These are wholesale prices which the dealers pay

for the cars they buy at the auction. The results are shown in Table V-7 which follows.

TABLE V-7

WHOLESALE AUCTION AVERAGE AUTO PRICES
SEATTLE AND DENVER
1968 and 1969

		Seattle		Denver	
Age	Model	Number Sold	Price	Number Sold	Price
1969					
0	69	543	$2554	198	$2570
1	68	1741	2179	503	1963
2	67	759	1493	842	1551
3	66	345	1140	453	1170
4	65	243	932	371	942
5	64	158	707	228	675
6	63	100	475	180	471
1968					
0	68	262	2497	69	2653
1	67	931	2164	384	1974
2	66	862	1506	547	1557
3	65	656	1193	393	1216
4	64	385	981	181	937
5	63	284	707	164	691
6	62	137	544	132	483

There seemed to be slightly lower wholesale prices in Seattle for older used cars in 1969 when compared to Denver. Although this sample covers a sufficiently large number of automobiles, no conclusions can be made about the behavior of these prices except that, in general, used car prices at the wholesale level are lower in 1969 than they were in 1968 in both cities. However, it will be recalled that 41 per cent of the Washington used car dealers interviewed stated that their prices increased at the retail level. When dealers pay less for their purchases, they might be expected to keep retail prices unchanged, or even to lower them and pass some of the benefit on to the consumer. Initiative 245 forced upon the dealer a loss of revenue from interest

income. Viewed in this light, his behavior may be more understandable. A price increase at the retail level, or even no price change for that matter, is one possible way of recouping interest income losses.

Although no average retail prices on these autos were available, this higher retail margin on used cars was substantiated from another sample that covered about 15 per cent of all used cars sold in the state of Washington. These unpublished statistics become more impressive when they are compared with similar retail prices in Oregon which does not have the 12 per cent interest limitation. The data show the dealers in Washington were making an average of $18 more on each used car sold in 1969 than in 1968. This represents a 13 per cent increase in 1969 over 1968. Dealers in Oregon were only making an average of $13 more, or 9 per cent. On new cars, dealers in Washington were making only $11 more (2.7 per cent), compared to Oregon's $23 (7.9 per cent). The reader will recall that of those dealers interviewed (Tables V-5 and V-6) 43 per cent of the new car dealers stated that they had raised prices by 5.3 per cent, whereas 41 per cent of the used car dealers raised prices by 11 per cent. These two samples are not strictly comparable since the interview survey covered the first quarter changes, whereas the second sample covered the whole of 1968 and 1969; however, the evidence in both takes the same direction.

This is not surprising. This phenomenon will be discussed more fully under the section on "Credit Availability." A brief explanation is that banks in 1969 were still willing to finance new or newer cars at 12 per cent. However, pressure was building on used-car financing. The results of this pressure in terms of the losses in finance income reported in our survey appear in Table V-8 below.

TABLE V-8

FINANCE INCOME FROM AUTOS

	% Increase or Decrease in 1969 from 1968	
	Used Cars	New Cars
Seattle	-41.7%	- 7.0%
Washington	-51.1	-13.7
Oregon	- 2.9	- 1.0

Several dealers expressed the opinion that this lack of financing availability was the cause of depressed prices at the wholesale level, especially, for older used cars. On the basis of such remarks, Table V-9 was revised in the following fashion:

TABLE V-9

AVERAGE WHOLESALE AUTO PRICES
SEATTLE AND DENVER, 1968 AND 1969

	1969		1968	
	Number of Cars	Average Price	Number of Cars	Average Price
Late model used cars (0,1,2,3 yr. olds)	3388 (1996)	$1980 ($1669)	2711 (1393)	$1752 ($1630)
Old model used cars (4,5,6 yrs. olds)	501 (779)	$ 770 ($ 755)	806 (479)	$ 810 ($ 724)

Note: Prices and number of cars enclosed in brackets are for Denver, Colorado.

The implications here seem fairly obvious. The older model car which a consumer purchases in Seattle costs him a relatively higher price than if he were to buy a later-model used car. One can safely assume that the majority of buyers of older used cars belong to lower income groups than those who can purchase newer model cars. If this is correct, the impact of Initiative 245 does not seem equally distributed, and its adverse effects are being borne by the lower-income consumer to a greater extent than by more affluent consumers.

Auto Sales Volumes

Published data that directly relates to the behavior of auto sales in Washington for purposes of a scientific analysis are scarce, and what is available leaves something to be desired for purposes of comparison with other state and national figures. Nevertheless, an attempt was made to assemble available information that is of some benefit in the presentation of an overall automobile market picture.

Few dealers in the survey volunteered information on their sales volumes. Of those few, five reported no change in the sale of new cars and nine reported that sales of used cars dropped by about 8 per cent in the first quarter of 1969 when compared with the same period in 1968, but no inferences can be drawn from figures obtained from such a limited response for purposes of analysis. The data obtained from the Department of Revenue for the State of Washington shows only a slight gain of 0.2 per cent in auto dealers' sales (unadjusted) for the year of 1969 over 1968 while the United States automotive retail sales grew 2.5 per cent.

TABLE V-10

AUTOMOTIVE RETAIL SALES[a]
WASHINGTON vs. UNITED STATES
(in millions of dollars)

	1967	1968	% Change Over 1967	1969	% Change Over 1968
Washington					
First Quarter	--	$222.592	--	$225.482	+1.3%
Second Quarter	--	$242.423	--	$256.619	+5.8%
Third Quarter	--	$238.536	--	$233.933	-1.9%
Fourth Quarter	--	$221.718	--	$210.942	-4.9%
Total Annual	$918.926	$925.269	+ 0.7%	$926.976	+0.2%
United States	$ 58,273	$ 65,261	+12.0%	$ 66,922	+2.5%

[a]Seasonally unadjusted sales include new and used car dealers plus tire, battery and accessory dealers.

Source: Washington: State Department of Revenue. United States: Automobile Manufacturers Association, "Annual Automobile Facts and Figures."

Table V-10 shows a substantial sales decline in the third and fourth quarters of 1969 that virtually wiped out any annual sales growth in Washington.

Numerically, the number of used cars reportedly sold in Spokane in the first quarter of 1969 was 12 per cent less than the same period in 1968, which

in magnitude agrees with published figures of 10.5 per cent decrease found for the three Spokane dealers included in this survey. However, Seattle showed a 5.5 per cent increase in the number of used cars sold at the auction for the first half of 1969 over the same period in 1968. Overall, this may suggest a slight depression of used auto sales in Washington. However, any depression may just as easily be in response to general economic conditions nationally. For instance, according to "Automotive News" sales of used cars in 1969 dropped 100,000 units below the 1968 total, but new car registrations were about 43,000 units above the 1968 level. It is not possible, therefore, statistically to isolate the effects of the passage of 245 from other economic variables when potentially the degree of change is this small, when subscribing to the assumption that the trend of auto sales in Washington should more or less follow the national trend.

Dealership Terminations

Information gathered from dealers during last summer's survey shows that in an effort to cut costs and to survive, one new and used car dealer mentioned that he had to release eight salesmen. Another used-car dealer reported that both cash and credit sales were down, and the only way he was able to stay in business was by terminating the services of one full-time and two part-time salesmen. A third new and used auto dealer advertised close-out sales and mentioned specifically in his advertisements that one of the main reasons for going out of business was Initiative 245. A manager of a new and used car dealership said that his former used car business had to be terminated, and that now he was working on a salary for another dealer. He also mentioned the names of five dealerships that had gone out of business. These and a few others were brought to our attention during interviews with automobile dealers. A fifth used car dealer confided that he expected to be forced out of business in a few months because of Initiative 245. Since the interview period in the summer of 1969 some other dealerships were terminated.

