I think, in which I did not refer to this Trading With the Enemy Act. I can only plead that I had only been aboard for 6 days at that time and I simply failed to give you the full information relative to this matter.

The second response I would give to you, we are not really relying on it. We think that in a real emergency situation it could be used as a basis for credit controls, but we do not propose to rely upon it.

Mrs. SULLIVAN. Let me just cite an illustration of why I am concerned; it is on the record and although it doesn't apply to the issue we are talking about here today, it indicates why I feel we should go into these things candidly.

As you may have heard, I have been at war with the administration for 3 years—but only openly since March—on the negotiations over the Panama Canal. I violently oppose the proposed treaty provisions to turn the authority over the Panama Canal to a country that is politically unstable.

During the past 3 years, when the negotiators have been coming to us in executive session to discuss the issues, I asked them time after time whether the Congress does not have to act as a whole if we are to turn over any property—bought and paid for by the United States—under any treaty. And the answer always was, "No, when we abrogate the treaty and make a new treaty it will only have to be ratified by the U.S. Senate." Now they are finding out they were wrong; yet for 3 years I had been raising the question with them. Whether they thought they had the right answers, or whether they went into it deep enough, I don't know. But I think many of these things need delving into. We are not always right as individuals. Our negotiators, who worked with some very clever people, evidently hadn't done their homework well enough to find out whether or not additional authority would be needed, and absolutely ignored our questions on it and made no further study on it.

I still have my doubts—going back to our own subject right now of standby credit controls in a national emergency—whether you have the authority to do what you would need to do in time of such emergency.

In this connection, the Wall Street Journal ran a very interesting story on June 20, 1967, called "The Emergency Jumble: Presidential Crisis Powers Are Irrational and Full of Gaps." I would like to include this article at this point in the record. I feel that the administration should devote more time to clarifying for us and for the public the emergency powers that it has or might need on a standby basis—especially in the area of economic stabilization and the control of consumer credit.

That is all I have at this point. If there are additional questions, you can answer them for the record.

Mr. BRYANT. Thank you.

(The article referred to follows:)

[From the Wall Street Journal, June 20, 1967]

EMERGENCY JUMBLE—PRESIDENTIAL CRISIS POWERS ARE IRRATIONAL AND FULL OF GAPS

(By Joseph W. Sullivan)

WASHINGTON.—The United States presently faces:
(A) Disturbance in its international relations;

(B) Actual or threatened hostilities;
(C) A threat of war;
(D) A threat of predatory incursions.

For President Johnson, in particular, the mulling of this checklist is more than a semantic exercise. Each check mark made by the Chief Executive can trigger an extra quantum of the far-flung reserve powers Congress has handed him over the years for crisis use.

From such gunboat-diplomacy relics as the authority to arm private vessels when there's "danger" that "physical force" may be applied against U.S. citizens or property abroad, these standby powers span the gamut to a temporary dictator's mandate to be invoked upon proclaiming that he "anticipates" an attack on the U.S.

So jumbled are the statutory tests for bringing all of them to bear, however, that (short of resorting to the anticipated-attack button) they almost defy coordinated use. More than a dozen finespun declarations, of which those on the checklist are only samples, would be required to trigger the President's arsenal in sequence. While his Office of Emergency Planning has devised, at least on paper, machinery for meeting all sorts of contingencies, even OEP officials are unclear as to which plans can be activated by which triggers. They can't, in fact, even say with certainty which ones are already authorized under President Truman's 1950 proclamation of a "National Emergency," a nuncio all authorities agree has continued in effect, though few are sure it should have—or would have if challenged in the courts.

Nor has Congress, it's quite plain, followed any cohesive design for attuning the triggers to the gravity of the crisis. Thus, an incongruous appendage to the military draft law empowers the President to direct and even seize industrial facilities for defense production upon finding that the "national security" requires it. But to activate tools for dealing with dislocations in the civilian economy, his only statutory recourse would be to forecast an attack on the U.S. in order to impose the sweeping economic controls conferred by the Federal Civil Defense Act. (One exception: Rationing of "critical" materials—but not price controls—could be imposed more easily under yet another law.)

Coming amid the war in Vietnam and the Middle East turbulence, the long-overhanging threat of a nationwide railroad strike starkly points up the entire system's irrationality.

OTHER CARRIERS NO PROBLEM

If the closedown threat were to loom against the maritime industry instead, the President would have authority as clear as any can be in this muddled field to take command of the U.S. merchant fleet as a "national emergency" measure. Should transit service have been imperiled in some city, the Secretary of Defense could have ordered continued service by "motor" carriers for military personnel and defense plant workers, also on the ground of a "national emergency." If military deliveries were about to be held up by a closedown in a plant instead of on the rails, moreover, the President could first order the contractor to keep the plant going and, if unheeded, seize the plant himself. (President Truman's failure to follow the procedural rules is what tilted the Supreme Court against him when it struck down his 1952 order seizing the nation's steel mills.)

By the quirks of the emergency law book, though, the 1916 statute covering railroads authorizes Presidential assumption of control only "in time of war." While President Truman relied on World War II's legal continuation to temporarily seize the railroads in 1946 and again in 1950, it is the Justice Department's view that this legal fiction can no longer be sustained.

Thus, however ringing Defense Secretary McNamara's statement that a rail strike would be "unthinkable" and would "cause critical and irremediable shortages for essential defense production," he and President Johnson say they can only look to Congress to prevent it. As last week's crushing House defeat of the Johnson settlement proposal made clear, though, the lawmakers are too fragmented to be counted upon. Seizure, binding arbitration, bars against industry-wide bargaining—all these were advocated by some faction, but none could command a House majority. Yet the stopgap strike bar finally voted is being resisted by the Senate and, as the two chambers grapple, the threat of a railroad shutdown continues unabated. (It's a matter of pure guesswork how long the rail unions will abide by their promise to forgo a strike while awaiting the verdict of a House-Senate conference.)

Still, haphazardness and sputtering on Congress' part aren't the only contributors to the emergency-preparedness mishmash, as the railroad episode also

shows. If the Administration were better braced internally, it might be able to make some use of contingency plans that President Kennedy ordered drawn five years ago for "centralized control of all modes of transportation in an emergency for the movement of passenger and freight traffic of all types."

"HOPELESS"

It would probably take a nuclear holocaust to justify full implementation of such plan. If they existed, though, the President might be able to draw on them now in a limited way by invoking an obscure section of the Interstate Commerce Act that permits him to direct all carriers to give priority to troops and military goods in time of "threatened war." The railroad unions say they're ready to keep military cargoes moving during any strike. Despite the Kennedy directive to prepare for such emergency movements, however, Mr. McNamara has told Congress the task is "hopeless."

It's still likely, to be sure, that Congress will ultimately provide the Administration some new tool for preventing a walkout. And however clumsy the legislative workings in this instance, there's still much to be said in theory for tailoring emergency measures to fit the emergency, as against writing broader powers into the lawbooks for use in unforeseeable future circumstances. While an ever-cautious Lyndon Johnson may spurn the use of emergency powers, moreover, some successor might be inclined to use them excessively. It's hardly likely, for example, that the Congressman who wrote provisions for "emergency" regulation of the currency into 1917's Trading With the Enemy Act foresaw Franklin Roosevelt's 1939 use of this authority to justify imposition of consumer credit controls.

Both diplomatic and domestic political reasons have deterred the Johnson Administration from invoking powers that require fresh proclamations of crisis. The President forewent a call-up of military reserves in 1965 at least in part because it would have entailed making an unsettling new declaration of "national emergency."

But should a nuclear showdown ever come, the President would clearly assume authority, on paper, to do most anything, and all the perplexities of the lesser statutory triggers would be rendered moot. Under the 1950 Civil Defense Act, the President is authorized to raise and spend funds about as he sees fit, to seize any property and to "sell, lease, lend, transfer or deliver materials or perform services for civil defense purposes on such terms and conditions as he may prescribe and without regard to limitations of existing law."

Even if Congress hadn't provided such a sweeping mandate, moreover, many legal scholars contend the President could assert all the powers anyway, relying on his Constitutional prerogatives as Commander in Chief. "Short of an invasion or attack on the U.S., the act's provisions are blatantly unconstitutional, but under the conditions they envision I suspect that the President's authority would expand just as far without them," says Benet D. Gellman, author of a Virginia Law Review article on emergency planning.

LESSER POWERS CAN BE HANDY

All the same, many of the lesser power grants would appear to fill gaps that might prove vexing in a pinch. One of these directs suppliers to give priority to the Government's communications, power, materials and transport needs; others suspend civil service hiring regulations, agricultural marketing quotas, requirements for bidding on defense contracts and for publication of newly issued patents.

While the President could probably assert implicit powers as Commander in Chief in a lesser crisis also, there's probably utility in the provisions that spell out his emergency authority to lift Congressional lids on military manpower and to lower bars against realigning the military services' respective combat functions.

Mr. Johnson is already drawing on a number of these prerogatives when they can be invoked unobtrusively by the Truman declaration of 1950. Defense "set-asides" of copper, direct negotiation of defense contracts and extension of Navy enlistment terms are all based on the Truman "emergency."

Some of the authority is itself vague (one provision would appear to sanction a Government shutdown or takeover of all broadcast stations and even the telephone system whenever there's a "threat of war"). But it's the vagaries

of the many triggering devices that render the entire system suspect. The President to draw just one further contrast, can activate and dispatch up to a million Army reservists into battle upon a simple "emergency" finding, yet it would take an "extraordinary emergency" for him to supersede a law barring harbor-dredging workers from toiling more than eight hours a day.

Congress should be acutely aware of the anomalies. Every Aug. 1 the lawmakers violate the law providing for Congressional adjournment by July 31, on account of the "emergency" that sprang up 17 years ago. Yet there's been no attempt to set criteria for the termination, or even the periodic reaffirmation, of emergency declarations—either of the sort now in effect or of the dictator's mantle provided by the Civil Defense Act.

True, Congress can vote to end emergency powers. But how is it to agree on that as long as it's perpetuating a spate of different standards for starting them.

Mrs. SULLIVAN. Governor, you have been very gracious in waiting to testify. We had hoped to reach you by the time you arrived here, but we can't control what happens in the House, so we just have to do the best we can. I know how busy you are and what a sacrifice it has been for you to come here and then have to wait.

Mr. BRYANT. On the contrary, it is a pleasure.

Mrs. SULLIVAN. Thank you very much. I also want to thank your two associates for coming.

Is Dr. Ralph R. Reuter, chairman of the Metropolitan New York Consumer Council, present?

Dr. Reuter, we tried to reach you late yesterday to warn you that we were not going to be able to have an afternoon session today. If you can testify briefly now, we would like to have you give us the benefit of your knowledge on the subject. Your entire statement will be made part of our record and we will read it and study it, but will you summarize it for us?

STATEMENT OF DR. RALPH R. REUTER, CHAIRMAN, METROPOLITAN NEW YORK CONSUMER COUNCIL

Dr. REUTER. That is exactly what I propose to do. I do not want to leave this microphone without congratulating the committee on what we consider to be an excellent bill in toto. We believe that some of the features that have been discussed this morning are most essential, particularly the garnishee question, and the matter of revolving credit which is becoming a real horrendous problem.

We think you should take particular note of the fact that in the State of New York we at one time thought we were ahead of everybody else in credit legislation. We don't feel that way any more. The credit people have found ways and means of getting around the laws and we now find credit as exorbitant, as was stated the other day to this committee by Senator Douglas. We have found cases where his figures were quite generous. We found it worse than that from so-called legitimate institutions. Consequently, we find this legislation in its entirety very, very necessary.

We would only hope that this bill will remain intact when it comes out of the House and out of the joint conference committee.

Thank you.

Mrs. SULLIVAN. Thank you, Doctor. There are people on this subcommittee who are fighting for this bill.

Our success remains to be seen.
(Dr. Reuter's full statement follows:)

TESTIMONY OF DR. RALPH R. REUTER, CHAIRMAN, METROPOLITAN NEW YORK CONSUMER COUNCIL, INC., NEW YORK, N.Y.

Madam Chairman and distinguished members of the Subcommittee on Consumer Affairs:

We feel proud and honored to be able to support H.R. 11601 without reservation.

The Metropolitan New York Consumer Council, an organization of more than one hundred and seventy member organizations who have gathered together in the Council to promote and educate for the consumers welfare, is indeed grateful that this legislation is finally receiving the kind of attention which it long ago deserved and which most certainly is rather belated.

Your hearings to date have undoubtedly convinced you that consumer credit is no longer a sales tool. It has become a sales object. Debt is promoted with all the skill and ingenuity that American advertising and sales promotion can muster. And debt is sold on precisely the same ethical standards as those that characterize the promotion of the cold cure, the headache remedy, the weight reducer, the cigarettes, the detergent, the hair ointment, etc. This is indeed a matter for real concern for the Congress of the United States as the elected representatives of all the people.

Twenty-two years ago, the big war was all but over. Back in 1945 people were beginning to satisfy their war-starved appetities for homes and things, and especially for cars, mostly with cash money. Mortgage debt for urban homes then was around $20 billion and short-term debt for goods—debt scheduled for repayment in five years or less—was less than $7 billion. Ten years later, in 1955, mortgage debt had grown to $88 billion, more than four times what it had been. Short-term debt had grown to $39 billion, six-and-a-half times what it had been. In another ten years, by 1965, mortgage debt had become $200 billion, ten times its 1945 level. Short-term debt had multiplied twelve times to a total of $80 billion. Because of its pivotal importance, it is the latter kind of debt, the debt associated with the acquisition of consumer goods and services, that we must point to. A house and lot can be considered an investment. But short-term debt for consumption purposes is seldom more than a promise to pay. The goods financed have no substantial market value once they are acquired and the promise to pay under an installment note is based largely upon the expectation of future earnings.

How will economic historians, or anthropologists, be able to explain in the year 2967 just what has happened to us during the past twenty-two years. How will they account for our having the largest per capita debt for consumption purposes in our history after experiencing twenty-two years of what we have called unprecedented prosperity? How will they explain that, during these twenty-two years of great prosperity, our personal bankruptcies rose to an all time high, more than double their number during the depths of the depression, increasing at a rate twice as fast as the population?

While debt for consumption purposes expanded twelve times over to reach $80 billion, disposable income only tripled between 1945 and 1965. Who then loaned out these billions so fast that debt increased three times as fast as did the wherewithal to pay them back? Commercial banks are the largest holders of consumer paper. They account for about 40% of the total. Sales finance companies come next, with less than half as much as the bank. Then come department stores, credit unions, other loan companies, and other retailers, etc.

With respect to consumer lending, the banker has certainly changed his conservative ways. We once understood that instalment loans on goods were a sound and solid undertaking because of the terms of such loans were so calculated that the goods sold constituted security for the debt financing involved in their sale. And this principle, we gathered, was, practically speaking, immutable because lenders were prudent. Ordinary people, as we all know, are not always so constituted that they withstand well the pressure of urgent present desires if there is a conflict between today's clear wants and tomorrow's hazy needs. But lenders are different. They are disciplined fellows. That is how they got where they are. Hence the once-prevalent idea was that we could all depend on the bankers and other lenders to insist on security for their loans and his prudence would save

both borrower and lender from overcommitment. But lender prudence, as we all now know, has turned out to be an illusion. You hardly ever hear the term used anymore. As for the practice it referred to, when 36-month auto loans became standard, any residual traces of lender prudence had evaporated. The fly-now, pay later era began in earnest.

But, then, how do lenders loan? They say they base their loans on the character of the borrower. Now that's a pleasant idea. It conjures up the figure of a friendly town banker looking a borrower straight in the eye and recognizing in a needy supplicant the sturdy, honest will of a Horatio Alger, Jr., hero. What actually happens, however, is that lenders holding consumer notes don't look into borrowers' eyes; they look at their handwriting. And the signatures giving commercial value to the paper are executed where goods are displayed and sold and where a salesman, on commission often, supplies first the pressure, then the pen. Today's borrower, as a matter of fact, often doesn't consider himself such at all. He is simply a buyer, a buyer on time. So what lenders really mean when they talk about a borrower's character is his credit rating, and that depends on a commercial service called credit checking, which is admittedly staggering into ineffectualness. The burden of trying to keep tabs on the ability to pay of some 25 to 40 million borrowers who are, month by month and day by day, pursued by a veritable army of credit granters has stumped us even in this computer age.

