

The consumer is hurt in two ways: First, he cannot readily compare the costs of competing credit offers. Second, he is led to believe that credit costs are lower than they actually are. Rates are quoted in ways that imply that they are very low, and to give the impression that they are effective annual rates when they are not.

What ordinary shopper is likely to multiply out the $1\frac{1}{2}$ percent a month on a revolving charge account by 12, to arrive at the true annual rate of 18 percent?

Will a borrower from a small loan company translate three percent a month into an astonishing 36 percent a year? Would he—or could he—ever figure out an annual rate equivalent for the split-level type of monthly finance rate—three percent on the first \$150; $2\frac{1}{2}$ percent on the next \$150 and one percent on the remainder to \$1,000?

A new car buyer purchasing at a \$5 per \$100 per year "add-on" rate understandably thinks this is an annual interest rate. So does the borrower from a bank who takes out an installment loan at an annual rate of five percent "discount." Very few can translate these into actual effective rates of 9.2 percent and 9.7 percent, respectively.

In no other field of lending does such disorder and confusion prevail. Business borrowers from banks and other financial institutions would not put up with the flim-flam in credit cost quotations that is defended as appropriate and even necessary in the consumer market.

Surveys have amply demonstrated that few consumers have any real knowledge of how much they pay for installment credit, and especially what they are paying in terms of annual interest.

For example, in 1960 the National Bureau of Economic Research found that 840 *Consumers Union* subscribers who reported the rates they paid on recent installment purchases estimated on the average, that they paid 8.3 percent. But the actual interest they paid as computed by the Bureau, was 23.2 percent. Borrowers who knew the true rate paid an average of 12.1 percent on loans under \$500. Those who were completely uninformed paid an average of 37 percent.

Whatever the mysteries of consumer credit financing, there is little mystery about why consumer borrowers know so little about its costs. They are concealed behind a curtain woven out of indecipherable statistics; a curtain that's pure gold on the side of the lender.

Stating credit costs on a uniform, annual effective rate basis would not only make it possible for consumers to shop readily among competing credit sources, but would stimulate such shopping. Many witnesses in the Senate field hearings of 1963-64 said, in effect, "If I had known the rate was 40 percent, I would have looked elsewhere," or "I would have made other arrangements."

If rates are soothingly low-sounding, such as two percent a month or \$7, \$8, or \$9 per \$100 per year, shopping for credit may not seem really necessary or worth while.

The truth-in-lending bill, as passed by the Senate does reflect overwhelming acceptance of the need for disclosure of finance charges on an effective annual rate basis, as well as the less controversial idea that full dollar costs be disclosed. But unfortunately the bill contains several exemptions, which will greatly weaken its effectiveness if ultimately accepted by the Congress.

1. *Revolving credit*

The most serious defect of S. 5 as it passed the Senate and of H.R. 11602 is its virtually complete exemption from annual rate disclosure requirements of so-called "revolving credit," widely used in department stores and banks. Probably less than 15 percent of an estimated \$3.5 billion of revolving credit would be covered. In future years revolving credit will become an increasingly important segment of the consumer lending industry.

The customary retailer charge on revolving credit is $1\frac{1}{2}$ percent per month, or a true annual rate of 18 percent per year.

We see no reason why a store or bank that charges at the rate of $1\frac{1}{2}$ percent per month on the unpaid balance should not be required to translate this percentage into 18 percent per year. Despite all the protestations of retailer representatives to the effect that 18 percent per year overstates the actual rate of charge on an annual basis, straight reasoning on this point has demonstrated that $1\frac{1}{2}$ percent is, in fact, 18 percent per year, when computed without regard to the so-called "free ride period" during which no finance charge is imposed.