Opinions expressed in the press by businessmen blamed Initiative 245 for auto industry problems. For example, during a panel discussion in a statewide press conference, Mr. Jenkins, Chairman of the Board of Seattle-First National Bank stated, "Washington State's Initiative 245 has made credit card business

unprofitable, is forcing auto dealers out of business, is damaging the real-estate industry, and must result in higher prices."[1] There was disagreement with the above contentions from another source. Joe Davis, President of the Washington State Labor Council responded by listing several factors that have influenced business, "Boeing has reduced its work force by almost 17,000; the national administration has deliberately set out to increase unemployment as an anti-inflationary weapon; construction starts have declined some 30 per cent, and inflation has cut into the wage gains received by the working men and women of the state."[2]

The president of the Seattle Automobile Dealers Association, Pat Goodfellow, has indicated several possible reasons for the closure of three or four major dealerships in the Seattle area in the past year, the reorganization or regrouping of seven or eight more and the failure of "countless" used-car dealers: high inventories; a cost of financing those inventories that "is out of sight"; increasing overhead; growing size of dealerships; a sluggish response to rapidly changing economic conditions; the credit squeeze created by rising interest rates charged dealers while Initiative 245 limits dealer interest charges to buyers to 12 per cent per year; the area's economic slowdown. "Initiative 245 would have been more tolerable under the interest rates we had three or four years ago," Goodfellow said.[3]

In reviewing the records of the Department of Motor Vehicles in Olympia during the months of June through December (no records were available for earlier months in 1968), it was learned that there were 171 new dealership applications in 1968 and 174 in 1969. In looking at the number of cancellations of dealer licenses for the same period, there were only 119 terminations in 1968 compared to 201 in 1969. (These data appear below in Table V-11.) One would suppose that the bulk of these are used car dealers. Usually, a business that deals with new cars has stronger financial backing.

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[1] *Seattle Times*, October 8, 1969.

[2] *Seattle Times*, January 11, 1970.

[3] *Seattle Times*, December 18, 1969.

TABLE V-11

NEW LICENSES AND TERMINATIONS OF AUTO DEALERSHIPS
JUNE TO DECEMBER, 1968 AND 1969

	1968	1969	Total
New Applications	171	174	345
Terminations	119	201	320

As far as the consumer is concerned, this may be a healthy sign if these businesses are terminated because of inefficiencies and high operating costs. But if Initiative 245 is the cause of such an adverse impact in this area, the consumer, in the long run, will have fewer alternatives and choices. His bargaining power may be reduced, and he may become "captive" to fewer competitors. The passage of time will be required to determine whether this decrease in competition injures consumers.

A Chi-square test was run on this data to determine whether there was a significant difference in the proportion of terminations between 1968 and 1969. The results give us a value of Chi-square equal to 11.03. This is significant at the 0.01 level.

The reader is cautioned that no claim is made that this significant increase in dealership terminations is due to Initiative 245 alone. Economic conditions in Seattle, high interest rates, and the general auto market can also be considered as contributing factors.

The reporting of dealership cancellations and new applications in Olympia is made on a monthly basis. As mentioned earlier, only the last seven months of 1968 were available, but all twelve months of 1969 could be obtained. These were as follows in Table V-12.

These monthly data present an interesting phenomenon. We suggest that a market which is in equilibrium, or which is in a reasonable position profitwise, will show a positive reaction manifested by new entries in response to exits out of the market. If the industry is in equilibrium, we should theoretically expect the number of new entries to correspond to the number of terminations

TABLE V-12

NEW LICENSES AND TERMINATIONS OF AUTO DEALERSHIPS
JANUARY TO DECEMBER, 1968 AND 1969

	1968		1969	
Month	Terminations	Applications	Terminations	Applications
January	--	--	19	37
February	--	--	34	32
March	--	--	36	31
April	--	--	20	32
May	--	--	31	41
June	0	36	27	20
July	14	19	27	41
August	0	34	27	34
September	42	16	43	23
October	20	29	32	22
November	37	17	35	23
December	6	20	10	11

Source: Washington State Department of Motor Vehicles

and, in fact, in a profitable market, new entries should even exceed exits until an equilibrium is reached. This suggested the application of a rank correlation test between the number of cancellations and the number of entries. After consideration of several alternatives, it was found that using a one-month lag in new applications for both 1968 and 1969 gave the best fit. This can be justified in terms of the real world situation. We cannot realistically expect new applications to respond to terminations spontaneously. Some such

cases may exist, but the majority of new entries would reasonably lag behind terminations. Not only does the process involve search and investigation on the part of the new applicant, but also the administrative procedures of licensing consume some time. On the basis of a one-month lag, the correlation coefficient for the last seven months of 1968 was a positive 0.56, and for the twelve months of 1969 was a negative 0.62.

The correlation coefficient for 1968 is not significant at the 0.05 level (it would have become significant if its value was 0.67, or if we had all 12 months of 1968), but it should not be completely disregarded. Actually it is the sign of the coefficient rather than the magnitude which is of most interest. The positive value in 1968 suggests that a high number of cancellations was associated with a similar number of new applications. And when cancellations were low, new applications were likewise. Such response is likely to happen in an equilibrium market.

Turning to the negative correlation coefficient in 1969, we find it significant at the 0.05 level. The negative sign can have two possible explanations with respect to the magnitude of exits and new entries. If low exits are accompanied by high new entries, the market would have to be highly profitable for such behavior to manifest itself. But the lack of increase in new applications in 1969 over 1968 (for the last 7 months of both years where a comparison can be made) does not support such an assumption. On the other hand, the negative sign can also mean that high cancellations are accompanied by low new entries, an indication of a depressed market. Such an assumption would have more support when we recall that for the last seven months of 1968 terminations amounted to 119, and in 1969 for the same period they were 201.

Again, no implication can be made that the depressed market is solely due to the effect of Initiative 245. It is necessary to remain aware of other economic factors in 1969 both on the national and local levels.

The standard deviation from regression shows a value of about 0.24. If the residuals from the true regression line are normally distributed, then b is normally distributed also with mean B and standard deviation equal to 0.24

To test the hypothesis that $B = B_o$, i.e. to see if the value of the coefficient is significant and makes a contribution in explaining new applications, we can use the t ratio:

$$t = \frac{b - B_o}{s_b} \qquad \text{with } n - 2 = 10 \text{ degrees of freedom}$$

$$t = \frac{0.58 - 0}{0.24} = 2.41$$

This value of t is significant at the 0.05 level. ($t_{.05(n-2)} = 2.23$) The coefficient of determination (R^2) is only 0.36. In other words we can attribute only 36 per cent of the variation in applications to cancellations. This value suggests the presence of other variables such as disposable income, employment, . . . etc. that may help explain the remainder of this behavior. It is proposed, therefore, that if further work is done in this area, a more comprehensive analysis of other economic variables may shed further light on this situation.

Leasing. At the time of the field interviewing program, it was not possible to discern any significant shift toward leasing programs in response to Initiative 245. There were only four automobile dealers who indicated that they were attempting to promote leasing, and two additional dealers expressed plans to promote leasing in the future. It seems logical that more dealers might move to leasing programs since the law does not regulate this activity. Of the dealers interested in leasing, however, several mentioned that they were interested in leasing for "its own sake" and not because of Initiative 245.

Data from a number of banks which finance dealer leasing of automobiles (Table V-13) show that in 1969 the number of leases financed increased by about one-sixth, and the dollar volume of lease financing increased by one-third over 1968. The average dollar size of the leasing finance contracts increased by about one-sixth.

In early 1970, there was an increase in the number of auto dealer advertisements which stressed leasing. Several of these presented two options: a long-term lease at a relatively low rate with no mileage charge, and a lease-purchase plan with higher rates and a mileage charge and specific purchase prices consumers would pay on conversion of the lease to a purchase. At this juncture, the lease plans appear more as positive sales devices than as defensive responses to financing problems created by the interest limitation law.

TABLE V-13

AUTOMOBILE LEASING
A SAMPLE OF BANKS FINANCING LEASING PLANS
STATE OF WASHINGTON
(thousands of dollars)

	1968		1969		Percentage Change	
	Number	Dollar Volume	Number	Dollar Volume	Number	Dollar
New	3503	13,093	4040	17,439	+15.3%	+33.2%
Outstanding	7310	19,698	8571	24,727	+17.2%	+25.5%

Average Dollar Size of Contracts

New:	1968	$3738	Percentage Change = +15.5%
	1969	$4317	
Outstanding:	1968	$2732	Percentage Change = +5.6%
	1969	$2885	

For consumers, the main attraction of the leasing plans appears to be the opportunity to start driving a new car without a downpayment. The long-term lease plans have the additional advantage that the rental costs are as low as, or lower than, normal monthly payments on outright purchase. Perhaps the most significant change observable is that leasing formerly seemed aimed at business and professional customers, whereas the current advertising is aimed at consumers. With available evidence, it is not possible to attribute increases in leasing to Initiative 245.