Just view the multiplicity of credit offered. In addition to instalment credit for autos and other durables, for jewelry, for tires, for furniture, and for home repairs, there are credit cards for both goods and services; there is revolving credit for all soft goods; there is the combination of credit card plus revolving credit offered by commercial banks (this is sometimes called a check-credit plan); and recently banks have inaugurated a new type of billing service for small retailers that opens up to every side street shop facilities for selling goods on credit. Now the hardware store, the drug store, dress shop, florist, beauty shop, sporting goods outlet, dry cleaner, toy store, TV repair shop, and stationer have joined the car dealer, discount house, furniture retailer, department store, appliance dealer, mail order house, house-to-house distributor, credit jeweler, gasoline station, book club, record club, hotel, restaurant, bus line, railroad, funeral parlor, and airplane company in the business of creating interest-bearing debt. Food is almost the only significant exemption in this onrush. Nearly all other goods and services, displayed from millions of counters and promoted by billions of advertising dollars, now provide eagerly promoted opportunities to borrow as you buy.

Is it surprising that credit checking flounders and that when a bankrupt lists his debts for the courts that list looks nothing like the record on the debtor to be found on file in the local credit bureal. This does not mean that borrowers are attempting and succeeding in a wholesale deception of lenders. Any commercial debt adjuster (whose job is to try to counsel debtors into solvency and who is paid a high fee by the over-committed family for the service) will tell you that, without exception, every client fails to remember all of his debts, try as he will. After all, there are sometimes as many as twenty creditors involved. And lenders themselves also withhold credit information from a credit rating bureau for their own reasons. Most bankrupt families, for example, list in their debt declarations loans in at least three different small loan companies—loans which a credit rating based on reliable credit checking would have forestalled. But the small loan companies of a given community frequently don't exchange borrower information with each other because, as they know all too well, one small loan leads to another, and the first lender does not want to make it easy for a second loan company, a competitor, to horn in. So loan companies hoard information on their own customers. And a large department store, depending on 90-day credit from suppliers for its stock, is not apt to rush bad news about the condition of its revolving credit accounts out to gossipy trade through a credit bureau, to which, of course, the store's own creditors also have access, So lenders themselves undermine the credit checking upon which they say they rely. Thus, for a number of reasons, credit checking as an effective bar to overcommitment is becoming, like lender prudence, a thing of the past.

Except for a few instances, lenders seem to be getting along fine. How do they do it? Different kinds of lenders have different angles and some have better ones than others. Let's take banks and sales finance companies first. They do the lion's share of the consumer credit business and they *do* an ingeniously devised hedge

against being caught with too much poor consumer paper. That hedge is known as a dealer reserve. It works this way. A car dealer, for example, sells his instalment contracts to a bank or a sales finance company. (This is, by the way, what happens to all but a tiny fraction of the contracts consumers sign at a dealer's lot or for that matter at most retail outlets where consumer durables are sold.) The lender makes a deal with the car dealer about how much he (the lender) wants to charge for the car loan. This is not the amount, however, that the car buyer pays. He pays more. If the lender's agreed-upon take from the loan is, say, 12% true annual interest, the dealer may write up a contract calling for 18%, 24%, or even 35½. (It is not written in, of course, as an interest charge; but as a sum called a time-price differential.) The difference between the lender's interest rate and the dealer's is known as the dealer's kick-back, or, in more polite terms, the dealer's reserve. It is his share of the finance charges. And whatever that amount may be, it is credited at the bank to the dealer's account. But, although the money is the dealer's—he pays income tax on it—the lender controls it. These funds are held by the lender until an agreed-upon total has been accumulated in the reserve. The total that must be maintained is a matter of negotiation between an individual dealer and a lender.

This reserve is supposed to insure the lender against poor consumer loans. Thus, when a car buyer fails to make his payment, the lender takes the balance due him on the contract out of the dealer's reserve and hands the contract back to the dealer. What happens when a bank or sales finance company dips into a dealer reserve to pay up a consumer loan is quite important to those of us who are concerned about the role of consumer credit in our lives today. On the lender's books that car contract, which went sour, appears as a fully paid-up loan. No wonder we hear such glowing reports from lenders about the quality of consumer credit, about how only 1% or 2% of instalment contracts are losses. Under such a foolproof scheme you wonder how there can be even a 1% or 2% loss. In many cases a bank's agreements with dealers will call for the bank returning the car as well as the contract to the dealer, hence there are repossession costs involved. These account for some of the losses. Then there is the skip—the fellow who signs a contract and takes off with a car to parts unknown where neither lender nor dealer nor their nationwide trading set-up can find him or it. And finally there are dealer failures and sometimes a lender has not had the foresight to fatten the reserve sufficiently to cushion him against all the loss from a bankrupt dealer's bad paper.

What about overcommitment? What about the risk to the whole community against which lenders would shield us? How does this dealer-reserve insurance system that protects lending affect borrowing?

The effect has been to turn retailing of durable goods into a game of chance in which chicanery can produce better returns from poor credit risks than price competition would allow on a cash sale. Car dealers, for example, would rather sell cars on credit to poor risks than to sell cars for cash. This doesn't mean that dealers would rather sell poor risks than good risks; but it does mean that the gamble of credit-selling holds out such rewards that cash sales tend to be less profitable than credit sales. Part of the profit on credit sales, of course, a goodly part, builds up in dealer reserves, but the lure of those funds that a dealer owns only after a fashion is more hypnotic than was the Piper of Hamlin. Then there are the insurance commissions to be earned on auto contracts. These are handsome. And insurance charges build up the interest earnings in a contract. Finally, a repossessed car also offers a promise of another sale, and another contract. Credit selling allows dealers to charge what the traffic will bear and under such circumstances the buyer often doesn't know what he has been charged. He'll know his trade-in and his monthly payments, and that's all. And that leaves all kinds of room for profitable maneuvers when an enterprising dealer has an unsophisticated customer at hand and there are, when it comes to credit contracts, millions upon millions who are unsophisticated.

The car story is duplicated in nearly all consumer durables, including television sets, furniture and rugs. For these goods, too, a dealer reserve protects lending and has much the same effect on borrowing. All these sellers say, and they mean it, that they make more on the credit than on the goods. Another group of lenders that has no dealer reserves to count on. It is a large group made up of various kinds of lenders: personal loan companies, department stores lending on revolving credit accounts, credit-card issuers, and banks, too, for that smaller part of their consumer lending where they deal directly with a borrower rather than through a dealer. Although this group of lenders is numerous,

the total of its outstanding loans is lower than the volume of consumer credit extended through banks and sales finance companies for dealer paper. These lesser lenders, nevertheless, have done pretty well for themselves so far.

With personal loan companies no goods are involved, of course, except for the chattels that may be put up as collateral. And these chattels, in most cases, are not actually a security for a loss so much as a potent threat of punishment against a delinquent borrower whose one and only broken down bed, although worthless, is quite important to him. At bottom, what personal loan companies and the rest of these lenders, who have no insurance set-up like a dealer reserve, depend upon to assure repayment of loans is police power. The auto dealers, too, fall into this group with the paper returned to them by lenders.

In advance of court action, collection procedures are tried, independent collection agencies may be called in, but early in the game references to legal action are a part of the collection pressure; and finally, garnishments or other judgments that become claims against real property are the inevitable punishment for the debtor who does not, or cannot, pay.

The buyer who signs the paper that makes him a debtor is seldom aware of how directly he has hazarded his total resources when he gives in to sales pressure. But the lenders and sellers are aware. They know how the law reads and how they would like it to read and how to change it, in session after state legislative session, to mold it closer to their objective of making police power a more effective and to them a less costly debt collection tool. What their efforts amount to, of course, is the creation of an even larger public subsidy for debt collection. Thus the country sheriff becomes a backstop for the salesman.

The tricks and strategems of the lender in the debt collecting process produce almost as many snares and pitfalls for the borrower as to those of the seller who induces buyers to become borrowers. Even among people whose social experience has been wide, there are only a few who are aware of how a debt can be, and is, escalated through the debt collection process; of how, for example, through a $195 debt a man can, as one did not long ago, lose a $5000 equity in his home. Here is an area of present-day living that we know little about. The debt collectors don't publicize it for the most obvious of reasons, and the debtors conceal it in shame. People don't like to talk about their debts.

Not only has the number of bankruptcies, for example, increased at an astonishing and puzzling rate during our great prosperity, but the percentage of those bankruptcies that are family, as opposed to business, financial failures has risen steadily. Today over 90% of the bankruptcies are consumer bankruptcies; the debts listed for the courts are debts for consumption purposes. Among the creditors listed by bankrupts, there are nearly always three and sometimes more personal loan companies. Usually these borrowings are consolidation loans, instalment personal loans at high interest rates—from 24% to 42%—to pay up other interest-bearing debt for goods. This kind of borrowing leads down a steep path to other loans for consolidation again and again, and interest on interest escalates the indebtedness at a tragic rate. A harbinger of things to come may lie in the fact that instalment personal loans, which account at present for about 25% of the consumer credit extant, are the most rapidly rising form of consumer debt today.

Why are so many people going bankrupt? Why, is it that on an up-curve of good times and with an unparalleled sustained increase in prosperity over many years bankruptcies multiply to unprecedented high figures?

One of the recent issues of U.S. News and World Report devotes a special feature to this inquiry.

U.S. News and World Report is hardly an ultra liberal publication it must be pointed out. It corroborates what many have been saying with grave warnings. A great deal of the cause originates out of the greed of retailers and the weakness and injustice built in bad state laws.

Annual loss from personal bankruptcies, says U.S. News and World Report, is one and one-half billion dollars, and the figure is going up. Experts clearly put the blame on the abuse of easy consumer credit. Bankruptcies have tripled in ten years. Say USNWR:

To most experts in the field, the main factor is the lure of easy credit. "A dollar down and a dollar a week" has given way to "no cash down and no payments for three months," or "no payments until spring," or ". . . until summer."

One leading authority is Linn K. Twinem, who for eight years has been chairman of the consumers bankruptcy committee of the American Bar Association.

Mr. Twinem tells "U.S. News and World Report" that about 1.5 billion dollars will "go down the bankruptcy drain" this year. That is counting personal bankruptcies only.

There are many reasons why people get "overextended on their debts," says Mr. Twinem. Many people, he explains, are "Misguided or misinformed" on money matters.

To most federal bankruptcy referees who face nearly a year's backlog of cases, ignorance and easy credit are the villains.

One of these referees says there are two big reasons for the bankruptcy boom. "One," he says, "I believe that credit is too easy. Second, credit is too expensive for the poor. A fellow buys a trailer for $4,000, and by the time he's through paying for it he has forked out $2,000 in credit charges. How crazy can you get?"

The race to keep up with the Joneses, consumer-credit counselors say, is being encouraged by some merchants, who use highly aggressive tactics in selling all sorts of consumer goods on credit.

Too many young families, these counselors say, cannot resist what looks like an easy way to enjoy immediately the good life that their parents waited decades to achieve.

Other factors cited: harassment by bill collectors and, in some states, laws that make garnishment of workers' wages so easy that many families feel driven to bankrutcy as the only way out.

What can be done? We believe that a beginning will be made by the passage of H.R. 11601. The need for outlawing garnishees has also been amply demonstrated. All too often they lead to harassment on the job at the very least and not infrequently loss of job. Moreover, in many cases the consumer was never properly served. "Sewer Service" is prevalent in many instances and most frequently the poorer the person the more likely that they were not served at all. It goes without saying, that these are also the people who can least afford to lose their job.

No comfort is to be found in a quirk in the consumer credit picture. A study, "The New Dimension in Mortgage Debt," published by the National Industrial Conference Board, reports that—

"Savings in the form of building up home equities by the consumer sector as a whole have abruptly abated. The annual withdrawals of equities now are approaching the annual amortizations on mortgage debt."

Cash realized by consumers through refinancing first mortgages or taking out second mortgages rose, according to the NICB study, from $4 billion in 1960 to $10 billion in 1963. On the basis of those totals and their rate of increase during the three years from 1960 to 1963, it is reasonable to postulate an annual withdrawal of home equities of $20 billion in the not too distant future. "Although in some instances home owners may decide to refinance to obtain better mortgage terms," comments the NICB, "cash is generally the sole objective . . ." And among the reasons for seeking cash the report lists "consolidation of short-term debt."

Refinancing or second mortgages for needed cash has been promoted by a segment of both sellers and lenders for a number of years but such promotion, especially for second mortgages, has been stepped up sharply. Unlike the refinanced first mortgage that usually runs 20 to even 30 years, the second deed is generally a short-term debt running for 36 to 60 months. Although the rates on these loans are quoted as from a 6% to 12% simple interest (depending on state real estate laws), the actual cost of such borrowing is much higher because, in addition to interest, other charges such as brokerage fees, finder's fees, investigation costs, etc., are levied as a front-end loan against the sum borrowed. The result is that the borrower may receive an amount that is as much as 30% to 40% less than the face of the note he signs. A *New York Times* (October 19, 1964) discussion of the rapid growth of second-mortgage financing cited the example of a debtor who, in return for $3000 cash, signed a second mortgage note for $5,075.

One business propaganda agency for the promotion of credit sends thousands upon thousands of booklets into our schools, publishes hundreds of analyses and fact books for our press, and is now establishing advisory and counselling services for debtors in city after city, is, as you might guess, really representing the sellers—the same sellers who tell us that they make more on the debt than they do on the goods. Here is where debt for consumption purposes in our times, in 1967, differs from that of other days. Extensions of consumer credit in the far, far past were understood to be exploitations of dire need. Extensions of consumer

credit in the fairly recent past, have been understood to be financial devices to promote the sale of goods. Today, however, the promotion of goods has become a device for the creation of interest-bearing debt. The nation's retail merchants at their annual convention in San Francisco 12 years ago put it succinctly with the phrase: "Bait the hook with merchandise."

It is obvious that urgent action is necessary. Action such as you are considering in H.R. 11601. The statistics of the U.S. Department of Commerce quite clearly show how necessary this legislation is. The U.S. Government paid $13 billion in interest on its $329 billion debt in 1966. In the same year U.S. Consumers paid nearly as much as $12 billion, in interest on installment debts, charge accounts and other loans of only $95 billion about three times the rate paid by government. Moreover, John Gorman, a Commerce Department economist, has figured out that nearly a fourth of the average family's income in 1966 went to pay off debts and the interest on debts.

Seven long years have passed since this legislation was introduced. Meanwhile, millions of our citizens have gotten themselves and their families into even greater financial difficulty due to a lack of curbs on the unbridled avarice of those in the credit business.

Bankers, small loan companies, retail merchants, and their various trade associations have violently opposed truth-in-lending from the beginning.

They have called it an attempt to hamstring private enterprise. They have described it as a move toward federal regulation of interest rates and credit charges. They have pleaded that it would be impossible to administer, because salesmen and sales clerks could not compute the finance charges they are asking the customer to pay.

These arguments are sheer and utter nonsense.

Truth-in-Lending imposes only two conditions on credit establishments and money-lenders. It would require them to tell their customers the total amount they are paying for credit:

*In dollars and cents.

*As an annual percentage rate on the loan or credit.

This is not regulation; it is simply disclosure.

A lender or credit house that is unwilling to do this must feel that it has something to hide. This, of course, is the point.

The credit houses and the loan companies know to the third decimal point exactly how much they charge for credit and at what annual rate. They have to know; it's how they make their money. They could provide their personnel with little tables—like the sales tax tables that perch on so many cash registers, and they do in many instances but to their salesmen only—that would give instant answers.

Nor is the requirement for a maximum finance charge unreasonable. Credit extended in an effective, useful and prudent manner can yield sufficiently to make much more handsome profits than many business organizations do.

The worst sufferers from excessive credit charges are those who can least afford them—the lower income groups. They have less cash, and greedy sellers can more easily exploit their need for credit. In addition, members of minority groups are often charged higher rates regardless of their personal credit standing.

But these are not the only victims. The well-to-do are also duped. The true rate of interest on one of the more popular college tuition loans was found to range from 26 to 54 per cent a year.

Servicemen are among the favorite targets, too. The Defense Department has sought to rescue them with a truth-in-lending directive of its own, requiring lenders to disclose finance charges and actual interest rates in transactions with men in uniform.

This very action by the Defense Department is some small indication of how serious the situation is in the area of credit. After all the Defense Department is essentially saying that these charlatans are prepared to take advantage even of men who are going to the battlefield and are prepared to die for their country. Furthermore, it is common practice for them to hound to death survivors of servicemen with means both legal and illegal which would shame the worst of us.

H.R. 11601 is necessary because businessmen have not learned that their continual wrongdoing must eventually lead to effective elimination of their evil deeds through meaningful legislation. It is not clear to them that accurate labelling and safe cars, for example, are ultimately in everyone's interest-including the businessman's. They fail to believe that honest business is the best business, as some learned a long time ago.

Yes, we are badly in need of legislation which will once again restore some sanity and decency to the area of credit.

In closing we believe it to be essential to remind you of some very vital statistics.

Half of all American families are now paying installment debt—two-thirds of them at last count—either had no money set aside for emergencies or had anywhere from $1 to $500 to tide them over in case of illness or death, loss of job or other disaster.

A full one-quarter of the poorest citizens, those families with incomes under $3,000 a year, were paying some installment debt. About half of these low-income debtors were spending at least 20 per cent of their incomes to pay off what they owe.

This is only part of the story. When the money we owe on our mortgages is included, a Commerce Department study shows that the average American family is using almost one quarter of the take-home pay to satisfy interest charges and to repay installments loans and mortgages.

There is mounting evidence that consumers are finding it more difficult to keep up their loan payments. A study by the American Bankers' Association discloses that at the end of April of this year, consumers were 30 days or more behind on 1.75 per cent of installment bank loans, the highest delinquency rate since the 1961 recession.

It is our sincere hope that your Committee will hold fast to the bill as it is presently written. That you will exert all of your might to assure its passage by the House and that out of the conference committee their emerge a bill closely resembling the present one.

We sincerely hope, that our expectations and your efforts will be rewarded with legislation which will do honor to the Congress of the United States and provide a measure of decency and protection to all of our citizens who have need of a credit vehicle.

Once again our sincere appreciation for your kindness in permitting us to be heard.

Mrs. SULLIVAN. Thank you very much for coming.

Tomorrow morning, we plan to complete this series of hearings, unless additional information is required. We will hear from the president of the Independent Bankers Association, and from representatives of the United Automobile Workers of America and the Idustrial Union Department of the AFL–CIO. We have received many communications from associations and organizations which have a direct interest in this legislation, or in some aspect of it, and those communications will go into our hearing record when appropriate.

The subcommittee will now recess until 10 o'clock Friday morning, August 18.

(Whereupon, at 12:30 p.m., the subcommittee recessed, to reconvene Friday, August 18, at 10 a.m.)

(The following material was subsequently submitted for the record:)

U.S. DEPARTMENT OF LABOR,
OFFICE OF THE SECRETARY,
Washington, September 6, 1967.

HON. LEONOR SULLIVAN,
Chairman, Subcommittee on Consumer Affairs, Committee on Banking and Currency, House of Representatives, Washington, D.C.

DEAR MADAM CHAIRMAN: At the conclusion of my testimony before your Subcommittee on August 17, 1967, on H.R. 11601 and related bills to provide for consumer credit protection, I was presented with two questions by counsel for the Subcommittee, and requested to furnish for the record my responses to them.

The questions and my responses are as follows:

"1. Mr. Secretary, are you aware of a study prepared by the Bureau of Business

and Economic Research of Michigan State University entitled 'An Analysis of Economic and Personal Factors Leading to Consumer Bankruptcies?' In this study, 80 percent of the persons who went bankrupt had been threatened with wage garnishment. Seventy-five percent of them indicated that garnishment or the threat of garnishment was the reason for their filing for bankruptcy. Do you agree, Mr. Secretary, that the correlation between consumer bankruptcies and wage garnishment has been adequately and positively established?"

I would agree that considerable evidence supports a conclusion that there is a correlation between consumer bankruptcies and wage garnishments. Our examination of the subject shows that there is a widespread opinion among judges, lawyers, economists and bankruptcy referees that there is a correlation. This is corroborated by the opinions of three referees in bankruptcy recently testifying from personal knowledge before the Subcommittee.

A study in 1965 by the Administrative Office of the United States Courts showed that bankruptcies were highest where wage garnishments were least restricted—Alabama (9,522) bankruptcies, Michigan (5,877), Ohio (14,850), Tennessee (8,602), and Oregon (3,080). Conversely, states strictly limiting or prohibiting garnishment had the fewest bankruptcies—Alaska (76), Pennsylvania (512), Texas (329), Florida (507), and South Carolina (140).

Evidence of a correlation between consumer bankruptcies and wage garnishments was among the considerations prompting me to call attention to the possible use of the bankruptcy powers as a Constitutional basis for developing measures to cope with the garnishment problem.

"2. Mr. Secretary, personal bankruptcies have risen from 19,033 in 1950 to 208,000 for the fiscal year ending June 1967. In the latter year consumer bankruptcies—that is wage earner bankruptcies—have accounted for over 190,000 of total personal bankruptcies. In excess of $1.25 billion in debts have been negated by such consumer bankruptcies. What, in your view, is the impact on our economy of this trend?"

I observe striking parallels between the upward trend in consumer bankruptcies and that of consumer credit, the latter expanding 40 times in the last 40 years. It is fair to assume that the credit abuses sought to be removed by legislation before the Subcommittee have been partially responsible for the credit-bankruptcy tandem. The removal of these abuses would likely tend to reduce the number of consumer bankruptcies and therefore have a wholesome impact upon the economy. In addition, I do not think I can overlook the personal tragedies of 190,000 persons and their families who found themselves so deep in financial trouble that they were forced to turn to bankruptcy for a solution.

If you wish any additional information concerning the subject matter of the proposals before you, I shall be pleased to assist you in any way that I can.

Sincerely,

W. WILLARD WIRTZ,
Secretary of Labor.

CONSUMER CREDIT PROTECTION ACT

FRIDAY, AUGUST 18, 1967

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON CONSUMER AFFAIRS
OF THE COMMITTEE ON BANKING AND CURRENCY,
Washington, D.C.

The subcommittee met, pursuant to recess, at 10:15 a.m. in room 2128, Rayburn House Office Building, Hon. Leonor K. Sullivan (chairman of the subcommittee) presiding.

Present: Representatives Sullivan and Stephens.

Mrs. SULLIVAN. The Subcommittee on Consumer Affairs will come to order.

This morning we will conclude our scheduled hearings into consumer credit and on the many bills now before us to regulate this vast industry which has brought to the American people the fruits of their future earnings, or perhaps, to put it another way, the enjoyment of their expectations.

None of us on this subcommittee opposes the use of credit, but we all hope that, as result of our efforts on this legislation, perhaps we can help all of the American people to have a better understanding of the costs of credit and thus be able to use it wisely. Our record is full of illustrations of the unwise and disastrous use of this magic device for acquiring goods or services you cannot at the moment pay for.

I want to pay tribute to the members of this subcommittee who were so faithful in attending our hearings, morning and afternoon, during the past 2 weeks. Mr. Annunzio asked me particularly to express his regrets to our witnesses this morning for his first absence—I think he has been at every session—but he had switched to today some engagements he had in Chicago last Friday in order to attend our hearing with the bankruptcy referees and that was before today's schedule was drawn up. I am sure other members who could not be present this morning also regret not being able to hear the final witness.

Our witnesses this morning come from the banking industry and from organized labor. It is very easy for us to remember when those two groups found nothing to share with each other except mutual distrust and perhaps bitter hatred. Things have changed so much for the better that a labor leader and a banker share many common problems and often solve them together.

Hence, I am going to ask all of the witnesses this morning to come to the witness table at one time and counsel with us.

We have the president of the Independent Bankers Association, Mr. Stanley R. Barber of Wellman, Iowa, accompanied by Mr. Howard Bell, of Sauk Center, Minn., executive director of an organization which is always welcome before the Committee on Banking and Currency; and, from the ranks of organized labor, Mr. Pat Greathouse, of Detroit, vice president of the United Automobile Workers of America. Mr. Jacob Clayman, administrative director of the Industrial Union Department of the AFL–CIO, was also scheduled for this morning but is not able to be here.

We have a lot of ground yet to cover in completing these hearings today and we have found that by having the witnesses make their presentations in turn, and then giving the members an opportunity to question any or all of them at one time, we can cover far more ground and make sure that each member can ask the question or questions he is most anxious to direct to a particular witness.

We also have with us Mr. Herbert O'Conor, Jr., former commissioner of banking for the State of Maryland. Mr. O'Conor, I understand that you would like to present to the committee a statement to be made part of the record since we may not have time to enable you to do it orally.

STATEMENT OF HERBERT R. O'CONOR, BALTIMORE, MD.

Mr. O'CONOR. I would have no objection if your schedule permitted it, but knowing that you have previous witnesses scheduled I will just offer it for the record if I may.

Mrs. SULLIVAN. We will be happy to accept it.

After we study your statement, if there are any questions that we would like to put to you, if we can give it to you in writing will you have your answers back to us in a few days?

Mr. O'CONOR. Very glad to do so. I would add this, I believe Mr. Keyserling testified on Wednesday.

He testified that he felt an 18-percent ceiling on interest was too high. I happen to agree with that. But I disagree with the fundamental practicality of trying to incorporate that in the bill this year. I think it is unrealistic to attempt it at this time and it might well destroy the passage of good legislation.

Thank you.

Mrs. SULLIVAN. Thank you very much for preparing a statement for our information, based on your extensive experience in this field.

(Mr. O'Conor's statement follows:)

STATEMENT OF HERBERT R. O'CONOR

I am Herbert R. O'Conor, of Baltimore, Maryland. I am a practicing member of the Maryland bar; my public service includes a term as State Bank Commissioner from May 1, 1963 until July 1 of this year. I do not purport to be an expert in the field of finance or a specialist in consumer loans or credit. Rather, I happen to be an interested citizen convinced that one of the essential safeguards to the system of government we all cherish is a well-informed public.

There can be no doubt about the fact that a very substantial portion of the American public is not aware of the true cost of borrowing money or obtaining credit in the purchase of goods and services. Much of this lack of understanding is due to the absence of meaningful and standard information about the various species of legitimate transactions.

Specifically, for example, the average person does not realize that neither a "6% discount loan" nor a "loan with 6% interest added on" really represents 6% interest. To the ordinary man "6% discount" suggests a cut in prices, a lower cost to him. In actuality the true rate of interest on a 6% loan discounted for five years is more than 15%. If the length of such a loan is for a longer period the rate of interest climbs steeply (e.g. at eight years it would be more than 18.5% interest). The true yield on a 6% add-on loan over a five year period is greater than 10.8%. Both methods of computing interest are allowed in Maryland.

It was reassuring, therefore, when the Senate approved S. 5 by a unanimous vote and it is encouraging to note that the House of Representatives is manifesting interest in similar legislation. It is most desirable that the two bodies agree on a bill this year while the circumstances are propitious.

Mrs. Sullivan and her cosponsors are to be commended for introducing a generally fine bill. H.R. 11601 would plug a number of loopholes in the otherwise desirable truth in lending bill passed by the Senate. The application of disclosure requirements to the advertising of credit as well as the actual transactions is a significant improvement. I do subscribe to the view expressed by Under Secretary of the Treasury Barr that the sure chance of passage which truth in lending has this year might be endangered if too much is attempted in one measure.

I support the inclusion of "revolving credit" under the bill, and agree in so doing with those who say that the quotation of an 18% per annum rate is considerably more useful and informative to the consumer and no more inaccurate than the frequently advertised "1½ per cent a month". When one first encounters the subject of interest in school, it is presented as an annual increment on principal. Because the great majority of experiences one has with interest thereafter are computed on a yearly basis, the original impression is enforced. The monthly statements showing a service charge of 1½% are simply not meaningful to the average housewife; she does understand 18% a year and if that is what she is being charged, that is what she is entitled to be told.

Even more essential, I feel, is the removal of the $10 exemption written into the bill in the Senate. Such an exception would remove the protection of this bill from those who need it most—the poor, who so often buy $25, $50 or $100 worth of, for example, furniture, without realizing that they are paying exorbitant prices for credit. A $10 exemption would be an open invitation to the unscrupulous to break up purchases into smaller units, on no one of which would the charge exceed $10.

The idea that credit transactions should be exempt if the amount involved is small is a fallacious one. It would be wrong to allow the people who most need help and some of whom are poor credit risks to begin with to place themselves deeper in debt without affording them the protection given the balance of society. This country must find a way to enable the impoverished to acquire necessities at reasonable costs. This challenge is one of the most difficult ones facing us in these evolving times. No one really believes the market place is going to be vacant just because the merchant is required to reveal the fact that the real price on an electric toaster is half again as much if its charged rather than paid for in cash.

On the question of whether or not first mortgages on homes should be included, there may be an honest difference of opinion as to the necessity of it. In this area, there is a real competitive market. In Maryland our savings banks, building and loan associations and insurance companies compete with each other and this promotes a low cost. Nonetheless, the rivalry among these fine segments of business and the fact that the most of them are above reproach does not mean that unconscionable lenders will not come along and take a first mortgage with outrageous terms.

In the area of second mortgages, there is no question as to the desirability of inclusion in your bill. No substantial price competition is now operative in this field, and the required disclosure of interest charges on such loans should be of significant benefit in safeguarding the consumer in this area. The Maryland Legislature has discharged its responsibility in this, as in other areas, by adopting a second mortgage law which requires, among other things, a complete disclosure of all finance costs in terms of simple annual interest. Such a requirement in the federal bill would be desirable and the list of exempt charges in the bill should be eliminated, since they offer substantial avenues for evasion and abuse in concealing interest charges, allowing a deceptively low annual interest rate to be quoted at the same time usury is committed in the padded charges.

I support the inclusion of credit insurance charges in the computation of the finance charge, since experience has shown that a heavy insurance charge with a hidden rebate to the lender is often used as a device for taking additional profit in the making of a loan. There might be excluded from the finance charge the insurance premium turned over to an insurer who is truly independent of the lender. In other words, the lender who requires the borrower to take the insurance should be made to include any commission he gets when he tells the borrower what his markup will be. Since the individual must incur this expense to obtain credit it is obviously part of his cost and it would be inconsistent with the fundamental principle of truth in lending to allow its exclusion when that individual is told what he is obligating himself to pay the lender.

I am apprehensive about the proposal of an 18% ceiling on interest. While it might help the residents of some states, it would also be used by lending interests to attempt to pressure legislators in states such as Maryland to relax their laws and allow a return which is neither justified nor currently allowed. It is my considered opinion that, for the present at least, the matter of interest ceilings and usuary laws is better left to the states. Traditionally the states have had the right and the duty to enact usury laws to protect unsophisticated and impecunious borrowers not equipped to shop for credit and unprotected by any real competition in the marketplace. Until and unless the states fail to meet their responsibility I for one do not favor preemption of the field of loan regulation by the Federal Government.

Professor Countryman in his able presentation to this Subcommittee pointed out that it is desirable to do more than protect wages from garnishment. I endorse his suggestion that assignment of future wages should be invalidated by legislation. It is difficult to imagine what would cripple a worker's morale more than the realization that he was working over a period of time for the benefit of a money lender to who he turned in an emergency.

Mrs. SULLIVAN. Now, Mr. Greathouse, Mr. Bell, Mr. Barber, will you please come to the witness table?

Mr. Barber, would you please introduce the gentlemen accompanying you, and after Mr. Barber does so, will you do the same for the record, Mr. Greathouse?

Mr. BARBER. I am Stanley R. Barber, president of the Independent Bankers Association of America and president of the Wellman Savings Bank in Wellman, Iowa. With me is Howard Bell of Sauk Centre, Minn., executive director of the association, and Horace R. Hansen of St. Paul, Minn., IBAA counsel.

Mrs. SULLIVAN. Mr. Greathouse, will you introduce your associates?

Mr. GREATHOUSE. Mr. Daniel S. Bedell of our Washington office, Mr. Paul Wagner and Mr. William Dodds from our Washington office.

Mrs. SULLIVAN. Mr. Barber, will you start with your statement? You may summarize it or read through it. It is quite short, I see.