Summary

In this chapter on product related responses of retailers, it has been pointed out that retailers who have suffered losses in credit income or who have seen credit revenues turn into credit losses can be expected to make up these

losses in other ways. Some of the ways relate directly and indirectly to the handling of credit itself and are discussed elsewhere. This chapter concerns itself with product related policies and decisions such as pricing, pricing of ancillary services, adjusting assortments, changing gross margin rates and/or generally improving merchandising efficiency.

The first product-related hypothesis posited in this study was, "Prices of merchandise frequently sold on credit have gone up." The majority of retailers responded that they had raised prices on all merchandise to make up for their losses on Initiative 245. Others raised prices on specific items usually sold on credit. In either case, the price rises negated the proposed benefits of the law, which were to lower the cost of credit and provide a net saving to consumers. Where prices were raised only on credit-sensitive items, the credit customer paid more for the goods. Where all prices were increased, the credit customer had to pay more for everything he bought in the store, whether he in fact charged everything he bought. The cash customer, of course, subsidized the credit customer by paying all of the price increases and receiving none of the benefits of interest limitation.

In addition to direct price changes, retailers sought to lower costs and increase revenues by instituting charges, or raising the level of charges, on ancillary services such as check cashing, wrapping and packaging, delivery, product installation, product service contracts, lay-away and parking.

In auto retailing, it was possible to get some external verification of the respondents assertions that prices had gone up on both new and used cars, but that they had gone up relatively more on older used cars. Even where prices may have remained stable, auto dealers were able to raise their gross margins on these older cars because their wholesale prices had declined. Further, higher gross margins were achieved by allowing relatively low trade-in allowances.

The second hypothesis was: "Different products and different businesses have been affected in different ways by the new laws." It can be seen in this chapter that items usually or frequently bought on credit, particularly autos, furniture and appliances, have been affected differently than items normally purchased for cash. Considerable adjustments were in evidence in the sale and financing of "credit-sensitive" items. In many cases, the actions of

respondents to raise prices to make up for lost interest revenue fell equally on all products in retail stores; i.e., the majority of the respondents raised prices on all merchandise. Other businesses raised prices on the credit types of items themselves. Still other merchants felt that the nature of competition on items such as major appliances prevented raising prices on these items. They were concerned that consumers could compare prices too readily, and that sales would be lost. In the auto retailing industry, there were differences between dealers and between products. Prices were raised proportionately more on used cars than on new cars, and gross margins were increased more on the used cars. In the sections of this report on financing, it is pointed out that banks quit financing cars older than a specified number of years, and this created special problems for businesses and consumers. The incidence of retailer mortality fell most heavily on used car dealers, and there were cases of new car dealers blaming Initiative 245 as one cause of going out of business. There were no cases reported of retailers other than auto dealers who failed in business as a result of Initiative 245, although there may have been some.

A third hypothesis was, "Leasing of merchandise frequently sold on credit has increased." The provision of leasing options by new car dealers appeared to increase, but it was not possible to attribute this to Initiative 245. There was no apparent increase in leasing of other consumer products.

The auto data supports conclusions in other parts of this study that the impacts of the Initiative fall more heavily on the lower income consumers. Other portions of the study show that credit became less available to lower income people and that they were likely to pay a much higher interest rate if they were able to get credit at all. The analysis of auto pricing demonstrated that prices on older autos have increased proportionately more than prices on newer autos. Since it is logical to assume that older autos are bought principally by lower income, less creditworthy consumers, the consumers at the bottom of the scale suffer on both the price of autos and on their costs of credit.

The increase in dealer mortality and the apparent decline in new business formations to replace failing businesses may not seem of immediate concern to consumers. Yet, for whatever effect this has on consumer welfare, the trend definitely represents a diminution of competition in auto retailing.

CHAPTER VI

GENERAL CONCLUSIONS

The conclusions are summarized in the Summary of Findings at the beginning of this report (Chapter II). In general, it can be stated that the impacts of Initiative 245 reached consumers primarily through the medium of business responses to the law. Businesses which dealt in consumer credit tended to lose revenues and profits because of the 12 per cent per year limit on the charge they could make for credit. The defensive measures taken by businesses involved increasing costs for some or all consumers and making credit more difficult for some to obtain. The law provided a rationale for raising prices, tightening upon credit, and other practices detrimental to consumers. Those who expected benefits from the Initiative probably did not foresee such effects on consumers.

Poor people were hurt most by the effects of the law. Some of them formerly able to obtain credit from certain sources were shut off from these sources. Some were unable to make purchases because their credit applications were refused. Some auto customers probably were shut out of the market because they could not make the increased downpayments or the monthly payments on shortened maturities. Some who obtained credit paid more for it than they would have paid for it before the law was passed.

Some cash customers were forced to subsidize credit customers through paying relatively higher prices for goods purchased. Some creditworthy customers pay more interest than before the law because their free credit time periods have been reduced. Some creditworthy customers of stores which, on the goods these customers bought did not raise prices enough to counterbalance losses in credit revenue, may have received a net reduction in the total cost of buying on credit. Those who benefited most were those who could buy merchandise on credit at less of a price increase than the drop in credit revenues and who did not buy anything in credit-granting stores for cash.

There were, of course, significant changes occurring in other economic factors during the period of the study. Many of the actions taken by retailers and financial institutions might have been influenced to some extent by tight

money, the increasing prime rate of interest, deteriorating economic conditions and inflation. The fact that a recession was developing in the state of Washington affected the external data used to verify the impacts of Initiative 245. The unemployment rate which was rising, particularly in the Seattle area, and the consequent weakening in incomes and demand, undoubtedly induced some measures quite the opposite of initial responses to the Initiative--and some measures which took the directions to be expected in response to the Initiative.

Additional research which might provide useful information would be to follow up on price movements over extended periods of time. Toward the end of this study it was found that certain sources of price information might be available for periods of several years. The same sources could provide data on downpayments and maturities. Further, although tests involving consumer interviews proved a failure in this study because of the inaccuracy of consumer answers, some means might be devised to derive meaningful information from consumer interviews.

If additional time and resources were available, relevant information might be obtained from a more detailed study of automobile data. For example, studies of the legal ownership of autos might show changes in financing patterns. Consumer interviews of persons whose cars were recorded as purchased through consumer finance companies might provide data on the practice of "mooring" (the use of multiple personal loans not formally connected with the auto purchase to put together auto downpayments).

Finally, if the law is changed again to allow higher interest or service charges on consumer credit, a follow-up study could more fully determine the relationships between rate limitation and its impacts.

APPENDIX

EXPLANATION OF TERMS*

Consumer finance company (or "small loan company"). Consumer finance companies are firms set up under special legislation to make it easier for people with relatively poor credit standings to borrow money. In the state of Washington, these firms are permitted to charge three per cent per month (36 per cent annual interest) on loans up to $300, one and one-half per cent (18 per cent annual) on loans between $300 and $500, and one per cent per month (12 per cent annual interest) on loans over $500. Loans may be made directly to consumers or may be made indirectly through retailers.

Sales finance companies. Sales finance companies (also called "captive finance companies") are set up by manufacturers to provide indirect financing for retailers of their products, although they may finance the sale of products other than their own. Examples include General Motors Acceptance Corporation and General Electric Credit Corporation.

Direct loan. The terms "direct loan," "personal loan" and "consumer loan" are generally used interchangeably in this report to apply to a loan having the following characteristics:

1. it is made to a consumer;
2. it is made by a specialized financial institution, such as a bank or small loan company;
3. it is made for a designated purpose;
4. the maximum amount is limited by the policy of the lender and, in most states, by statute; and
5. it is to be repaid in installments.