STATEMENT OF STANLEY R. BARBER, PRESIDENT, INDEPENDENT BANKERS ASSOCIATION OF AMERICA; ACCOMPANIED BY HOWARD BELL, EXECUTIVE DIRECTOR; AND HORACE R. HANSEN, COUNSEL

Mr. BARBER. Our association, at its 1967 convention in New Orleans last March, adopted the following resolution:

Resolved, That the Independent Bankers Association of America is of the firm opinion that the public should be made fully cognizant of the actual interest rate being paid on any financial transaction: Now, therefore, be it

Resolved, That the Independent Bankers Association of America urges all companies, agencies or individuals extending credit to disclose this information fully and clearly; and further, this Association approves the passage of interest rates disclosure legislation, such as S. 5 and H.R. 949, provided any final bill

is in such form that it can be technically administered and applies to all extenders of credit.

The organization I represent, composed of some 6,500 National- and State-chartered community banks throughout the United States, believes strongly in the public's right to know the facts of a financial transaction.

We believe there is no valid reason why a customer or borrower should not have an accurate and understandable statement of the cost of borrowing and credit. We also believe this is in the public interest.

Presently, commercial banks effectively inform the consumer-borrower of financing charges. Comptroller of the Currency William B. Camp has testified before the Senate Banking and Currency Committee in praise of national bank performance in this area. We believe State banks have much the same performance record.

A subcommittee of our Federal Legislative Committee was appointed to study H.R. 11601 and H.R. 11602. Conclusions reached by this group at a meeting in Chicago on August 4 form the basis of this testimony.

Provisions of section 203 in the Sullivan bill, H.R. 11601, regarding disclosure of finance charges, follow generally S. 5 as adopted by the Senate and embodied here in the Widnall bill, H.R. 11602.

In both proposals, the Federal Reserve Board is designated as the agency to prepare regulations for implementing the legislation.

Should either bill become law, we are confident that the Board would promulgate fair and workable disclosure regulations. Such regulations would ease the burden of compliance by our member banks.

Section 204 of the Sullivan bill includes guidelines to the Board for writing regulations. These provide for tolerances, adjustments, and exceptions. Perhaps most important, so far as our member banks are concerned, is that the Board would prepare tables and charts for quick calculation of interest rate charges.

The Board should not, however, be made the policeman for all violations of all types of creditors as provided in the Sullivan bill section on administrative enforcement. These duties are not in keeping with its functions and it is not equipped to handle them. The testimony of the Board in the Senate on this point should be carefully reviewed. We believe the enforcement procedure of the Widnall bill is preferable.

As to the period for which the finance charge is to be disclosed, whether monthly or annually, it is the position of our association that the requirements should apply uniformly and equally to all types of creditors. Thus, whether the rate is disclosed on a monthly or annual basis, there would be for the borrower an ease of understanding exactly what he is paying.

Certainly the dollar amounts of finance charges should be disclosed on consumer loans. We recognize that it is difficult to arrive at an annual interest rate on credits containing variable terms. It is our sincere desire that the small banks forming the bulk of our association's membership could, under this legislation, continue to offer loans tailored to specific and particular needs of customers.

Section 211 of the Sullivan bill specifies July 1, 1968 as the effective date. We believe this date is too early and does not allow sufficient time for development of regulations that would be equitable for all segments of the credit industry.

Section 204 of the Sullivan bill permits the option of stating the finance charge in terms of dollars or percentage until July 1, 1968. Again, we believe this is too early. We suggest that the option continue until the Board has fully and carefully completed all of its rules and regulations, and has prepared its tables and charts for interest computations. The date for termination of the option should be fixed by the Board, but should be no later than January 1, 1972, the date set in the bill adopted by the Senate. During the option period, we believe lenders should be allowed to state finance charges in terms of dollars per hundred on the unpaid balance, as is now customary.

We agree with the Federal Reserve Board that if the total finance charge for a closed end credit is $10 or less, the transaction should be exempt from disclosure requirements.

The history of the legislation before you is that it is primarily designed to regulate consumer credit. We note that agriculture loans are now included among those on which disclosure would be required. We favor exclusion of agriculture loans from disclosure. Such loans are not in the consumer credit category.

We object to any provision that includes, as part of the cost of credit, the premium for credit life insurance. This adds an unnecessary complication to an already complicated piece of legislation. Credit life insurance is not a charge for lending money.

We have no objection to including the standards in the Sullivan bill as to advertising of credit terms. These are almost identical to requirements for disclosure statements. However, we feel that the phrase "specific credit terms" in subsection (j)(1) on page 15 is vague and needs clarification.

For example, assume an advertisement states only that auto loans may be repaid over a 36-month period, or states only that auto loans are available at "low bank rates," with no specifics as to rates or amounts of monthly payments. Would such statements violate this portion of the bill, or is the phrase "specific credit terms" intended to exempt such advertisements? The same question applies to the phrase "specific terms" in subsection (k) on page 16. We believe such statements should not be construed as being in violation of this section in the Sullivan bill.

There are three provisions in the Sullivan bill that are covered in State laws and we feel strongly these should be left to the State and not preempted by the Federal Government. They relate to the maximum interest rate (p. 17), confession of judgment (p. 17) and garnishment (pp. 33 and 34).

As to maximum interest rates, most States have legislation which, by virtue of Federal law, applies to national banks as well as State banks. The Congress long ago determined that the States are best able to decide what kind of banking accommodations suit their varying economies, not only as to interest charges but also as to other basic areas of bank regulation. What is best for an industrial State may not be best for an agricultural State. The Congress never has sought to preempt the financial field or to impose any rigid or monolithic system upon the States.

Garnishment of wages and confession of judgment as means of enforcing payment of loans have been long established and are the subject of State laws. These laws vary widely. There are no cogent reasons for the Federal Government to destroy these State laws. If properly designed, these laws furnish security and thus enhance availability of credit. Banks must be concerned with their depositors' money. To take away these forms of security is not in the public interest.

As to civil and criminal penalties, we feel that an aggrieved person should have a civil remedy, but only after any error or violation is discovered and the creditor has had a reasonable time to correct it.

For example, if the annual percentage rate is stated to be 6 percent and is actually 6½ percent, the customer should be paid the difference within 15 days after discovery by either party. If the creditor fails or refuses to pay within that time, only then should court action be permited.

The amount of judgment should be no more than the difference, plus reasonable costs. This is the practice in most collection situations in our courts today, and it should be no different here. The civil penalties stated in these bills are apt to unduly encourage lawsuits against creditors. We have no objection to severe penalties for habitual offenders.

We can see no reason for the bill to create the presumption that the creditor is dishonest and deliberately falsified the rate. If the creditor is in fact dishonest, that remedy should be under a limited criminal penalty.

The criminal provisions are too severe and we oppose them as written. They should be limited to permit their use only in case where the creditor "repeatedly, knowingly, and willfully" violates the law. The penalty should be limited to fines up to $5,000. The provision for imprisonment should be deleted.

As to penalties generally, we feel that in new and untried "fair practice" legislation such as this, initially it would be best to think in terms of moderate penalties.

We see no need for creation of a Commission on Consumer Finance. The Federal Reserve Board necessarily would consult with many representatives from all areas of the credit field in developing the contemplated regulations. No matter how well chosen, no nine-member commission could possibly represent a cross section. Furthermore, the Board and the Attorney General are required to give Congress and the President a full report each year on the experience under the act. This should be sufficient.

The section on commodity futures trading does not appear to us as being within the scope or purpose of these bills.

We see no point to the section on Presidential standby power, to cause controls over consumer credit. A "national emergency" is undefined and such drastic controls should be invoked only when Congress finds an emergency to exist. This section should be deleted.

In closing, I wish to reiterate our concern, previously expressed in our testimony on the Senate side, that disclosure legislation would put banks at a disadvantage in competing with captive finance companies controlled by manufacturers or retailers.

For example, an automobile dealer could adjust or "pack" the price of a car to the extent that he could quote a finance charge that was ostensibly lower than that available at a bank. A furniture dealer could do the same.

Under these circumstances, the total cost to the purchaser would be more than if he had bought a car or furniture at a fair price and had financed his purchase with a bank loan. Our estimate is the volume of such "rigged" transactions would increase sharply if disclosure proposals become law.

In prior years, the Congress has considered bills to force manufacturers to divest themselves of finance companies. Enactment of a law prohibiting a manufacturer from financing what he sells would be an effective roadblock to the type of "rigged" transactions we have mentioned. We believe that divestiture of captive finance companies should be considered in connection with this legislation.

If disclosure is to become a standard procedure, perhaps consideration should be given to a truth-in-packaging law, which would force the seller of merchandise or services to list on each sales tag or invoice his costs, plus his markup, expressed in amount and percentage.

In summary: Our association favors the objective of truth in lending but believes that great care must be exercised so that any legislation attempting to achieve this objective does not unduly restrict industry and commerce.

We are pleased to present our views to you and will attempt to answer any questions you may have.

Thank you for your attention.

Mrs. SULLIVAN. Thank you, Mr. Barber.

I would just like to make one comment before we go on and that is, we do have a truth-in-packaging law, but I am afraid it is as weak as the Senate bill on truth in lending, S. 5.

Mr. BARBER. I misstated when I suggested consideration might be given to truth in packaging and meant to say truth in pricing could be a logical further extension if true disclosure were to be made. This suggestion was somewhat with tongue in cheek.

Mrs. SULLIVAN. We have had some rather unsatisfactory experiences with the so-called truth-in-packaging law.

(The following letter from Mr. Barber was subsequently received and included in the record:)

INDEPENDENT BANKERS ASSOCIATION OF AMERICA,
Wellman, Iowa, August 29, 1967.

HON. LEONOR K. SULLIVAN,
Chairman, Subcommittee on Consumer Affairs of the Committee on Banking and Currency, Rayburn House Office Building, Washington, D.C.

MADAM CHAIRMAN: * * *

I wish to reaffirm the willingness of banking to make available full information regarding credit transactions. We ask only that the legislation be made applicable to all extenders of credit and that it not result in an undue burden to banking and other lenders. We noted in our testimony that we urge deletion of agricultural credit from disclosure legislation. Agricultural loans are very largely capital type credits. In addition, these loans are practically entirely on a simple interest basis. Our 6,500 banks are largely serving smaller agricultural communities and the additional effort of reporting this type of credit would be considerable.

We also wish to reemphasize what we feel is a real danger in disclosure legislation. This is the driving of interest rates underground and the elimination of

the two price system. As long as merchants have two avenues of profit, namely mark up on goods sold and interest on financing of goods sold, and lenders have only the latter, it is difficult for us to see how disclosure can be applied equitably to all segments of the industry. Short of a "truth-in-pricing" bill, or more correctly short of price controls and profit limitations, disclosure legislation cannot effectively curb discretionary pricing of profit margins and products with the result that finance charges can be concealed. This, obviously, bears unfairly on the banking industry, which we believe most agree has been following high ethical standards in lending.

Respectfully submitted.

STANLEY R. BARBER, *President.*

Mrs. SULLIVAN. Now, Mr. Greathouse, do you feel you would like to read through your statement or summarize it?

STATEMENT OF PAT GREATHOUSE, VICE PRESIDENT, UNITED AUTOMOBILE, AEROSPACE & AGRICULTURAL IMPLEMENT WORKERS OF AMERICA, AFL–CIO, AND FOR THE INDUSTRIAL UNION DEPARTMENT OF THE AFL–CIO; ACCOMPANIED BY DANIEL S. BEDELL, LEGAL REPRESENTATIVE; PAUL WAGNER, LEGAL REPRESENTATIVE; AND WILLIAM DODDS, DEPUTY DIRECTOR, LEGAL DEPARTMENT, UAW

Mr. GREATHOUSE. I would like to go through most of it. I will see if I can summarize it.

I now have the opportunity of speaking today not only for the million and a half members of our union but also speak for the Industrial Union Department of the AFL–CIO. Mr. Clayman will rely on the statement that I have here today.

There is no question about the significance of this legislation and the need for truth-in-lending as most all witnesses who have appeared before your committee have testified. We have followed the hearings closely and have read the testimony and certainly agree that this legislation is long overdue. We say in our statement at least 5 years overdue—I think the need for the legislation has been much greater than 5 years. But if you take the orignal submission made by Senator Douglas and allow for a couple of years, we think the legislation should have been enacted at least 5 years ago.

While the poor and the average factory worker are misled by current credit practices, middle-class and well-educated Americans also need the benefit of truth-in-lending legislation. A recent study revealed that four out of every 10 persons with a college education do not know how much they are paying in credit charges.

Truth-in-lending legislation can also make a definite contribution to lowering the cost of living for millions of American families. Interest on consumer credit amounted to some $13 billion in 1966. This legislation should result in cheaper credit for the American public. It will have an impact on the pockets and pocketbooks of men and women in all walks of life in all parts of the country. Furthermore, it will especially help those who are most deceived by present credit practices, the poor and the disadvantaged in the inner city ghettos and in the isolated rural slum areas.

Until now, the lack of effective price competition based upon accurate information has allowed high prices, excessive profits, and encouraged inefficient operations in the consumer credit field. Truth-in-lending will produce invigorated competition in the credit industry.

Lenders offering low interest rates should see an increase in their business, as is rightfully due to those who offer the lowest prices in our free economic system. Businessmen extending credit at higher interest rates will be under pressure to economize and increase the efficiency of their operations, or to work under lower profit margins than they have been accustomed to in the past.

Congress can contribute significantly to the war to eliminate poverty by enacting legislation to protect the consumer from the malpractices and misinformation that are all too common in the field of consumer credit. The poor have not escaped the mass media's bombardment of messages to buy now and pay later. Slogans such as "easy payments" and "no money down" have been very effective in luring even those on extremely limited incomes. The result is that substantial numbers of today's poor have been exploited in the marketplace. Many have become hopelessly entangled in problems of installment debt. Too often the consequences have been threats, legal penalties, and even loss of their jobs as a result of missed payments.

Because major department stores and other sources of reasonably priced credit are often unreachable and are not usually willing to extend credit to them, the poor usually fall prey to less scrupulous merchants.

Numerous studies have revealed how the poor pay higher prices and receive shoddy merchandise at the same time. On top of this, they pay usurious interest rates so that they wind up paying in total several times the usual retail price. Then, they are faced with the threat of repossession and losing their merchandise entirely if they are not able to keep up with the excessive payments they are required to make.

It is no wonder then that we discover that in the recent catastrophic rioting in Detroit, the victims of burning and arson included 32 furniture, appliance and hardware stores, and 23 clothing and jewelry stores. These types of outlets in ghetto areas are very often known for their excessive credit practices. Numerous stories on the riots appeared in the Detroit press alluding to the systematic burning of stores which were believed to engage in excessive credit practices. One columnist writing for the Detroit News claimed that:

> A Negro woman on relief set fire to a furniture store because she felt she would never be able to pay the bill she owed there. Due to the interest rate she was being forced to pay $910.12 to satisfy an original debt of $285.

While our society can never tolerate looting and burning no matter how deep the social injustices that breed these irrational and lawless acts, it seems to me that we can take some elemental steps right now to begin to eliminate the conditions that lead men to become looters and burners. The passage of the strong truth-in-lending provisions and other sections of H.R. 11601 which help to stamp out shady and immoral practices in the consumer credit field can do more to help maintain law and order in our cities than a dozen repressive antiriot bills.

The consumer is not the only one who will benefit from truth-in-lending legislation. Truth-in-lending will protect the ethical lenders and business merchants from losing business to unscrupulous competitors. An otherwise honest businessman is subject to tremendous pressure to adopt unethical credit practices by his unethical competitor in order to stay in business and earn a decent living. By requiring every lender to be truthful and to state the true interest rate in a uniform

manner, we can break the endless chain of misleading claims and shabby deceptions which now characterize too large a segment of the credit industry. Businessmen would be secure in the knowledge that higher cost competitors cannot lure away their customers with deceptive credit information.

While the modified truth-in-lending bill passed by the Senate represents progress in the long efforts to enact meaningful legislation in this area, a number of glaring weaknesses and loopholes are contained in that version which can seriously weaken the effectiveness of truth-in-lending protection. I am most happy to see that H.R. 11601, which your committee is considering, closes most of these loopholes.

The basic premise behind truth-in-lending legislation is that the true facts as to interest and financing charges and annual interest rates should be disclosed on all types of credit so that the public can compare and make a sound choice in obtaining credit. The omission from coverage in the Senate version of revolving credit accounts, and purchases where the finance charge is $10 or less, opens up glaring loopholes that could possibly nullify most of the protection provided by this legislation.

Revolving credit accounts is the fastest growing form of credit in the country today. In addition, the interest rate charged on these accounts is typically 18 percent a year, a most excessive rate of interest equal to the national interest rate ceiling recommended elsewhere in H.R. 11601. There is no reason why department stores, credit card plans, and others who offer revolving credit accounts cannot state their interest rate charge on an annual basis. If they are required to state only the monthly rate of interest, millions of consumers could be led to believe that the interest rates on these accounts are among the lowest available to them, where the actual fact, revolving credit accounts are one of the most costly forms of credit available.

The existence of such a glaring loophole as this can only encourage installment sellers and lenders to abandon other forms of credit that they now offer and operate on a revolving credit basis. The effect would be to water down considerably the protection that the consumer direly needs. Furthermore, it would place in an unfair competitive position those businessmen who would be required to state interest rates on an annual basis.

The exclusion from coverage under the Senate bill of debts of small amounts where finance charges are less than $10 is completely unjustified. Interest rates are often the highest on these smaller loans, where the cost of the item is $100 or less. Moreover, these smaller sized purchases make up the bulk of the credit buying for the average worker and for those living in poverty. The argument that the true interest charges are hard to compute in these cases, or that this would constitute a costly inconvenience to merchants does not hold up when elaborate tables have been prepared which avoid the need for the seller to do any computations. The only difference in computing interest charges and interest rates on a $100 loan as compared to a $1,000 loan or a $10,000 loan is one or two decimal points.

I am most happy to see that the bill your committee is considering does not allow such flimsy reasoning to stand in the way of providing needed protection for the low-income family making small purchases.

One of the greatest sources of credit problems for the workingman and the poverty stricken is the oversimplified, confusing, misleading, or blatantly deceptive advertising of credit and the sale of goods on credit. If truth-in-lending legislation is to be truly effective, the true facts of the interest charge and the interest rate should be available to the prospective customer before he has decided where he is to make a purchase or a loan. With the high-pressure salesmanship that exists in many retail establishments, the average worker does not have a truly free choice to determine where he can make his purchases on the most economical basis if he is initially misled by advertising of the cost of credit.

While we cannot mandate that the true cost of credit be inserted in all advertising of consumer goods, we should require that any advertising of credit costs state the truth about interest charges. The omission of advertising from the coverage in the Senate-passed bill is a grave weakness. The UAW strongly supports the provisions of the bill before your committee which bring advertising under truth-in-lending protection.

Other improvements in H.R. 11601, as compared to the Senate passed version of truth in lending which the UAW strongly supports, is the provision for full disclosure on charges on first mortgages, where discounts and the point system are most confusing to the average homebuyer, and the inclusion of insurance charges levied against consumer credit as part of total finance charges in computing the true cost of credit.

I would like to point out one area regarding the truth-in-lending provisions of the excellent bill before your committee that we in the UAW would like to see changed. This is the choice of the Federal Reserve Board as the agency charged with enforcing the truth-in-landing legislation. The Federal Reserve Board is an agency that is basically oriented toward the banking business. Furthermore, it has little or no experience in the consumer protection field, and has no staff ready to carry out the enforcement provisions in the bill.

In its place, we would recommend that enforcement of consumer credit legislation be placed in the hands of the Federal Trade Commission. The FTC is already in the field of advising and protecting the consumer. It has far more expertise in the fields of retail selling and advertising, has a history of dedicated efforts to protect the consumer from unjust, illegal, and fraudulent practices, and has an efficient system for monitoring advertising, for investigating complaints, and for instituting the type of proceedings called for to bring about compliance with this legislation.

I am sure that the members of this committee are aware that placing a law on the statute books does not in itself accomplish the end objective of providing adequate protection for the American people. I urge that you make every effort to provide the best mechanism for vigorous, efficient, and fair enforcement in the consumer credit field.

The UAW would like to go on record in strong support of the provisions of this bill that would outlaw wage garnishments. The device of garnisheeing wages is used with abandon by numerous unethical merchants who prey upon unsuspecting workers with their easy-payment schemes. The tragic results are pay envelopes reduced to the

point where workers can hardly support their families, inconvenience and extra costs for employers, substantial court costs imposed on taxpayers, disciplinary suspensions which make it even harder for workers to repay their debts, and outright dismissal and loss of employment.

Unscrupulous merchants often use the courts as a collection device without even attempting to use other legitimate means of collection. They often sell goods on credit when they know a worker is already overextended in debt, with the knowledge that they have a sure-fire method of collecting the payment.

Legitimate businesses with substantial reputations are able to collect on bad debts without resorting to garnishments. Merchants and creditors in Texas, Pennsylvania, and Florida, where garnishments are outlawed, have learned to adjust their collection practices without ill effects or any noticeable reduction in the volume of retail sales.

The statistics on the extent of garnishments are staggering. In just one court alone in the city of Detroit, the common pleas court, 55,000 garnishments were issued in 1966. It is estimated that 95 percent of these garnishments were issued by default where the defendant never defended himself from becoming garnished. This took place in spite of the fact that this court is a liberal court in dealing with this issue, and has established a conciliation system to attempt to settle debts without having to attach wages.

A most unfortunate side effect of the garnishment system is that the courts often become the "enemy" in the eyes of the poor. They become further convinced that the society which they come to know as the "system" only works against them and grinds them down.

A revealing study conducted among low-income families in New York City uncovered the fact that one out of every five of the families interviewed had been threatened with garnishments, had their wages garnished, or had goods repossessed. Typically, low-income families faced a major crisis of this type whenever the chief breadwinner became ill or unemployed.

The problems the poor face arising out of garnishments often go hand in hand with direct exploitation by merchants. In the same study in New York City mentioned above, David Caplovitz cited as typical this experience of a 28-year-old Puerto Rican man:

> I bought a set of pots and pans from a door-to-door salesman. They were of very poor quality and I wanted to give them back but they wouldn't take them. I stopped paying and told them to change them or take them back. I refused to pay . . . They started bothering me at every job I had. Then they wrote to my current job and my boss is taking $6 weekly from my pay and sending it to pay this.

An additional problem which compounds the consumer problems of low-income families is the fact that these families often do not know where to turn to for help if they are cheated by merchants. Even if they do know where to go for help, they are usually unable to obtain it. The New York City study pointed out that 64 percent of the families interviewed did not have any idea of where to obtain help against unscrupulous merchants. Furthermore, only 9 percent of the families who encountered these problems actually sought professional help, although more than one-third cited a source of help that they knew about.

It is apparent to the UAW that Congress must take additional steps to protect the consumer and to eliminate unethical practices in the merchandising and credit fields. The Commission on Consumer Finance provided under title III of this bill appears to provide an excellent vehicle to determine further steps of a regulatory or legislative nature needed to provide the long overdue protection that the consuming public deserves.

The provision of H.R. 11601 calling for a national ceiling on interest rates makes extremely good sense to the UAW. Excessive profits from interest charges for fast buck merchants and small loan companies who prey primarily on the poor should rapidly become a thing of the past. However, the ceiling of 18 percent established in this bill is too high. The 18-percent rate charged by many department stores on revolving credit is so excessive that it can actually result in a greater profit on the credit transaction than on the original sale of the item itself. Conventional bank rates and interest rates on commercial credit are very substantially lower than 18 percent. Credit unions are able to extend loans to working people and to the poor at about half that rate.

In its place, we would suggest a flexible ceiling that would be related to going interest rates such as the Federal Reserve Board's discount rate. Your committee might investigate what multiple of the discount rate would be most appropriate to provide a flexible and workable ceiling that would relate to changing conditions in the national economy. The difficulty with any flat rate is that it would have to be high enough to provide adequate leeway in a tight money market when interest rates are extremely high generally. When you do this, however, the ceiling does not provide any significant protection against usurious interest rates in normal times when interest rates are low.

Madam Chairman and members of the subcommittee, the UAW would like to go on record in opposition to that portion of H.R. 11601 which would provide for emergency control of consumer credit by the President of the United States. This provision does not come under the scope of consumer credit protection. Rather, it deals with overall economic policy. It is a form of economic control to which the UAW is opposed. It could only lead to hardships for the individual consumer in need of credit, while the major borrowers in this country, business and industry, would not be subject to such controls. It would constitute discriminatory legislation, applying only to those with the least ability to overcome the consequences of such legislation. There appears to be no need to enact any ecoonmic controls over credit in the present state of the economy, nor does it appear likely that emergency credit controls will be needed in the foreseeable future.

The provision in H.R. 11601 which prohibits the use of confessions of judgment in consumer credit transactions is highly deserving of legislative enactment. This device, used by predatory merchants to induce debtors to waive their legal rights to contest any judgments that may be entered against them, is an excellent example of how our legal system is perverted to exploit the poor.

Typically, such a clause is inserted in the fine print of the contract which the borrower is required to sign. There is no justification for allowing this practice where the typical individual has no knowledge and no bargaining power to enable him to avoid surrendering valuable

legal rights, and thus become subject to severe financial hardship at a later date.

In a similar fashion, the UAW feels additional protection is needed to prohibit entirely the use of wage assignments in the consumer credit field. Here is another example where a borrower is placed under extreme pressure, often without any knowledge or full understanding of the consequence, to sign away his rights and allow a creditor to attach his wages at any time in the future that he sees fit. These so-called "voluntary" agreements to attach wages are coercive rather than voluntary in the typical seller-purchaser relationship. Since wage assignments have many of the pernicious effects of wage garnishments, both should be treated the same and abolished in the same legislation.

Another area where your committee should act to protect the consumer is to regulate the pernicious practices of many merchants in repossessing goods purchased on credit. This is particularly a problem in "add-on" purchases, where a merchant sells another item on credit before a purchaser completes payments on the original item that he bought.

If the customer misses one payment, merchants have often repossessed both items, even though the amount already paid has been more than enough to completely repay the outstanding debt on the original item. Actual situations have been reported in the press where four or more items purchased on an add-on installment basis have been repossessed, even though the value of one item alone was sufficient to satisfy the outstanding debt.

Legislation should prohibit the repossession of any item whenever full payment has already been made. The language of the legislation could provide that when debt is outstanding on two or more items, payments be allocated to each of the items, based on the ratio of the original purchase price of each of the items to the other items. Further, repossessions should be limited by statute to the extent necessary to satisfy any outstanding debt. Merchants should also be required to return to the purchaser any proceeds gained from the sale of the repossessed items that is over and above the amount of debt still owing.

There are a number of additional areas requiring legislative protection which this committee should seriously consider. Many of the abuses and shady practices could be eliminated from the credit field if lenders and merchants offering goods on credit were licensed and had to meet adequate standards covering the entire scope of their lending practices.

The lack of adequate legal recourse for consumers who have outstanding debt on shoddy and defective merchandise needs to be remedied. The common abuse of using fine print to prevent customers from knowing what they are signing could be abolished by requiring print to be a certain minimum size on credit contracts. Steps might also be taken to simplify the obscure legal language on credit contracts so that customers would know exactly what they were agreeing to.

Madam Chairman, I want to thank you for the opportunity of appearing here today to express the views of the UAW. I hope I have spelled out for you very frankly the areas where our union would like

to see positive congressional action. We are aware of political realities, and do not take the position that the bill that comes out of your committee this year need contain all of our recommendations. We would leave it up to you and your committee to determine how much can be passed through the Congress this year and how much might be enacted next year and in subsequent years.

The members of our union are extremely gratified with the efforts of you and your committee to enact long-overdue reforms in the field of consumer credit. You may be assured that the UAW will stand strongly behind your efforts to adequately protect the American consumer.

We hereby enlist in your crusade for the duration.

(The complete statement of Mr. Greathouse follows:)

STATEMENT OF PAT GREATHOUSE, VICE PRESIDENT, UNITED AUTOMOBILE, AEROSPACE & AGRICULTURAL IMPLEMENT WORKERS OF AMERICA, AFL–CIO

Madame Chairman and Members of the Subcommittee, I am grateful for the opportunity to appear here today to express the strong support of the 1,500,000 members of the UAW and the 5,000,000 other members of the Industrial Union Department, AFL–CIO (IUD) for the measures that you are considering to provide long overdue protection for the American public in the field of consumer credit. The bill that you are considering, H.R. 11601, is a piece of pioneering legislation of substantial significance that can be of great benefit to the average American family. This bill not only incorporates strong truth-in-lending provisions that should have been enacted at least five years ago, but also contains additional provisions that can begin to reform other predatory practices in the consumer credit field that have worked untold hardships on millions of American families.

The Need for Truth-in-Lending

Truth-in-Lending legislation is sorely needed to protect the consumer's right to know the full facts about credit rates and interest charges so that he can compare all alternatives and make an intelligent choice among the various credit plans that may be available to him at any given time.

President Johnson stated this very simply in his 1967 Message to the Congress on Consumer Protection:

"The consumer has the right to know the cost of this key item [credit] in his budget just as much as the price of any other commodity he buys . . . The consumer should not have to be an actuary or mathematician to understand the rate of interest that is being charged."

While the poor and the average factory worker are misled by current credit practices, middle-class and well-educated Americans also need the benefit of truth-in-lending legislation. A recent study revealed that 4 out of every 10 persons with a college education do not know how much they are paying in credit charges.

Truth-in-lending legislation can also make a definite contribution to lowering the cost of living for millions of American families. Interest on consumer credit amounted to some $13 billion in 1966. This legislation should result in cheaper credit for the American public. It will have an impact on the pockets and pocketbooks of men and women in all walks of life in all parts of the country. Furthermore, it will especially help those who are most deceived by present credit practices, the poor and the disadvantaged in the inner city ghettos and in the isolated rural slum areas.

Until now, the lack of effective price competition based upon accurate information has allowed high prices, excessive profits, and encouraged inefficient operations in the consumer credit field. Truth-in-lending will produce invigorated competition in the credit industry. Lenders offering low interest rates should see an increase in their business, as is rightfully due to those who offer the lowest prices in our free economic system. Businessmen extending credit at higher interest rates will be under pressure to economize and increase the efficiency of their operations, or to work under lower profit margins than they have been accustomed to in the past.

The Poor are Victimized

Congress can contribute significantly to the war to eliminate poverty by enacting legislation to protect the consumer from the malpractices and misinformation that are all too common in the field of consumer credit. The poor have not escaped the mass media's bombardment of messages to buy now and pay later. Slogans such as "easy payments" and "no money down" have been very effective in luring even those on extremely limited incomes. The result is that substantial numbers of today's poor have been exploited in the marketplace. Many have become hopelessly entangled in problems of installment debt. Too often the consequences have been threats, legal penalties, and even loss of their jobs as a result of missed payments.

Because major department stores and other sources of reasonably priced credit are often unreachable and are not usually willing to extend credit to them, the poor usually fall prey to less scrupulous merchants.

Numerous studies have revealed how the poor pay higher prices and receive shoddy merchandise at the same time. On top of this, they pay usurious interest rates so that they wind up paying in total several times the usual retail price. Then, they are faced with the threat of repossession and losing their merchandise entirely if they are not able to keep up with the excessive payments they are required to make.

Is it then no wonder that we discover that in the recent catastrophic rioting in Detroit, the victims of burning and arson included 32 furniture, appliance and hardware stores, and 23 clothing and jewelry stores. These types of outlets in ghetto areas are very often known for their excessive credit practices. Numerous stories on the riots appeared in the Detroit press alluding to the systematic burning of stores which were believed to engage in excessive credit practices. One columnist writing for the *Detroit News* claimed that:

"A Negro woman on relief set fire to a furniture store because she felt she would never be able to pay the bill she owed there. Due to the interest rate she was being forced to pay $910.12 to satisfy an original debt of $285."

While our society can never tolerate looting and burning no matter how deep the social injustices that breed these irrational and lawless acts, it seems to me that we can take some elemental steps *right now* to begin to eliminate the conditions that lead men to become looters and burners. The passage of the strong truth-in-lending provisions and other sections of H.R. 11601 which help to stamp out shady and immoral practices in the consumer credit field can do more to help maintain law and order in our cities than a dozen repressive anti-riot bills.

Ethical Merchants Protected

The consumer is not the only one who will benefit from truth-in-lending legislation. Truth-in-lending will protect the ethical lenders and business merchants from losing business to unscrupulous competitors. An otherwise honest businessman is subject to tremendous pressure to adopt unethical credit practices by his unethical competitor in order to stay in business and earn a decent living. By requiring every lender to be truthful and to state the true interest rate in a uniform manner, we can break the endless chain of misleading claims and shabby deceptions which now characterize too large a segment of the credit industry. Businessmen would be secure in the knowledge that higher cost competitors cannot lure away their customers with deceptive credit information.