For a more detailed explanation of terms, see: Robert H. Cole, *Consumer and Commercial Credit Management*, Third edition (Homewood, Illinois: Richard D. Irwin, 1968); Elvin F. Donaldson and John K. Pfahl, *Personal Finance*, Fourth edition (New York: The Ronald Press, 1965); and Richard P. Ettinger and David E. Golieb, *Credits and Collections*, Fifth edition (Englewood Cliffs, New Jersey: Prentice Hall, 1962).

Indirect loan. "Indirect loans" are loans made by financial institutions to finance merchants' sales of durable goods--such as automobiles and household appliances--on the installment plan. The operation is, in effect, "indirect lending" by the financing agency to the consumer.

In "indirect" financing of installment sales, the prospective customer makes application for credit to the dealer or merchant, not the financing agency. The dealer interviews the customer and collects the basic credit information. He then clears the application with the financing agency, which usually makes a credit investigation, although the dealer may himself perform this task.

The customer has no contact with the financing agency until after the sale is made--the merchant handles all the details of the transaction in much the same way that an installment sale is made in a department store. The customer usually makes a downpayment, and agrees to pay the balance of the sale price, plus credit costs, in equal installments. He signs a promissory note and a conditional sales contract, chattel mortgage,* or bailment lease.*

The indirect lending activities of small loan companies are generally referred to as the purchase of conditional sales contracts, while indirect lending activities of banks are generally designated as indirect loans.

Recourse plans. Sales finance companies and banks finance retail instalment sales under several different "recourse" plans.

(a) No-recourse or non-recourse plans place all the risk on the financing institution. If the customer (debtor) defaults, the agency repossesses the goods and stands any loss. Dealers operating under no-recourse plans are generally inclined to submit to their financing agency the credit applications of all prospective customers except obviously impossible risks. Consequently, financing agencies generally limit no-recourse plans to dealers and retail customers with

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*When one purchases goods and executes a chattel mortgage as security for the purchase price, title to the goods passes from the seller to the buyer as a consequence of the sale and back to the seller by virtue of the chattel mortgage. The seller thus holds legal title until final payment is made. In the bailment lease, title to the goods remains with the seller until the final payment has been made and then it is purchased for a nominal sum which is usually waived by the seller. When the conditional sales agreement is used, title to the goods remains with the seller until the last payment has been made.

good credit ratings. (As a general rule, finance companies handle retail instalment sales under this plan.)

(b) Limited recourse plans divide the credit risk between the retail dealer and the financing agency.

(c) Full recourse plans place all the credit risk on the retail dealer. If the customer (debtor) defaults, the financing agency reassigns the contract to the dealer, who bears whatever losses are involved. (As a general rule, banks finance retail installment sales under this arrangement.)

Credit life insurance. While there are several variations of credit life insurance, the basic objective is always the same--it is meant to assure full payment of a loan in the event of the death of the buyer. Health and/or accident provisions are sometimes included in the policies or else in separate insurance policies.

Participation. The term "participation" refers to the practice whereby a financial institution shares the interest proceeds from an indirect loan or a conditional sales contract with the retail dealer. Thus, on an indirect loan of $100, the dealer receives from the financial institution $100 plus a certain percentage, generally called "participation rate," of the interest on the loan.

Discount. The term "discount" refers to the practice whereby a financial institution charges the dealer a certain rate per annum for making an indirect loan or purchasing a conditional sales contract. Thus if a small loan company buys a $100 conditional sales contract, it will pay the dealer not the face amount of the contract, but rather $100 less whatever annual rate of discount it is charging at that particular time. (If a 3 per cent annual discount is charged, the dealer will receive $97, assuming the contract has a one year maturity. If the contract has a two year maturity, the dealer will receive $94.)

Flipping. The term "flipping" refers to the practice among loan companies of converting a conditional sales contract to a direct loan. While a maximum simple interest rate of 1 per cent per month can be charged on a conditional sales contract as a result of Initiative 245, a simple interest rate of 3 per cent per month can be charged on direct loans of amounts less than $300, 1½ per cent per month on amounts between $300 and $500, and 1 per cent per month on amounts over $500.

Mousing. The term "mousing" is used in the retail auto industry to denote the practice of dealing with consumers who are unable to make downpayments. The consumers are sent to two or more consumer finance companies to obtain a series of small personal loans. These loans are not connected formally with the auto purchase, and the auto is used as collateral only on the balance remaining after the downpayment is made. In the state of Washington, the remaining balance--as a retail purchase--incurs a maximum interest rate of 12 per cent per year, but the series of personal loans used to put together the downpayment may cost the consumer as much as 36 per cent annual interest.

Questionnaires

ECONOMIC IMPACT OF INITIATIVE 245 - SURVEY

AUTO DEALERS

1. Type of Dealer: Please check category which best describes your operation.

   a. _____New and used vehicles

   b. _____Used vehicles

Firm: _____

Name of Person(s) interviewed: _____

Position: _____

Address: _____

Phone: _____ _____

Date of Interview: _____

No. _____

ECONOMIC IMPACT OF INITIATIVE 245

QUESTIONNAIRE FOR AUTO DEALERS

This group of questions will deal with changes you may have made in direct response to Initiative 245 (either the passage of the initiative or its taking affect on 12/5/68) when dealing with consumers.

Circle Response

1. Have you increased the average selling prices on

   a) new vehicles — Yes No

   b) used vehicles — Yes No

   If yes, by how much?* _____
   (*trade-in price change?)

2. Have you increased prices on other items in response to Initiative 245 (i.e., parts, service, TBA)? Yes No

   If yes, identify _____

   _____

3. With respect to the following product related charges, do you charge for

	No Change	Prior to Initiative 245 (before 12/5/68)		Amount	In Response to Initiative 245 (since 12/5/68)		Amount
a) product delivery	_____	Yes	No	$_____	Yes	No	$_____
b) service contracts	_____	Yes	No	$_____	Yes	No	$_____
c) product guarantees (warranties)	_____	Yes	No	$_____	Yes	No	$_____

   d) other product related services

   Identify _____
   (handling, check cashing, make ready, etc.)

   Comment:

4. With respect to the following credit related fees and policies, do you require

	No Change	Prior to Initiative 245 (before 12/5/68)			In Response to Initiative 245 (since 12/5/68)		
				Amount			Amount
a) a service fee (minimum)	_____	Yes	No	$_____	Yes	No	$_____
b) a loan fee	_____	Yes	No	$_____	Yes	No	$_____
c) an investigation and credit report fee	_____	Yes	No	$_____	Yes	No	$_____
d) credit insurance	_____	Yes	No	$_____	Yes	No	$_____
e) cash/credit differential	_____	Yes	No	$_____	Yes	No	$_____
f) late payment fee	_____	Yes	No	$_____	Yes	No	$_____

g) other? Identify _____

_____

Comment:

5. In response to Initiative 245 do you now promote auto leasing instead of purchasing?

Circle Response

Yes No

Comment:

6. Do you intend to promote more auto leasing in response to Initiative 245?

Yes No

If yes, why?

7. What is your policy with respect to recourse on credit paper.

Before passage of Initiative 245:

If yes, to what extent _____

In response to Initiative 245:

If yes, to what extent _____
(repurchase agreements)

8. When selling paper to banks, what was the participation rate or discount rate

   Prior to Initiative 245? _____

   In response to Initiative 245? _____

   Comment:

9. Have you changed the credit eligibility rules for consumers in order to reduce expected losses in response to Initiative 245?

   Yes No

   Specify rules changed: New: _____

   Used: _____

10. Do you now reject applicants for credit whom you would have accepted before Initiative 245 took affect?

	Prior to Initiative 245 (before 12/5/68)	In Response to Initiative 245 (since 12/5/68)
Yes____ No____ Rejection rate:	_____	_____

   If yes, why?

11. Do you now advertise or promote the availability of credit (same____ more____ less____) in response to Initiative 245?

   What have you done?