Senate Version Must Be Strengthened

While the modified truth-in-lending bill passed by the Senate represents progress in the long efforts to enact meaningful legislation in this area, a number of glaring weaknesses and loopholes are contained in that version which can seriously weaken the effectiveness of truth-in-lending protection. I am most happy to see that H.R. 11601, which your committee is considering, closes most of these loopholes.

The basic premise behind truth-in-lending legislation is that the true facts as to interest and financing charges and annual interest rates should be disclosed on all types of credit so that the public can compare and make a sound choice in obtaining credit. The omission from coverage in the Senate version of revolving credit accounts, and purchases where the finance charge is $10 or less, opens up glaring loopholes that could possibly nullify most of the protection provided by this legislation.

Cover Revolving Credit

Revolving credit accounts is the fastest growing form of credit in the country today. In addition, the interest rate charged on these accounts is typically 18 percent a year, a most excessive rate of interest equal to the national interest rate ceiling recommended elsewhere in H.R. 11601. There is no reason why department stores, credit card plans, and others who offer revolving credit accounts cannot state their interest rate charge on an annual basis. If they are required to state only the monthly rate of interest, millions of consumers could be led to believe that the interest rates on these accounts are among the lowest available to them, where in actual fact, revolving credit accounts are one of the most costly forms of credit available. The existence of such a glaring loophole as this can only encourage installment sellers and lenders to abandon other forms of credit that they now offer and operate on a revolving credit basis. The effect would be to water down considerably the protection that the consumer direly needs. Furthermore, it would place in an unfair competitive position those businessmen who would be required to state interest rates on an annual basis.

No Exclusion for Small Purchasers

The exclusion from coverage under the Senate bill of debts of small amounts where finance charges are less than $10 is completely unjustified. Interest rates are often the highest on these smaller loans, where the cost of the item is $100 or less. Moreover, these smaller sized purchases make up the bulk of the credit buying for the average worker and for those living in poverty. The argument that the true interest charges are hard to compute in these cases, or that this would constitute a costly inconvenience to merchants does not hold up when elaborate tables have been prepared which avoid the need for the seller to do any computations. The only difference in computing interest charges and interest rates on a $100 loan as compared to a $1,000 loan or a $10,000 loan is one or two decimal points.

I am most happy to see that the bill your committee is considering does not allow such flimsy reasoning to stand in the way of providing needed protection for the low income family making small purchases.

Critical Need To Cover Advertising

One of the greatest sources of credit problems for the working man and the poverty stricken is the oversimplified, confusing, misleading, or blantantly deceptive advertising of credit and the sale of goods on credit. If truth-in-lending legislation is to be truly effective, the true facts of the interest charge and the interest rate should be available to the prospective customer before he has decided where he is to make a purchase or a loan. With the high pressure salesmanship that exists in many retail establishments, the average worker does not have a truly free choice to determine where he can make his purchases on the most economical basis if he is initially misled by advertising of the cost of credit.

While we cannot mandate that the true cost of credit be inserted in all advertising of consumer goods, we should require that any advertising of credit costs state the truth about interest charges. The omission of advertising from the coverage in the Senate-passed bill is a grave weakness. The UAW and the IUD strongly supports the provisions of the bill before your committee which bring advertising under the truth-in-lending protection.

Other improvements in H.R. 11601 as compared to the Senate passed version of truth-in-lending which the UAW and the IUD strongly supports is the provision for full disclosure on charges on first mortgages, where discounts and the point system are most confusing to the average home buyer, and the inclusion of insurance charges levied against consumer credit as part of total finance charges in computing the true cost of credit.

F.T.C. Should Enforce Law

I would like to point out one area regarding the truth-in-lending provisions of the excellent bill before your committee that we in the UAW and IUD would like to see changed. This is the choice of the Federal Reserve Board as the agency charged with enforcing the truth-in-lending legislation. The Federal Reserve Board is an agency that is basically oriented towards the banking business. Furthermore, it has little or no experience in the consumer protection field, and has no staff ready to carry out the enforcement provisions in the bill.

In its place, we would recommend that enforcement of consumer credit legislation be placed in the hands of the Federal Trade Commission. The FTC is

already in the field of advising and protecting the consumer. It has far more expertise in the fields of retail selling and advertising, has a history of dedicated efforts to protect the consumer from unjust, illegal and fraudulent practices, and has an efficient system for monitoring advertising for investigating complaints and for instituting the type of proceedings called for to bring about compliance with this legislation.

I am sure that the members of this committee are aware that placing a law on the statute books does not in itself accomplish the end objective of providing adequate protection for the American people. I urge that you make every effort to provide the best mechanism for vigorous, efficient, and fair enforcement in the consumer credit field.

We Should Abolish Wage Garnishments

The UAW and the IUD would like to go on record in strong support of the provisions of this bill that would outlaw wage garnishments. The device of garnisheeing wages is used with abandon by numerous unethical merchants who prey upon unsuspecting workers with their easy payment schemes. The tragic results are pay envelopes reduced to the point where workers can hardly support their families, inconvenience and extra costs for employers, substantial court costs imposed on taxpayers, disciplinary suspensions which make it even harder for workers to repay their debts, and outright dismissal and loss of employment. Unscrupulous merchants often use the courts as a collection device without even attempting to use other legitimate means of collection. They often sell goods on credit when they know a worker is already over-extended in debt, with the knowledge that they have a sure-fire method of collecting the payment.

Legitimate businesses with substantial reputations are able to collect on bad debts without resorting to garnishments. Merchants and creditors in Texas, Pennsylvania, and Florida, where garnishments are outlawed, have learned to adjust their collection practices without ill effects or any noticeable reduction in the volume of retail sales.

The statistics on the extent of garnishments are staggering. In just one court alone in the City of Detroit, the Common Pleas Court, 55,000 garnishments were issued in 1966. It is estimated that 95 percent of these garnishments were issued by default where the defendant never defended himself from becoming garnisheed. This took place in spite of the fact that this court is a liberal court in dealing with this issue, and has established a conciliation system to attempt to settle debts without having to attach wages.

A most unfortunate side effect of the garnishment system is that the courts often become the "enemy" in the eyes of the poor. They become further convinced that the society which they come to know as the "system" only works against them and grinds them down.

A revealing study conducted among low income families in New York City uncovered the fact that one out of every five of the families interviewed had been threatened with garnishments, had their wages garnisheed, or had goods repossessed. Typically, low income families faced a major crisis of this type whenever the chief breadwinner became ill or unemployed.

The problems the poor face arising out of garnishments often go hand in hand with direct exploitation by merchants. In the same study in New York City mentioned above, David Caplovitz cited as typical this experience of a 28 year old Puerto Rican man:

"I bought a set of pots and pans from a door-to-door salesman. They were of very poor quality and I wanted to give them back but they wouldn't take them. I stopped paying and told them to change them or take them back. I refused to pay. . . . They started bothering me at every job I had. Then they wrote to my current job and my boss is taking $6 weekly from my pay and sending it to pay this."

An additional problem which compounds the consumer problems of low income families is the fact that these families often do not know where to turn to for help if they are cheated by merchants. Even if they do know where to go for help, they are usually unable to obtain it. The New York City study pointed out that 64 percent of the families interviewed did not have any idea of where to obtain help against unscrupulous merchants. Furthermore, only nine percent of the families who encountered these problems actually sought professional help, although more than one-third cited a source of help that they knew about.

It is apparent to the UAW and the IUD that Congress must take additional steps to protect the consumer and to eliminate unethical practices in the mer-

chandising and credit fields. The Commission on Consumer Finance provided under Title III of this bill appears to provide an excellent vehicle to determine further steps of a regulatory or legislative nature needed to provide the long overdue protection that the consuming public deserves.

National Interest Rate Ceiling

The provision of H.R. 11601 calling for a national ceiling on interest rates makes extremely good sense to the UAW and the IUD. Excessive profits from interest charges for fast buck merchants and small loan companies who prey primarily on the poor should rapidly become a thing of the past. However, the ceiling of 18 percent established in this bill is too high. The 18 percent rate charged by many department stories on revolving credit is so excessive that it can actually result in a greater profit on the credit transaction than on the original sale of the item itself. Conventional bank rates and interest rates on commercial credit are very substantially lower than 18 percent. Credit unions are able to extend loans to working people and to the poor at about half that rate.

In its place, we would suggest a flexible ceiling that would be related to going interest rates such as the Federal Reserve Board's discount rate. Your committee might investigate what multiple of the discount rate would be most appropriate to provide a flexible and workable ceiling that would relate to changing conditions in the national economy. The difficulty with any flat rate is that it would have to be high enough to provide adequate leeway in a tight money market when interest rates are extremely high generally. When you do this, however, the ceiling does not provide any significant protection against usurious interest rates in normal times when interest rates are low.

UAW and IUD Opposes Emergency Credit Controls

Madame Chairman and members of the subcommittee, the UAW and the IUD would like to go on record in opposition to that portion of H.R. 11601 which would provide for emergency control of consumer credit by the President of the United States. This provision does not come under the scope of consumer credit protection. Rather, it deals with overall economic policy. It is a form of economic control to which the UAW and the IUD are opposed. It could only lead to hardships for the individual consumer in need of credit, while the major borrowers in this country, business and industry, would not be subject to such controls. It would constitute discriminatory legislation, applying only to those with the least ability to overcome the consequences of such legislation. There appears to be no need to enact any economic controls over credit in the present state of the economy, nor does it appear likely that emergency credit controls will be needed in the foreseeable future.

Ban Confessions of Judgment

The provision in H.R. 11601 which prohibits the use of confessions of judgments in consumer credit transactions is highly deserving of legislative enactment. This device, used by predatory merchants to induce debtors to waive their legal rights to contest any judgments that may be entered against them, is an excellent example of how our legal system is perverted to exploit the poor. Typically, such a clause is inserted in the fine print of the contract which the borrower is required to sign. There is no justification for allowing this practice where the typical individual has no knowledge and no bargaining power to enable him to avoid surrendering valuable legal rights, and thus become subject to severe financial hardship at a later date.

Prohibit Wage Assignments

In a similar fashion, the UAW and the IUD feels additional protection is needed to prohibit entirely the use of wage assignments in the consumer credit field. Here is another example where a borrower is placed under extreme pressure, often without any knowledge or full understanding of the consequence, to sign away his rights and allow a creditor to attach his wages at any time in the future that he sees fit. These so-called "voluntary" agreements to attach wages are coercive rather than voluntary in the typical seller-purchaser relationship. Since wage assignments have many of the pernicious effects of wage garnishments, both should be treated the same and abolished in the same legislation.

Regulate Repossession Practices

Another area where your committee should act to protect the consumer is to regulate the pernicious practices of many merchants in repossessing goods pur-

chased on credit. This is particularly a problem in "add-on" purchases, where a merchant sells another item on credit before a purchaser completes payments on the original item that he bought. If the customer misses one payment, merchants have often repossessed both items, even though the amount already paid has been more than enough to completely repay the outstanding debt on the original item. Actual situations have been reported in the press where four or more items purchased on an add-on installment basis have been repossessed, even though the value of one item alone was sufficient to satisfy the outstanding debt.

Legislation should prohibit the repossession of any item whenever full payment has already been made. The language of the legislation could provide that when debt is outstanding on two or more items, payments be allocated to each of the items, based on the ratio of the original purchase price of each of the items to the other items. Further, repossessions should be limited by statute to the extent necessary to satisfy any outstanding debt. Merchants should also be required to return to the purchaser any proceeds gained from the sale of the repossessed items that is over and above the amount of debt still owing.

Other Areas for Future Action

There are a number of additional areas requiring legislative protection which this committee should seriously consider. Many of the abuses and shady practices could be eliminated from the credit field if lenders and merchants offering goods on credit were licensed and had to meet adequate standards covering the entire scope of their lending practices. The lack of adequate legal recourse for consumers who have outstanding debt on shoddy and defective merchandise needs to be remedied. The common abuse of using fine print to prevent customers from knowing what they are signing could be abolished by requiring print to be a certain minimum size on credit contracts. Steps might also be taken to simplify the obscure legal language on credit contracts so that customers would know exactly what they were agreeing to.

Madame Chairman, I want to thank you for the opportunity of appearing here today to express the views of the UAW and the IUD. I hope I have spelled out for you very frankly the areas where our union would like to see positive Congressional action. We are aware of political realities, and do not take the position that the bill that comes out of your committee this year need contain all of our recommendations. We would leave it up to you and your committee to determine how much can be passed through the Congress this year and how much might be enacted next year and in subsequent years.

The members of our unions are extremely gratified with the efforts of you and your committee to enact long overdue reforms in the field of consumer credit. You may be assured that the UAW and the IUD will stand strongly behind your efforts to adequately protect the American consumer. We hereby enlist in your crusade for the duration.

Mrs. SULLIVAN. Thank you, Mr. Greathouse.

Before Mr. Stephens and I begin to question you, I want to say that I am sorry that you gentlemen have not had a better attendance of members of the subcommittee this morning. You both have given outstanding and important testimony.

I will make sure that all of the members do receive copies of your statements, however, and I will personally urge them to read your testimony.

I would like to call your attention to an article by Sylvia Porter in last night's Washington Star. It describes how to cut costs on your mortgage. I think it is one of the best examples of what we are trying to accomplish in this legislation—to show people what they are actually paying for credit and to help them, through this knowledge, to make intelligent decisions on how long a period, for instance, their mortgages should be written for. Without objection, I will place it in the record at this point.

(The article referred to follows:)

[From the Washington (D.C.) Evening Star, Aug. 17, 1967]

How To Cut Costs on Your Mortgage

(By Sylvia Porter)

How much money could you save by repaying your home mortgage in 20 years instead of 30 years?

What is the difference to you over the long range if your home mortgage interest rate is 6 percent as against 6.5 percent.

Or if you make a big vs. a small down payment?

These are three key questions to explore if you are now shopping for a home mortgage. And these are three key areas in which you can achieve significant savings.

As a guide to the right answers for you, this column will give the pertinent dollars-and-cents comparisons.

On interest rates, you'll probably find that all major lenders in your area offer home mortgages at similar interest rates. Nevertheless, a seemingly minor difference can mean hundreds of dollars in savings over the life of the mortgage. Here's the comparison for a $10,000 mortgage with a 20-year repayment period:

Interest rate (percent):	*Total interest*
6	$7,194
6.5	7,893
7	8,607
7.5	9,334

From this table, it's easy enough to see that even ½ percent on a $10,000 loan can mean savings in the $600–700 range over a 20-year period, and that a difference of 1 percent can mean savings of nearly $1,500.

If you shorten the repayment period of your $10,000 mortgage, your savings are even more dramatic. Here's the comparison for a $10,000 mortgage at 6 percent interest over various repayment periods:

Repayment period:	*Total interest cost*
10 years	$3,322
15 years	5,190
20 years	7,193
25 years	9,329
30 years	11,582

From this table, it's obvious you can save $4,388 in interest simply by repaying the mortgage in 20 instead of 30 years.

Of course, if you sharply reduce the repayment period of your loan, you'll have to pay more each month. Using the example of a $10,000 mortgage at 6 percent:

Repayment period:	*Monthly payment*
10 years	$111
15 years	84
20 years	71
25 years	64
30 years	60

The longer repayment period seems attractive but you've already read how much extra interest you pay when you stretch out.

The larger your down payment, the smaller will be the amount of your mortgage, and thus the smaller will be the amount of interest you will pay over the years, and the cheaper will be the over-all cost of the loan to you.

The average loan-to-price ratio in the nation today for a new home is 74.9 percent—i.e., the average mortgage being granted is for about 75 percent of the purchase price and the average down payment is 25 percent.

But averages are useless in terms of individuals. Your key rules for savings on your home mortgage are: shop for the lowest available interest rate in your area, make the largest feasible down payment, repay your mortgage in the shortest feasible period of time.

Mrs. SULLIVAN. She has taken a $10,000 mortgage for comparison, starting with a 20-year repayment period.

She shows if it is a 6 percent, you pay a total of $7,194 in 20 years. If it is at 6½ percent, the total is $7,893. If it is at 7 percent, the interest total is $8,607. At 7½ percent, the total of interest you pay would be $9,334.