12. As far as you can determine, what has been the impact of Initiative 245 upon consumers?

13. For border cities

   a) To your knowledge, have local customers increased their purchases from out of state

      in response to Initiative 245: Yes____ No____

      in response to Initiative 245: Yes____ No____

14. Would you please give us a sample of the type of consumers you rejected as marginal credit risks? (names)

   Prior to Initiative 245

   In Response to Initiative 245

15. What is the minimum downpayment as a percent of price you require from credit buyers in the following situations?

		Prior to Initiative 245	In Response to Initiative 245
superior credit risk:	new vehicles	_____%	_____%
	used vehicles	_____%	_____%
average credit risk:	new vehicles	_____%	_____%
	used vehicles	_____%	_____%
below average credit risk:	new vehicles	_____%	_____%
	used vehicles	_____%	_____%

16. Capacity to pay at time of application: What were the monthly payments as a percentage of monthly take-home pay which best describe your marginal consumer credit applicant?

Prior to Initiative 245

In Response to Initiative 245

17. What per cent of your consumer auto financing is done by:

	Prior to Initiative 245		In Response to Initiative 245	
	New	Used	New	Used
Your firm	____	____	____	____
Banks	____	____	____	____
Finance Companies	____	____	____	____

18. What is your average credit turnover?

	1st Qtr. 1968	1st Qtr. 1969
Credit sales	_____	_____
Accounts Receivable	_____	_____

Comment:

19. Number of Loan Payments: What was the percentage of loans with the following maturities?

	Prior to Initiative 245		In Response to Initiative 245	
	New	Used	New	Used
Single payment	____	____	____	____
6 months	____	____	____	____
12 months	____	____	____	____
24 months	____	____	____	____
36 months	____	____	____	____
More than 36 months	____	____	____	____

20. What dollar volume of your business was done:

	1st Qtr. 1968		1st Qtr. 1969	
	New	Used	New	Used
on cash basis	____	____	____	____
on leave basis	____	____	____	____
on credit basis	____	____	____	____
total sales	____	____	____	____

21. Has your finance income changed?

	1st Qtr. 1968	1st Qtr. 1969
a) Gross finance income	____	____
b) Bank or finance company discounts (costs)	____	____
c) Net finance income	____	____

Comment:

ECONOMIC IMPACT OF INITIATIVE 245

RETAIL ESTABLISHMENTS

I. Type of Retailer: Please check the one category and sub-category(s), where appropriate, which best describes your operation.

a. _____ general merchandise store
   _____ department store
   _____ limited price variety store
   _____ miscellaneous general merchandise store

b. _____ apparel, accessory store
   _____ men's clothing, accessories
   _____ women's clothing, accessories
   _____ family clothing, accessories
   _____ shoe store
   _____ other apparel, accessories

c. _____ furniture, home furnishings
   _____ furniture, home furnishings
   _____ household appliance, radio, television, music store

d. _____ retail hardware

e. _____ home and auto supply

f. _____ other (please list the three most important items.)

   _____

   _____

   _____

Firm: _____

Name of Person(s) interviewed: _____

Position: _____

Address: _____

Phone: _____

Date of Interview: _____

No. _____

ECONOMIC IMPACT OF INITIATIVE 245

QUESTIONNAIRE FOR RETAILERS

1. What kinds of credit do you extend to consumers?

	Prior to Initiative 245 (before 12/5/68)		After Initiative 245 (since 12/5/68)	
a) installment credit	Yes	No	Yes	No
b) revolving credit	Yes	No	Yes	No
c) open book credit	Yes	No	Yes	No
d) bank credit cards	Yes	No	Yes	No
e) other _____				

2. Since the passage of Initiative 245 (11/68) have you encouraged the consumer to switch from one form of credit to another? Circle One: Yes No

If yes, switch from _____ to _____

_____ to _____

Comment:

3. Have you in response to Initiative 245 selectively increased prices Circle One

a) on credit sensitive items (those usually bought on credit)? Yes No

b) on all merchandise? Yes No

c) Other _____
(specific items for example)

d) comment:

4. With respect to the following product related charges, do you charge for:

	Prior to Initiative 245 (before 12/5/68)			After Initiative 245 (since 12/5/68)			No Change
			Amount			Amount	
a) product delivery	Yes	No	_____	Yes	No	_____	_____
b) product installation	Yes	No	_____	Yes	No	_____	_____
c) product returns	Yes	No	_____	Yes	No	_____	_____
d) service contracts	Yes	No	_____	Yes	No	_____	_____
e) product guarantees (warranties)	Yes	No	_____	Yes	No	_____	_____
f) other product related services							

Identify _____

(handling, packaging, wrapping, check cashing, etc.)

Comment:

5. With respect to the following credit related fees and policies, do you require

	Prior to Initiative 245 (before 12/5/68)			In Response to Initiative 245 (since 12/5/68)			No Change
			Amount			Amount	
a) a service fee (minimum)	Yes	No	_____	Yes	No	_____	_____
b) a loan fee	Yes	No	_____	Yes	No	_____	_____
c) an investigation and credit report fee	Yes	No	_____	Yes	No	_____	_____
d) credit insurance	Yes	No	_____	Yes	No	_____	_____
e) cash/credit differential	Yes	No	_____	Yes	No	_____	_____
f) a one-time set up fee for new accounts	Yes	No	_____	Yes	No	_____	_____
g) late payment fee	Yes	No	_____	Yes	No	_____	_____
h) changed loan maturities	Yes	No	_____	Yes	No	_____	_____
i) other? Identify							

_____

(e.g., filing fee)

Comment:

6. Have you changed the average down payment/sales price ratio <u>in response to Initiative 245</u>?

		From	To
Yes	Increase	_____%	_____%
	Decrease	_____%	_____%
No, remains unchanged			

Comment:

7. Have you <u>in response to Initiative 245</u> reduced the actual time period of

a) service contracts Yes No

b) merchandise guarantees and warranties Yes No

Comment:

Do you carry your own retail sales financing? Yes No

If no, go to question 11.

8. Have you <u>in response to Initiative 245</u> changed the average time periods over which you are willing to extend credit?

		From	To
Yes	Increase	_____ mos.	_____ mos.
	Decrease	_____ mos.	_____ mos.
No, remains unchanged.			

Comment:

9. Do you now reject applicants for credit whom you would have accepted before Initiative 245 took affect?

			Prior to Initiative 245 <u>(before 12/5/68)</u>	In Response to Initiative 245 <u>(since 12/5/68)</u>
Yes	No	Rejection Rate	_____	_____

If yes, specify rules changed _____

_____

Comment:

10. What proportion of your total consumer credit sales is financed through

	Prior to Initiative 245 (1st qtr. 1968)	After Initiative 245 (1st qtr. 1969)
a) your firm	_____%	_____%
b) bank loans	_____%	_____%
c) bank cards	_____%	_____%
d) finance companies	_____%	_____%

Comment:

11. Has your total volume of sales changed? Compare the first quarter of 1968 with the first quarter of 1969.

	1st Qtr. 1968	1st Qtr. 1969
a) volume of total sales	$_____	$_____
b) volume of credit sales	$_____	$_____
c) ratio of credit/total sales	_____%	_____%

Comment:

12. Has your finance income changed? Compare the first quarter of 1968 with the first quarter of 1969?

	1st Qtr. 1968	1st Qtr. 1969
a) Gross finance income	$_____	$_____
b) Bank or finance company discounts (costs)	$_____	$_____
c) Net finance income	$_____	$_____

Comment:

13. What is your average credit turnover?

	No Change	1st Qtr. 1968	1st Qtr. 1969
Credit Sales	_____	_____	_____
Accounts Receivable (As of March 30)	_____	_____	_____

Comment:

14. To your knowledge, have local customers increased their purchases from out of state

    In response to Initiative 245: Yes_____ No_____

    In response to other factors: Yes_____ No_____

15. As far as you can determine what has been the impact of Initiative 245 upon

    a) consumers? _____

    _____

    b) your own business? _____

    _____

16. Please give us a sample of the type of consumers you rejected as <u>marginal credit risks</u>? (Names)

    <u>Since the passage of Initiative 245</u>

17. Capacity to Repay: What were the monthly payments, <u>at time of application</u>, as a percentage of monthly takehome pay which best describes your <u>marginal</u> consumer credit applicant?

    <u>Prior to Initiative 245</u>

    <u>In response to Initiative 245</u>

ECONOMIC IMPACT OF INITIATIVE 245 - SURVEY

CONSUMERS

(Note: This questionnaire was used experimentally but was found to be unproductive.)

Hello. I am _____. I am a Research Assistant in the Graduate School of Business Administration at the University of Washington. We are conducting a study to determine what the impact of Initiative 245 has been upon the consumers in our state. You may recall that this Initiative reduced the maximum allowable interest rate charged for consumer credit from 18 per cent (1½ per cent per month) to 12 per cent (1 per cent per month). We are interviewing consumers like yourself and we need your help in answering a few questions to see how this new law is working out.

ECONOMIC IMPACT OF INITIATIVE 245 - SURVEY

CONSUMERS

Since the passage of Initiative 245 in December 1968:

Circle Response

1. Have you attempted to purchase an appliance, furniture, or car? Yes No

2. Did you finally purchase the item? Yes No

   a) If no, was it because you could not obtain financing? Yes No
   Please explain. _____

   _____
   (fine out avenues he attempted)

   b) If yes, what was the item(s)? _____ new____
   used ____

   (1) If used, did you first intend to purchase a new item? Yes No

   (2) Explain (could obtain lesser financing) _____

   _____

3. How did you pay for the item?

   a) cash_____ If cash, savings_____ cash on hand_____

   b) why cash?

   c) credit_____ Who financed it? _____
   (retailer?)

   d) If not financed by retailer, was it your first choice? Yes No

   e) If no, explain _____

   _____

4. Do you have a revolving charge account? Yes____ No____

   If no, have you recently applied for one? Yes____ No____

   Comment:

5. Have you had any credit privileges denied? Yes____ No____

   By retailer? _____

   Bank _____

   Finance company _____

   Were you given a reason? Yes____ No____

   What was the reason?

6. Have retailers encouraged you to lease the item rather than purchase it?

   Yes____ No____

7. If a retailer refused you credit, were you encouraged to obtain the whole _____ or part _____ of the amount from another source? Yes____ No____

   If yes, who? Bank____ Finance Company____ Other____

8. This time last year, was it easier for you to get credit before passage of Initiative 245? Yes____ No____

ECONOMIC IMPACT OF INITIATIVE 245 - SURVEY

FINANCIAL INSTITUTIONS - FINANCE COMPANIES

I. Type of financial institution: Please check the one category and sub-category, where appropriate, which best describes your operatio:

a. _____bank

_____federal charter

_____ branch

_____state charter

_____branch

_____mutual savings

b. _____finance company

_____branch

c. _____credit union

d. _____savings and loan

Firm: _____

Name of Person(s) interviewed: _____

Position: _____

Address: _____

Phone: _____

Date of Interview: _____

No. _____

ECONOMIC IMPACT OF INITIATIVE 245

QUESTIONNAIRE FOR FINANCIAL INSTITUTIONS

1. What were the monthly payments, at time of application, as a percentage of monthly takehome pay which best describes your marginal consumer credit applicant?

	Prior to Initiative 245	In Response to Initiative 245
a) direct loans:	_____	_____
b) indirect loans:	_____	_____

2. What is your overall rejection rate for:

	Prior to Initiative 245	In Response to Initiative 245
a) direct loans:	_____ %	_____ %
b) indirect loans:	_____ %	_____ %
c) credit cards:	_____ %	_____ %

3. In response to Initiative 245, have you changed your policies with respect to:

	No Change	Prior to Initiative 245 (before 12/5/68)		Amount	In Response to Initiative 245 (since 12/5/68)		Amount
a) a minimum service fee - direct loans	_____	Yes	No	_____	Yes	No	_____
- credit cards	_____	Yes	No	_____	Yes	No	_____
b) a loan fee - direct loans	_____	Yes	No	_____	Yes	No	_____
- credit cards	_____	Yes	No	_____	Yes	No	_____
c) an investigation and credit report fee - direct loans	_____	Yes	No	_____	Yes	No	_____
- credit cards	_____	Yes	No	_____	Yes	No	_____
d) credit insurance - direct loans	_____	Yes	No	_____	Yes	No	_____
- credit cards	_____	Yes	No	_____	Yes	No	_____

	No Change	Prior to Initiative 245 (before 12/5/68)		Amount	In Response to Initiative 245 (since 12/5/68)		Amount
e) a one-time set up fee for new accounts							
- direct loans	_____	Yes	No	_____	Yes	No	_____
- indirect loans	_____	Yes	No	_____	Yes	No	_____
f) late payment fee							
- direct loans	_____	Yes	No	_____	Yes	No	_____
- indirect loans	_____	Yes	No	_____	Yes	No	_____

g) Others? Identify (filing fee) _____

_____

4. When you buy credit paper from retailers, do you discount? Yes____ No____
   If yes: (a) what was the rate prior to Initiative 245? _____
   (b) what is the rate in response to Initiative 245? _____

   Comment:

5. In response to Initiative 245, have you changed your policies regarding recourse on indirect loans?

   _____

   _____

6. As far as you can determine what has been the impact of Initiative 245 upon:

   a) Consumers? _____

   _____

   b) Retailers? _____

   _____

   c) Financial Institutions? _____

   _____

7. What was the volume of consumer loans in each of the following loan categories?

	1st Qtr. 1968	1st Qtr. 1969	No Change
a) new car purchases:			
direct loans	$_____	$_____	_____
indirect loans	$_____	$_____	_____
b) used car purchases:			
direct loans	$_____	$_____	_____
indirect loans	$_____	$_____	_____
c) appliances and household goods			
direct loans	$_____	$_____	_____
indirect loans	$_____	$_____	_____
d) boats and marine goods			
direct loans	$_____	$_____	_____
indirect loans	$_____	$_____	_____
e) travel and vacation			
direct loans	$_____	$_____	_____
f) consolidated debt			
direct loans	$_____	$_____	_____
g) total direct loans	$_____	$_____	_____
h) total indirect loans	$_____	$_____	_____

ECONOMIC IMPACT OF INITIATIVE 245 - SURVEY

FINANCIAL INSTITUTIONS - COMMERCIAL BANKS

I. Type of financial institution: Please check the one category and sub-category, where appropriate, which best describes your operation.

a. _____bank
   _____federal charter
      _____branch
   _____state charter
      _____branch
   _____mutual savings

b. _____finance company
   _____branch

c. _____credit union

d. _____savings and loan

Firm: _____

Name of Person(s) interviewed: _____

Position: _____

Address: _____

Phone: _____

Date of Interview: _____

No. _____

ECONOMIC IMPACT OF INITIATIVE 245

QUESTIONNAIRE FOR FINANCIAL INSTITUTIONS - COMMERCIAL BANKS

1. What were the monthly payments, at time of application, as a percentage of monthly takehome pay which best describes your marginal consumer credit applicant?

	Prior to Initiative 245	In Response to Initiative 245
a) direct loans:	_____	_____
b) indirect loans	_____	_____

2. What is your overall rejection rate for:

	Prior to Initiative 245	In Response to Initiative 245
a) direct loans:	_____%	_____%
b) indirect loans:	_____%	_____%
c) credit cards:	_____%	_____%

3. In response to Initiative 245, have you changed your policies with respect to:

	No Change	Prior to Initiative 245 (before 12/5/68)			In Response to Initiative 245 (since 12/5/68)		
a) a minimum service fee				Amount			Amount
- direct loans	_____	Yes	No	_____	Yes	No	_____
- credit cards	_____	Yes	No	_____	Yes	No	_____
b) a loan fee							
- direct loans	_____	Yes	No	_____	Yes	No	_____
- credit cards	_____	Yes	No	_____	Yes	No	_____
c) an investigation and credit report fee							
- direct loans	_____	Yes	No	_____	Yes	No	_____
- credit cards	_____	Yes	No	_____	Yes	No	_____