Then taking this same $10,000 mortgage at 6 percent, she shows what the total interest cost would be for a repayment period of 10 years, 15 years, 20 years, 25 years, and 30 years. The interest on a $10,000 mortgage at 6 percent runs to $11,582 over a 30-year period. Then she also points out that for this mortgage of $10,000 at 6 percent for a repayment period of 10 years, the monthly amortization cost would be $111. And she goes on for 15, 20, 25, up to 30 years. For 30 years the monthly payment would be $60. In entering into a mortgage, you sort of gage what your income hopes are for the next few years, at least, in order to determine how much you can afford to pay a month and, from that, determine how long you want the mortgage to run. It gives the family an opportunity to look over the various alternatives and make a judgment. We were told by FHA that they do give a very clear picture of the entire cost of an FHA mortgage for its full term, but I don't know if they break it down this clearly. This information is instructive, and it gives people a choice.

They may decide, well, maybe I better not take a 30-year mortgage—maybe a 20-year one would be better, and if it only costs $11 more a month—$71 a month instead of $60—maybe we can find some way to pay that extra $11 a month and cut down the term of our mortgage by 10 full years and save $4,389 in interest.

There are usually similar choices in any form of credit transaction, but too many people don't realize that in buying on credit they are using somebody else's money to satisfy their wants and desires, and that this is expensive. Credit is pictured in such a different light to the public today that people are encouraged to satisfy every desire whether or not they can afford it, not realizing that there is a substantial cost to them in such transactions.

They just come in, sign their names, pay for it as they use the goods or services—which is good, if people are able to carry the finance costs of things they want to buy—but often these extra costs are hidden and disguised, or deceptively represented as being free.

Mr. Greathouse, I was glad to receive your support on the proposal for an interest rate ceiling, for the garnishment provision, and for some of the other things in H.R. 11601. The fear has been expressed, however, that the 18-percent ceiling would result in raising all rates to that level. Do you think that that would happen or do you feel that many consumers are now paying far more than 18 percent?

Mr. GREATHOUSE. There are consumers that are paying more than that, but there are also a number of consumers that are paying less than this.

We share the fear that setting this at 18 percent, even, would become the floor as well as the ceiling. While we think that sometimes 18 percent might be proper, there are other times when interest rates generally are lower and there should also be a lower ceiling on interest rates here for consumer credit. Just as there are lower interest rates for other forms of credit.

Mrs. SULLIVAN. I realize that danger in trying to set any Federal interest rate for borrowing. But I think many people just don't realize that they are already paying far more than 18 percent.

Mr. GREATHOUSE. This is why we tie it to the Federal discount rate. We think the ceiling should be related to control of interest rates generally. If you used some multiple of the Federal discount rate this would provide more equity during different periods of money availability.

Mrs. SULLIVAN. As an illustration of how much people can really be paying in interest charges, I want to insert an article which appeared in the Boston Herald, the Washington Star, and other papers last Saturday, by a well-known real estate man and writer, Mr. Bernard C. Meltzer, who tells about a real horror case involving what is supposed to be a 4-percent mortgage. According to the writer, this 4-percent figure could go to 344 percent because of the tricks and gimmicks in the deal.

(The article referred to follows:)

[From the Boston (Mass.) Herald, August 12, 1967]

YOUR REAL ESTATE PROBLEM SOLVED—TRUE INTEREST RATE OFTEN HARD TO FIGURE

(By Bernard C. Meltzer)

At one time, mortgage lenders competed primarily based on interest rates. Many still do, but new financing gimmicks introduced in recent years make it almost impossible to compute the true rate—even by experts.

"DEAR MR. MELTZER: I need $5,000 by the first of the year, so I'm going to get a mortgage. Since my house is worth over $20,000, this should be no problem. It's only a question of shopping around to get the best interest rate.

"My bank is willing to give me the money at 6 percent interest. A local finance company, and I'm a complete stranger to them, is willing to give me the money for 4 percent. It's true, they do have a few extra charges like insurance, appraisals, etc. (I'm enclosing copies of their papers for your examination.)

"I always was poor in math, so please tell me whether all these extra fees amount to more or less than the 2 percent difference in interest rates.

"Mr. T. T."

Answer: A best as can be determined, the extra charges raised the true interest rate from our correspondent's estimate of 4 percent to 344 percent. The papers contain almost every known gimmick for raising the true interest rate. For the information and enlightment of readers, these are enumerated below:

1. Five years' interest (4 percent of $5,000) amounting to $1,000 is added to the amount borrowed and the face amount of the loan reads $6,000, and not $5,000.
2. The interest rate of 4 percent during the whole period is computed based upon $6,000 and the remaining balance or amount owed.
3. The borrower is allowed only one day grace period in which to make mortgage payments. If he misses that day, the late penalty is then 1 percent a day.
4. The pre-payment penalty is 20 percent.
5. The borrower has to buy life, disability, health and accident, and homeowner's insurance from the lender's agent at very high rates.
6. An inspection fee of $100 is charged the first year and $50 per year thereafter.
7. The legal fee is set at $300 and the annual legal fee thereafter is $100.
8. The appraisal fee is $100 and the annual appraisal fee thereafter is $50.
9. Borrower agrees to pay a 10 percent placement fee for securing the loan.

Mrs. SULLIVAN. Mr. Stephens, since there are just the two of us here, we can take turns in questioning. Why don't you go ahead now?

Mr. STEPHENS. I would like to make some observations and inquiry at this point on the 18 percent.

You are familiar with the argument on the side of companies that use revolving credit plans, that if they are required to translate the 1½-percent charge into an annual rate it would be 18 percent, but that it would not be a true reflection of the transaction. They have provided charts which show that in a great number of instances the actual annual rate after the year is over amounts to 10 or 11 percent, and that in only one instance out of 40 different items the rate would go over 18 percent, based upon an actual way the accounts are paid.

Wouldn't that then be a burden on the man who has the revolving credit plan to require him to say that 18 percent is true when he is not charging 18 percent?

Mr. GREATHOUSE. As I understand most of these plans—there is no charge for the first 30 days, and after that 30 days the interest rate is 18 percent a year or 1½ percent per month.

Now, in most cases the original price is a cash price if the price is paid within a 30-day period. But once they start to charge interest they then charge interest at the rate of 18 percent per year.

Now, this can be clearly stated that after the 30-day period is over you then pay interest at the rate of 18 percent per year.

Mr. STEPHENS. They would have to put 18 percent on and they would have to explain that 18 percent only pertains if you carry this all the way through the entire year, provided you pay a specific amount and provided you do several other things, and you add a considerable amount to the bookkeeping and to the explanation and would it help the creditor any?

All you have done is cause the man who is using this type of credit to think he is paying 18 percent when he is not actually paying 18 percent. So you don't have truth-in-lending.

Mr. GREATHOUSE. I don't want to argue with you, but it seems it can be simply stated by saying that you pay at the rate of 18 percent a year after the first 30 days, which is really what you are doing. You pay an annual rate of 18 percent after the first 30 days.

Mr. STEPHENS. Not necessarily—depends on how much you pay back.

Mr. GREATHOUSE. But you are paying at the annual rate of 18 percent.

Mr. STEPHENS. No, if you figure it out, it may come out to 10 percent.

Mr. GREATHOUSE. If you pay 1½ percent a month, once you start paying it, that is at the rate of 18 percent a year, even if you only have the money for 6 months.

Mr. STEPHENS. If it goes for 12 months.

Mr. GREATHOUSE. You are paying it at the rate of 18 percent even if you only pay it for 2 months.

Mr. STEPHENS. It won't figure out that way if you only have the credit for 10 days.

Mr. GREATHOUSE. As I said, I don't want to argue with you, but once you start paying interest, if you pay at the rate of 1½ percent per month, you are paying at the rate of 18 percent per year, and I don't care whether you pay it for 1 month or 12 months, out of the year.

Mr. STEPHENS. Mathematically, though, it doesn't figure out that way.

Mr. GREATHOUSE. I think it does.

Mrs. SULLIVAN. Would the gentleman yield? I would like to put a question to Mr. Barber at this point.

If I am going into the bank as a depositor, to deposit $100 in a savings account, and you advertise that you pay 5 percent a year on savings, at the end of the year I could expect—these are time deposits—I can expect that I will get $5 in interest and that I would have a balance of $105 at the end of the year, is that true?

Mr. BARBER. That would be correct.

Mrs. SULLIVAN. But if I don't live up to the terms you require, and do not leave that $100 in the bank for the whole year, or the specified time, in order to earn any interest, what rate would you be paying me?

Mr. BARBER. Well, I think the law is fairly clear on time certificates of deposit. Time certificates of deposit are actually contracts—I am speaking not as an attorney—between the depositor and the bank by which the bank agrees to pay a contract rate of interest for the use of these funds for an agreed period.

Mrs. SULLIVAN. If I leave it in for that specified period—6 months or a year—I expect to get 5 percent.

Mr. BARBER. That is correct.

Mrs. SULLIVAN. But if I don't leave it in for the required period—if I need that money before the period ends—I can get it out?

Mr. BARBER. Well——

Mrs. SULLIVAN. I can apply for my money and get it back, can't I?

Mr. BARBER. Probably, but not necessarily. When you purchase your certificate of deposit you are in effect loaning the bank the money for 12 months and the bank agrees to pay you 4.5 percent—it is more comfortable for me to say 4.5 percent because that is what we are paying for the 12-month period.

Actually, the bank normally would return it to you in the event that you needed it prior to the end of the year, but banks are restricted somewhat in that, too, because I believe the Federal Deposit Insurance Corporation regulation stipulates that we cannot return it to you, even if we wish, unless you sign what is called a certificate of necessity indicating that you have need for the funds in advance of maturity.

Mr. STEPHENS. I think what she has in mind is not the time deposit—that is not a demand deposit—but a savings account.

Mrs. SULLIVAN. Within 90 days you can apply for it.

Mr. STEPHENS. That is right, but you can't get it before the 90 days. But if you have got a savings account that is different. You can withdraw the latter at any time but not a time deposit.

Mrs. SULLIVAN. On a savings account, you may say you are going to pay 4 percent or whatever your going rate is.

Mr. BARBER. Yes.

Mrs. SULLIVAN. But if I don't leave that money in for the specified period, what rate do you pay me at the end of the year?

Mr. BARBER. I think there probably is quite a variable in that and savings accounts would probably be easier to talk about in this way.

Many banks require that the dollars be in the account on the day the interest is calculated. So, if you withdraw that you wouldn't receive interest on that portion which you withdraw and the rationale behind that, I think, is that the bank has agreed to pay 4 percent for a 6-month period. If it does not have use of those funds for a 6-month

period, if it is in fact a demand deposit, then it is of much less value to the bank because it has, as a matter of fact, not had the use of those funds.

However, many banks would, I believe, figure the interest to the date of withdrawal and many banks would, as a matter of fact, pay interest starting at the first of the month if the deposit is made as late as, say, the 10th of the month.

So, they would be paying a little more than 4 percent, actually, a little riper.

Mrs. SULLIVAN. The only thing that I am trying to get at, Mr. Barber, is that, when you take the money from the depositor, you say you will pay so much interest per year. But that all depends on what the customer does about that money—whether he leaves it in to earn the interest or not.

The same thing is true when we buy on credit. They say they are going to charge us 1½ percent a month. We may not pay our bill each month, as we are supposed to do, and they then charge us at a rate of 1½ percent per month and there are 12 months in a year so it is 18 percent a year that they are charging us. It all depends—the eventual charge depends—upon how we use that credit each month during the year with this firm.

I don't care how long we argue this with the retail people, there is only one answer. If they are going to charge us 1½ percent a month, they are charging us 18 percent a year. It may not figure out to that at the end of a year because it depends on the individual's use of the charge account.

But we have had arguments for 2 solid weeks on that point. They had the same argument for 7 years in the Senate committee. I suppose we are not going to change the minds of the spokesmen for the stores offering revolving credit because they insist upon pointing to the yield from a particular account at the end of a year. But that is not what they are telling the customer in signing her up for a charge account. I don't care what kind of terms they make, or when they start their credit charges, the charges are for a period of 1 month.

I will never pay credit costs if I can pay cash in 90 days. I think it is still the "law of the land" that payment in 90 days is cash.

But I have been told that the department stores just don't tell this to their customers unless they ask—or unless they have a strict policy now that they don't give 90-day credit. But nevertheless, this is the argument that I was trying to use on them.

In depositing money in your bank, we are told we are going to get a certain rate of interest per year and it is up to the depositor to live up to those conditions in order to earn it. It is up to the user of credit in the department store to decide how and when he will pay, so he can arrange to avoid credit charges, but if he doesn't, they still charge so much per annum, which we figure is 18 percent, when they charge 1½ percent a month.

Mr. STEPHENS. I will try to make an analogy. I don't know whether I can or not.

The checking account that a person has in a bank is subject to a service charge comparable, I think, to the revolving fund charges. Now, are we trying to tell the bank that they must put down on the bank monthly statement that the service charge of 5 cents per check, if

your balance is under a particular amount, is a charge that the bank is making against you to put your money in the bank and the bank must state that at a percentage of annual interest that it is charging?

Now, there is an analogy between the fact that what is called 1½ percent interest rate on a revolving account is a service charge comparable to the bank service charge for allowing people to use the credit machinery and is like holding the merchandise and having the use of it. Should the banks be required to put down the service charge on my checking account in the annual interest rate?

Would you feel like that you should be required to put down what your service charge is to let me have a checking account? If you look at that from one standpoint perhaps you are using my money and are charging me interest to use my money. But, you don't call it that. You call it a service charge. You are keeping my books for you, that is what you are doing.

Mr. BARBER. This is right. The bank service charge is justified, I think, as a payment or more accurately as a partial reimbursement for the service that the bank renders to the customer in doing his bookkeeping for him and in handling his checking account activity.

Mrs. SULLIVAN. Would the gentleman yield?

Mr. STEPHENS. Yes.

Mrs. SULLIVAN. Is it not true, though, that unless the banks have a credit card service, they are not in revolving charge? You are not charging 5 cents a check or 10 cents a check on a loan basis—you are providing a service, not lending money.

If they have a small amount in the account, you are going to charge them because you can't make an effective use of their money while it is deposited. But for those who maintain a certain balance in their accounts, you make no charges.

Mr. BARBER. That is correct.

Mrs. SULLIVAN. The charge you make on checking accounts is not for the loan of the money; it is for a service you are giving them for the handling of their checks.

Mr. BARBER. The banks are rendering the depositors a service for maintaining his account. If the customer in return leaves an adequate working balance, a portion of which the bank can in turn invest and earn on, then the bank would not make a service charge, if that balance is low enough that the bank would otherwise incur a loss, then the bank would attempt to levy a service charge to recoup its costs.

Mr. STEPHENS. And that service charge is the cost of servicing that account?

Mr. BARBER. That is correct.

Mr. STEPHENS. In that instance, that is a justification for starting out on the revelation of charges and the reason for a $10 charge not to be revealed as an interest charge. Under the disclosure plan here you have a finance charge of $10.

Merchants have appeared before this committee and in the Senate committee who use the revolving plan or don't and it is pretty well established according to their costs that the $10 charge is the actual cost of putting on the books an initial charge—whether it is an 18-month payment or a 12-month payment or whether it is paid off the first of the month. That would be analogous to the bank service charge more fully than otherwise.

Mr. BARBER. I think so. I would like to comment, if I could, regarding this minimum. We stated in our testimony that we would favor exclusions of finance charges of $10 or less as was in S. 5 and as in the Widnall bill.

The reason for that is because on very small loans for short lengths of time the cost factor is definitely involved. You read many different figures as to what it costs to put a loan on a bank's books.

I am thinking now strictly about banking rather than Mr. Greathouse who was referring to merchandisers. In our little bank we charge $1 minimum for a $100 loan. I have read that cost accountants say that this should not be $1 but it should be $5 or $10. That it costs that much to put a loan on the books.

So we loan a fellow $100 for 10 days until payday and we charge him $1 for it. Let's say for a week. If my arithmetic is right, we are charging him 52-percent interest on an annualized basis. And by so doing we are incurring what a cost accountant says would be a $4 loss.

I would think that it would not be fair to report that as 52 percent simple annual interest. The larger banks, many, would charge $5 for that and would still prefer not to make the loan because it is not a profitmaking credit.