	No Change	Prior to Initiative 245 (before 12/5/68)		Amount	In Response to Initiative 245 (since 12/5/68)		Amount
d) credit [illegible]e							
- dire[illegible]ans	_____	Yes	No	_____	Yes	No	_____
- credit cards	_____	Yes	No	_____	Yes	No	_____
e) a one-time set up fee for new accounts							
- direct loans	_____	Yes	No	_____	Yes	No	_____
- indirect loans	_____	Yes	No	_____	Yes	No	_____
f) late payment fee							
- direct loans	_____	Yes	No	_____	Yes	No	_____
- indirect loans	_____	Yes	No	_____	Yes	No	_____

g) Others? Identify (filing fee) _____

_____

4. When you buy credit paper from retailers, do you discount? Yes___ No___

If yes: (a) what was the rate prior to Initiative 245? _____

(b) what is the rate in response to Initiative 245? _____

Comment:

5. In response to Initiative 245, have you changed your policies regarding recourse on indirect loans?

_____

_____

6. As far as you can determine what has been the impact of Initiative 245 upon:

a) Consumers? _____

_____

b) Retailers? _____

_____

c) Financial Institutions? _____

_____

7. What was the volume of consumer loans in each of the following loan categories?

	1st Qtr. 1968	1st Qtr. 1969	No Change
a) new car purchases			
direct loans	$_____	$_____	_____
indirect loans	$_____	$_____	_____
b) used car purchases:			
direct loans	$_____	$_____	_____
indirect loans	$_____	$_____	_____
c) appliance and household goods			
direct loans	$_____	$_____	_____
indirect loans	$_____	$_____	_____
d) boats and marine goods			
direct loans	$_____	$_____	_____
indirect loans	$_____	$_____	_____
e) travel and vacation			
direct loans	$_____	$_____	_____
f) consolidate debt			
direct loans	$_____	$_____	_____
g) total direct loans	$_____	$_____	_____
h) total indirect loans	$_____	$_____	_____

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1/27/72

Representative Bill Moran:

All the members of the Senate Commerce Committee will be out of town tomorrow and therefore will not be able to attend your Joint Judiciary and Commerce Committee meeting on HB 174 and HB 453. Thanks for the invitation.

Sen. Ron Rettig

File
HB 174

Cliff, Will you please handle this for our committee. I'd like to be in Juneau Thanks Ron

Alaska State Legislature

House

JUDICIARY COMMITTEE
Pouch V
Juneau, Alaska 99801

JUNEAU ALASKA

January 26, 1972

Honorable Robert H. Ziegler, Sr.
Senate Judiciary Chairman
Pouch V - Capitol Building
Juneau, Alaska 99801

Re: HB 174 - Uniform Consumer Credit Code
HB 453 - Relating to Consumer Credit

Dear Senator Ziegler:

The House Commerce and Judiciary Committees are sponsoring a joint public hearing on House Bill 174 (Uniform Consumer Credit Code) and House Bill 453 (Relating to Consumer Credit). As the title of House Bill 174 suggests, it is the draft prepared by the National Conference of Commissioners on Uniform Laws. I have been informed that House Bill 453 was drafted at the Boston College Law Center pursuant to a grant from the Office of Economic Opportunity.

The hearings will be held in the House Conference Room, beginning at 1:30 p.m. on Friday, January 28, and will continue over into Saturday as need may require.

The National Conference has made available Neil Butler, Esquire, of Denver, Colorado, and Richard Wheatley, Esquire, of Stillwater, Oklahoma. I understand that these members of the bar are particularly qualified to discuss House Bill 174.

Norm Banfield will be leaving for Europe this weekend. As a courtesy to him, Jay Kerttula and I have agreed to convene our respective committees immediately upon adjournment of the House on Thursday, January 27. It is my understanding that Mr. Banfield wishes to testify in favor of House Bill 174 and in opposition to House Bill 453. We hope to have Mr. Banfield's testimony taken also in the House Conference Room.

On the assumption that the Senate Commerce and Judiciary Committees will have some bill under consideration pursuant to House action, Mr. Kerttula and I invite the attendance and participation of your committee members at the above session. We also request that you make the fact of such hearings known to other members of the Senate by announcement on the Floor.

In the interest of time, I am designating a copy of this letter for Senator Rettig. I hope he will not be offended that I have not written to him separately.

Sincerely,

William J. Moran
Chairman

cc: Honorable Ron Rettig
Senate Commerce Chairman

Alaska Retail Association

HB 174
HB 453

Box 1727 Anchorage, Alaska 99510
Phone: 272-4222

January 14, 1972

Rep. William J. Moran
Alaska State House
Pouch V State Capitol Bldg.
Juneau, Alaska

Dear Representative:

We are once again recommending the passage of the Uniform Consumer Credit Code which has been introduced in the House as HB 174.

This proposal, which was drafted by the National Conference of Commissioners on Uniform State Laws, would serve to eliminate the vast majority of problems extant in the area of consumer credit law. It provides for concise regulation of the consumer credit industry, has consumer protection provisions which go well beyond those available under present Federal or State law and would provide for healthy competition among credit grantors. This increased competition will serve to insure an adequate supply of credit to all segments of our society.

We would appreciate you taking a few minutes from your very busy schedule to read the enclosed booklet, entitled "Questions & Answers on UNIFORM CONSUMER CREDIT CODE". We are certain you will find that UCCC answers many of the problems related to consumer credit.

Sincerely,

Dean Ehrich
Legislative Agent

DE:kt
Enclosure

HOUSEHOLD FINANCE CORPORATION
RESULTS OF SMALL LOAN OPERATIONS IN ALASKA
1968 - 1969 - 1970
(Exclusive of Income from Contracts Purchased)

	1968	1969	1970
Loans outstanding at begir ing of year	$1,512,601	$1,838,691	$2,453,776
Loans outstanding at end of year	1,838,690	2,453,776	2,409,209
Average loans outstanding	1,675,645	2,146,233	2,431,493

Expenses of Operations

Classification	Amount			Percentage of Average Loans Outstanding		
	1968	1969	1970	1968	1969	1970
Advertising	$16,576	$17,176	$11,730	0.99	0.80	0.50
Bad Debts	30,490	30,452	53,217	1.82	1.42	2.19
Rent	38,314	34,891	36,940	2.35	1.63	1.52
Salaries	100,748	111,737	121,334	6.01	5.21	5.00
Supervision	39,058	43,195	50,481	2.33	2.00	2.12
State and Local Taxes	29,470	28,027	29,026	1.76	1.30	1.20
Federal Income Taxes	134,774	162,333	130,301	8.00	7.56	5.77
Telephone and Telegraph	27,800	32,394	26,583	1.66	1.50	1.09
Legal, Postage, Supplies, etc.	28,815	30,104	30,635	1.72	1.40	1.26
	$446,050	$490,310	$490,250			
Interest rate required on loans to pay expenses, exclusive of interest on borrowed funds				26.64%	22.82%	20.65%

Average Assets Used Each Year

	1968	1969	1970
Average assets used in business	$1,787,706	$2,280,363	$2,569.106

Net Profit Percentage

1968 Net profit of $128,275 ÷ assets used of $1,787,706 = 7.18% return on investment
1969 Net profit of $157,686.30 ÷ assets used of $2,280,363 = 6.91% return on investment
1970 Net profit of $134,538 ÷ assets used of ~~$134,538~~ $2,569,106 = 5.24% return on investment

HOUSEHOLD FINANCE CORPORATION

1968 Operating Statistics

	Average Amt. Loaned Per State	Percent of Average Loan Balance Spent for: Salaries	Rent	Adv.	Admin.	Taxes	Deprec.	Bad Debts	Other Exp.	Total
Alaska	$ 1,732,164	5.79	1.87	1.01	2.27	2.22	.34	1.43	2.78	17.71
Washington	$ 21,110,000	3.37	.69	.72	1.92	.48	.19	1.75	1.46	10.58
Oregon	$ 4,627,000	3.47	.85	.75	1.86	.58	.10	2.81	1.82	12.24
California	$162,429,000	3.59	.73	.55	1.92	.97	.19	1.73	1.43	11.11
U. S. Average	$ 6,512,000	3.53	2.07	1.04	1.72	.35	.13	.81	2.19	11.84

HB-174

JUDICIARY COMMITTEE
Pouch V
Juneau, Alaska 99801

January 26, 1972

Honorable Robert H. Ziegler, Sr.
Senate Judiciary Chairman
Pouch V - Capitol Building
Juneau, Alaska 99801

Re: HB 174 - Uniform Consumer Credit Code
HB 453 - Relating to Consumer Credit

Dear Senator Ziegler:

The House Commerce and Judiciary Committees are sponsoring a joint public hearing on House Bill 174 (Uniform Consumer Credit Code) and House Bill 453 (Relating to Consumer Credit). As the title of House Bill 174 suggests, it is the draft prepared by the National Conference of Commissioners on Uniform Laws. I have been informed that House Bill 453 was drafted at the Boston College Law Center pursuant to a grant from the Office of Economic Opportunity.

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In the interest of time, I am designating a copy of this letter for Senator Rettig. I hope he will not be offended that I have not written to him separately.

Sincerely,

William J. Moran
Chairman

cc: Honorable Ron Rettig
Senate Commerce Chairman

Pouch V
Juneau, Alaska 99801

January 21, 1972

Richard Wheatley, Esquire
University Bank
Post Office Box 1067
Stillwater, Oklahoma 74074

Re: HB 174 - Uniform Consumer Credit Code
HB 453 - Relating to Consumer Transactions

Dear Mr. Wheatley:

This letter will confirm our telegraphic invitation and request of this date for your appearance before a joint meeting of the House Commerce and Judiciary Committees of the Alaska Legislature on January 28 and 29 to testify and otherwise participate in the consideration of the above-named bills, now before the House Commerce Committee. Both bills have a second referral to the House Judiciary Committee. HB 174 is the Uniform Consumer Credit Code as prepared by the National Conference of Commissioners on Uniform State Laws; HB 453 is a proposal in the same area of legislative concern which was prepared at the Boston College Law Center pursuant, as we understand, to a grant from the Office of Economic Opportunity. Copies of both bills are enclosed.

The joint meeting will convene at 1:30 p.m. on January 28 in the House Conference Room, Second Floor, Capitol Building, and will continue into the following day as may be required. Because of the interest in the subject, as well as its complicated nature, a second day of testimony will undoubtedly be necessary. (Norman C. Banfield, Esquire, of the Juneau Bar, will appear on January 27 to permit him to meet a commitment elsewhere; a sponsor of HB 453 has requested that witnesses for his bill also be heard approximately one week later.) All members of the Legislature will be invited to attend and to participate in the hearings. The Senate Commerce and Judiciary Committees will undoubtedly be present.

We are grateful to you for your willingness to participate in these important hearings and to give us the benefit of your expertise; we are grateful to the National Conference for their support of your attendance; and, we are grateful to Frederick O. Eastaugh, Esquire, Alaska's Commissioner to the Conference, for his, as always, generous assistance.

Please let us know if we can be of help with respect to your accommodations or other amenities while you are in Juneau. Our addresses are as above; we can be reached telephonically at (AC 907) 586-5288 (Chief Clerk); 586-6614 (Commerce); or 586-6795 (Judiciary). Please note that Juneau is on Pacific Standard Time, that is, Oklahoma is two hours earlier.

Please again accept our thanks for your kind assistance.

Sincerely,

William J. Moran
Chairman, Judiciary Committee

Jalmar M. Kerttula
Chairman, Commerce Committee

Enclosures - Copies of HB 174
and HB 453

cc: Frederick O. Eastaugh, Esquire
Post Office Box 1211
Juneau, Alaska 99801

WJM:JMK:mm

Pouch V
Juneau, Alaska 99801

January 21, 1972

Richard Wheatley, Esquire
University Bank
Post Office Box 1067
Stillwater, Oklahoma 74074

Re: HB 174 - Uniform Consumer Credit Code
HB 453 - Relating to Consumer Transactions

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Please again accept our thanks for your kind assistance.

Sincerely,

William J. Moran
Chairman, Judiciary Committee

Jalmar M. Kerttula
Chairman, Commerce Committee

Enclosures - Copies of HB 174
and HB 453

cc: Frederick O. Eastaugh, Esquire
Post Office Box 1211
Juneau, Alaska 99801

WJM:JMK:mm

Pouch V
Juneau, Alaska 99801

January 21, 1972

Neil Butler, Esquire
2450 Colorado State Bank Building
16th & Broadway
Denver, Colorado 80202

Re: ✓HB 174 - Uniform Consumer Credit Code
HB 453 - Relating to Consumer Transactions

Dear Mr. Butler:

This letter will confirm our telegraphic invitation and request of this date for your appearance before a joint meeting of the House Commerce and Judiciary Committees of the Alaska Legislature on January 28 and 29 to testify and otherwise participate in the consideration of the above-named bills, now before the House Commerce Committee. Both bills have a second referral to the House Judiciary Committee. HB 174 is the Uniform Consumer Credit Code as prepared by the National Conference of Commissioners on Uniform State Laws; HB 453 is a proposal in the same area of legislative concern which was prepared at the Boston College Law Center pursuant, as we understand, to a grant from the Office of Economic Opportunity. Copies of both bills are enclosed.

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Please again accept our thanks for your kind assistance.

Sincerely,

William J. Moran
Chairman, Judiciary Committee

Jalmar M. Kerttula
Chairman, Commerce Committee

Enclosures - Copies of HB 174
and HB 453

cc: Frederick O. Eastaugh, Esquire
Post Office Box 1211
Juneau, Alaska 99801

WJM:JMK:mm

January 18, 1972

Norman C. Banfield, Esquire
Faulkner, Banfield, Doochever
& Doogan, Attorneys
Suite 201 - 311 Franklin Street
Juneau, Alaska 99801

Re: SB 42 - Amending Retail Installment Sales Act
SB 242 - Interest on Loans
SB 174 - Uniform Consumer Credit Code
SB 353 - Consumer Transactions

Dear Norm:

Confirming our conversation today concerning your letter to me of January 10, it is my intention to delay further action on SB 242 and SB 42 pending consideration of SB 174 and SB 353. The latter two bills are scheduled for joint public hearing before the House Commerce and Judiciary Committees on January 26, at 1:30 p.m., in the House Conference Room. It is expected that these hearings may continue into January 27. I know also that Representative Farrell, co-sponsor of SB 353, may request that additional hearings be held the following week, probably on February 4.

Mr. Karttula is scheduled to testify on SB 174 and SB 353 a bit earlier to accommodate your departure from Alaska. Since our present plan is not to have a calendar on Thursday, a meeting with you immediately on adjournment on January 27 seems the most practical. I should think that you could conclude your presentation by noon that day. Please let me know.

Sincerely,

William J. Moran

cc: Rep. Karttula
Rep. Farrell
Mr. Eastaugh

File HB 174

LAW OFFICES OF
FAULKNER, BANFIELD, BOOCHEVER & DOOGAN
SUITE 201, 31 FRANKLIN STREET
JUNEAU, ALASKA 99801
TEL. 586-2210
AREA CODE 907

HERBERT L. FAULKNER
NORMAN C. BANFIELD
ROBERT BOOCHEVER
FRANK M. DOOGAN
AVRUM M. GROSS
MICHAEL M. HOLMES
SANFORD SAGALKIN

January 20, 1972

The Honorable William J. Moran
Chairman, Judiciary Committee
House of Representatives
Juneau, Alaska 99801

Re: HB 42 - Amending Retail Installment Sales Act
HB 242- Interest on Loans
HB 174 - Uniform Consumer Credit Code
HB 453- Consumer Transactions

Dear Bill:

Thanks for your letter of January 18, 1972, regarding the above bills. I will be ready after the House adjourns on January 27th and will give you a summary of the contents and purposes of HB 174. It is possible that more qualified persons may appear later but I will give you a resume of the bill which will help you to understand a more detailed analysis which may be made by others as you will have a picture of the scheme developed by the Code.

At the present time I have inquired as to whether Household Finance Corporation can have one or more persons present who have followed the development of the Code much more closely than I have. I will let you know if they can be present for the hearings on January 28th and 29th.

Yours very truly,

N. C. Banfield

NCB:db

cc: Jalmar M. Kerttula
Marty Farrell
F. O. Eastaugh