Again, if my hurried arithmetic is right, I think that a bank would be charging 260 percent interest if it had a $5 minimum $100 loan for a week. Well, a bank just isn't going to be advertising that it charges 260-percent interest. The $5 minimum charge is reasonable and fair. Relating it to an annual rate makes it appear high.

So what the bank is going to do, they will say, "I am sorry we don't have that kind of loan any more?"

Mrs. SULLIVAN. If I may interrupt there—you certainly don't advertise that you will lend $100 for only a week. I am sure you don't want that kind of business, or go out to stimulate it. You only do that as a favor or accommodation to a regular customer, I imagine.

But if a man knew that he was paying 260 percent for a loan he needed so badly, let him know it. Let him know how silly it is to spend that much to use credit for such a short length of time.

Mr. BARBER. I should correct my statement perhaps. I didn't mean that we would advertise. I should have perhaps said we wouldn't care to tell the world that we are charging 260 percent interest if we charged the borrower $5 for the use of $100 for 10 days or whatever the period would be. We would not put that in the form of an advertisement obviously, but if we rendered this to him in the disclosure basis we would be telling the world that he would go down the street and he would say, "I am paying the bank 260 percent interest."

However, it would be a service that the bank would prefer it would—would prefer not to perform in the first place.

I will go back to the $1 minimum because that is what our little bank charges—so we would be accused of charging 52 percent interest. They now accuse us of charging 7 percent and try to give me a guilty conscience. It doesn't at all. But if they said we charge 52 percent interest on a loan we prefer not to make, and I think it is a legitimate loan, I don't think he is foolish for borrowing it because he just happens to need $100 before payday. He wants to go on vacation and it is worth $1 to him rather than have the boss forward his checks.

So, I don't think the charge is exorbitant. I don't think the borrower is foolish. I think the bank is rendering a service and this would be a very good example, an indication that these small amounts should not be reported on an annual-rate basis.

Mr. STEPHENS. One further thought to completely channel the thought along the line of what we are talking about, and that is this: In addition to protecting the consumer from exorbitant charges, we must, I think, keep in mind this thought—that these people tell us that it costs an average of $10 to put this credit on the books.

Now, if they required the creditor to do a great number of things to add to his costs, we may not be doing the consumer a favor by putting those costs on the creditor because the creditor is going to pass it on to the consumer and it is only going to raise the price to the consumer. That is what is concerning me and appeals to me about this $10 limit because if you require more you are just adding more costs to the bookkeeping. That is going into the overhead cost of the business and the merchants are going to raise their prices to the consumer. You haven't done anything for the consumer except tell him what is the truth and let him pay more.

What good have you done the consumer? You let him know what the truth is but you also have been a party to making the price go up. That's why I think the $10 exemption is all right.

Mr. GREATHOUSE. Could I comment on that?

I think what Mr. Barber is talking about might be a rare individual case of a person making an individual loan. What we are generally concerned with is repeated charge account buying where people have charge plates and they go back on a repeat basis. They do this anyway—you buy an item, it is added to your account. We are not talking about any additional bookkeeping. Certainly it is added to your account now and there are charts available which says how much the interest should be on this.

As a matter of fact, in many places we find that when we buy consumer items and then go to make payments on them we make payment to a different place. Sometimes the merchant does the bookkeeping work and then turns it over to a finance company anyway.

On the other point, if the 18 percent per year is proper after they start paying interest, then it seems to me the 1½ isn't proper.

Senator Douglas said he couldn't see why merchants were reluctant to tell people there are 12 months in a year. This is what you are talking about, that there are 12 months in a year.

One other thing that I would like to comment on. I think the committee should know what we are running on to—even on the basis of paying cash in 90 days. I recently made a purchase and I inquired as to whether or not there was a cash price if I paid within 90 days and was told yes. However, there was a service charge of $8 or $10 that you had to pay. So even then, even though they do not quote interest charges for the first 90 days, they want you to pay a service charge.

So, the best thing to do is to pay cash.

One other comment if I may on this. I think there is a big difference between what we are talking about here and the charges made by banks for a service that the bank performs for you. But first of all, every bank that I know of does outline to you their procedure for charging you for

writing checks and for the matter of handling deposits. They also outline to you——

Mr. STEPHENS. The percentage figure?

Mr. GREATHOUSE. Banks do it on the basis of how much it costs per transaction, but in this case it seems to me to be completely different. It is not a matter of you using the bank's money. This is a service charge, as I understand it, that the banks make for handling paperwork, of paying out your money to somebody else, and not for the use of the money at all.

So, this is the charge that they make to pay out your money against a check that you have written to someone else or to make a deposit.

It would be a service like a normal service and not really for using the money.

I don't think it is a good comparison.

I think certainly there does need to be real protection in all of these fields.

Mrs. SULLIVAN. I certainly agree with you on that, Mr. Greathouse. I have never looked on any service charge in using a checking account as anything but a charge for the work the bank has to do.

You are not borrowing money from the bank, because the minute you are overdrawn in your account, you are told about it. So, the banks are not lending the checking account customer anything. You are merely doing him a service. So there shouldn't be any percentage rate required on checking account service charges because you are not extending credit.

But when we get into the $10 exemption in the Senate bill, I am heartily against exempting the $10 credit charge from an annual percentage rate disclosure requirement. When a person goes into an appliance store or any other store and buys an article costing $100 or so or goes to a loan company and makes a loan of $50, or $100 or in that area of cost, such a person should know what he is paying in interest on that transaction—whether it be a loan or whether he is purchasing something. He should know what the percentage is that he is paying.

This is the area in which I think the highest rates of interest are actually charged.

The cost is just as much to make a $10 loan or $100 loan as to make a $1,000 loan. When people want to buy an appliance for $100 or so, and if the credit charge for $100 or less is under $10, I think the stores should have to show that individual exactly what he has to pay in percentage, as well as in money, for the period of time they want that credit.

Undoubtedly, we are fighting in behalf of people who, in many instances, could not care less what they have to pay. All they want to know is how much they must pay a month. But I think sometimes we have to protect people from themselves. And if they are given an honest and full account of what it costs them to buy on credit, they might begin to shop more intelligently. It is not going to stop them from buying. However, it might stop them from going to the person who is going to gouge them on the credit terms.

We have been told by some of the witnesses that what the unscrupulous retailer would do would be to raise the basic price of his

product if he felt he couldn't compete percentagewise in the charge for credit.

But again, the customer would have a choice—if he can get the same television set in one place as in another, and if there is $50 or $100 difference in the price, if he is foolish enough to pay the higher price because he can get credit there and couldn't get it in the legitimate store, at least he knows what he is doing and he is doing it with his eyes open. This is what we are trying to accomplish in this legislation. That is why we want to put back into the bill as it passed the Senate the revolving charge and the items on which the credit costs are $10 or less.

Mr. Barber, we had Mr. Bailey, of the Marine Midland Corp. of Buffalo, testify before us and he suggested that a bank which makes a loan for $50 for 1 month and charges the customer $5 for the loan would not want to reveal, or would be too embarrassed to reveal, that they were charging an annual rate of 120 percent. If they were required to state that rate, he said they would stop making such loans.

Do you concur in that?

Mr. BARBER. Indeed I do. As I said when I misused the word "advertise," banks would not like to tell the world that they were charging in our little instance 52 percent or 260 percent if you charged a $5 minimum, although it costs you $5 to put that loan on the books.

So, rather than do that we would say we have no more $100 loans. We would then be going so far in protecting our customer that we made credit unavailable to him. That would be of no service at all. If banks are willing to make loans with no profit as a service I would think they should probably be encouraged to do that.

Mr. Greathouse indicated that we were talking about different things and this we are. However, as far as our 6,500 member banks are concerned, this is not a unique instance. It is quite a common one. We are very, very frequently called upon to make $25 loans, $50 loans, $100 loans to wage earners, reputable honest people. We are not the least bit concerned about collecting credit. We know they are going to repay it and we are happy to make them a loan and we charge them $1 for it.

I have been using the $100 for an example, if we make it $25 we are charging 208 percent interest. I wouldn't like to have that done. I don't think it is fair to ask the bank to say: "We are annualizing that at 208 percent because we are making an accommodation loan." I would suggest possibly on these items bearing a charge of $10 or less, that certainly the dollar amount should be disclosed. There is nothing wrong with that. We would be delighted and we do now tell our customer: "Surely, we will loan you $35 until payday and we will charge you $1 for it." He is happy about it because he is getting in fact a bargain.

Mrs. SULLIVAN. When you state the borrower is entitled to an accurate understandable statement of the costs of borrowing, is what you really mean that he is entitled to such information only to the extent that it doesn't embarrass you?

Mr. BARBER. It is not going to embarrass us because we are not going to do it. The person that you are trying to protect is not going to be able to borrow money on those terms.

Mrs. SULLIVAN. You repeated that you wouldn't want to advertise things of that sort, and yet you have said, too, that these are not the usual loans—these are unusual.

Mr. BARBER. Mr. Greathouse said these are the unusual things. I, as a matter of fact, said they are quite common, quite customary and in the vast majority of our banks throughout the country they are making little short-term loans all the time.

Mrs. SULLIVAN. You are not in business for making small loans like that to people who are in temporary distress. You are in the business, primarily, of longer term loans, such as mortgages and business loans which are the big part of your business.

Mr. BARBER. Yes; it is indeed. But I have always been of the opinion that a small person in financial stature is as entitled to have credit available to him as the very large borrower and I believe that. And I think this would very likely mean that the little fellow wouldn't be able to borrow his $10 or $50 until payday.

Mrs. SULLIVAN. I don't see why you would refuse to lend him money under these circumstances simply because you would be obliged to show the rate of interest he has to pay.

Mr. BARBER. I would say because of the unfavorable publicity that we would get that was costing us money in the first place.

Mrs. SULLIVAN. Don't the credit unions offer $100 loans for short periods for only 12 percent instead of 200 percent?

Mr. BARBER. That would mean with no minimum—12 percent of $100 for 2 days? I am not a mathematician. Let's figure out what it is.

Mrs. SULLIVAN. Our counsel just said that credit unions do lend up to $100 loans at 12 percent annual rate, regardless of the period.

Mr. BARBER. $100 at 6 percent for 60 days is $1. For 6 days it is 10 cents. So for 1 day it is 1⅔ cents. I doubt that any credit union or any other lender would loan for less than a 2-cent interest charge.

Mrs. SULLIVAN. I am not certain of this. Counsel said there is no minimum rate, but I would have to check on that, because I am not sure.

Mr. BARBER. If there were no minimum rate then I could borrow from my friendly credit union, my non-tax-paying credit union, $100 for 1 day and they charge me 1 penny and we would say, let's round that down to nothing. I question that whether they will do that.

Mrs. SULLIVAN. Credit unions have been formed to take care of these temporary small loans that people need for a short time. Normally, unless they are used to going to the bank for many other things, they don't go to the banks for this kind of loan, from the information we have.

I have no idea what percentage of your banking business is attributed to this type of loan but I imagine it would be a small percentage.

Mr. BARBER. A small percentage but all of our customers who need $100 for 7 days would come to us. Maybe before they went to their brother-in-law or the credit union if they will do it for a penny.

Mr. GREATHOUSE. If I could just comment on the credit unions—I know in the credit union which we have there is 1 percent per month which is prorated for any part of the month that you use the money and also our credit union then rebates 25 percent of the 1 percent that you paid for interest.

Mrs. SULLIVAN. Thank you.

You say, Mr. Barber, that the criminal provisions of the bill are too severe and that violations should only be considered subject to prosecution when they are repeated.

Now, really, Mr. Barber, we are talking about a criminal statute. How many murders or armed robberies would you condone before you would have the criminal laws apply? Or, perhaps more to the point, how many bank robberies would you sanction before you believe that the felon should be arrested and brought to justice? Two? Three? If we are imposing criminal penalties, then, certainly, they should be enforced on the first violation and every time a violation occurs.

Mr. BARBER. Our only thought about that is that we think that the violation should be repeated and it should be knowing and it should be willful and that an unintentional infraction shouldn't open the door to prosecution and lenders shouldn't be treated as though they were guilty, whatever the bill shows—if it were just an oversight or an isolated instance.

Mrs. SULLIVAN. We certainly would not want this power used to prosecute anyone criminally for a minor oversight. But I don't think we want to give unscrupulous lenders a clear field to "one bite" as with a biting dog.

Mr. Barber, I am delighted to see your statement, that—

> We believe there is no valid reason why a customer or borrower should not have an accurate and understandable statement of the cost of borrowing and credit.

We are all agreed on the principle you state. The only difference would seem to be as to how we will implement that principle. I would be particularly interested in an expression of your views on why you do not favor provision for administrative enforcement contained in my bill, but prefer to leave such matters to civil suits brought by debtors—who can't afford to bring them—or criminal suits brought by the Department of Justice—who will be too busy to bring them—rather than requiring that the responsible administrative agency act to protect the public?

Mr. BARBER. Well, as I understand it, the U.S. district attorney would handle the criminal aspect of it and I think would handle it well.

Mrs. SULLIVAN. I am not a lawyer, I can't argue this part of it with you.

Mr. BARBER. I am not, either, I should probably refer this question to our counsel, Mr. Hansen.

Mrs. SULLIVAN. The only thing we know is that someone who is in trouble hasn't the money, if they are terribly in debt, to bring a lawsuit. This is why we feel that we need an agency to protect the public from violations.

Mr. STEPHENS. As I understand the position of the independent bankers, it is not that you don't believe any penalties should be assessed against the violators of the rules and regulations, as set out in the bill; you just don't believe there ought to be the heavy criminal penalties assessed in the Sullivan bill. Do you agree with the position that penalties that are in the S. 5 bill are all right?

Mr. BARBER. Not entirely. We believe as far as the criminal aspects are concerned that the penalty should be at, at least at the outset should be a fine rather than imprisonment and we believe——

Mr. STEPHENS. In both bills?

Mr. BARBER. Yes, and the offense should be repeated and knowingly and willful and that goes right along with the bill on page 19 in which it says "however, any creditor who willfully and knowingly uses such tables and charts in such a manner as to consistently understate the annual percentage rate."

So, we have no objection to penalizing the consistent violator. We do object to penalizing an isolated infraction and we object to being guilty until proven innocent—to assuming that the lender is, in fact, dishonest. Because we think our lenders are basically not dishonest and that any infractions that have been made really have not come from the banking segment of the industry.

We think we are clean and we have not gouged the public and we are doing a good job of disclosing. We don't want to be burdened with a tremendous amount of additional administrative work that isn't going to be really worth while.

Mrs. SULLIVAN. Gentlemen, I have several questions I would like to read into the record that I think you and your counsel, Mr. Barber, could answer when you get your transcript and the same with you, Mr. Greathouse. We are running against time. I didn't think Mr. Stephens and I could keep this going so long this morning, but we have.

I have several questions for you, Mr. Barber. The first one is this: You say that the requirements of stating an annual percentage rate—assuming the bill were to take effect July 1, 1968—doesn't give the Federal Reserve Board adequate time to prepare regulations, tables, and so forth. However, Mr. Barber, are you aware of the fact that the Massachusetts truth-in-lending law went into effect 90 days after it was signed by the Governor of the State?

Massachusetts officials were here before the committee last Monday and they indicated that 90 days gave them plenty of time to prepare the necessary regulations and charts. July 1, 1968, is more than 300 days away. Don't you think that, if we enacted this law within the next 2 months, that the Federal Reserve Board would have ample time to issue regulations, prepare charts, and so forth?

(The reply of Mr. Barber follows:)

We feel that actually it would be most difficult to have this law take effect by July 1, 1968. The Federal Reserve Board is not familiar with this and has not had the opportunity to study in depth the entire area of interest rate disclosure. It is our opinion that they will surely desire and should be afforded ample time in which to develop the regulations. This could well require hearings as well as extensive research and study. We think that a flexible effective date should be permitted in order that the Fed itself could determine when it was ready which in no event would be later than January 1, 1972.

Mrs. SULLIVAN. Next, Mr. Barber, you stated that credit life insurance is not a charge for lending money. However, isn't it true that banks extend loans, telling the individual what his payments are in

dollars and cents without revealing to him what part of that payment is payment on the principal, what part is payment on interest, and what part of the payment is for credit life insurance or other charges?

Isn't it also true that banks and other financial institutions often require that the borrower not only purchase credit life insurance, but that such insurance be purchased from the lender or from a specific agent of the lender?

And, isn't it still further true that such lenders have ties with, receive kickbacks from, and indeed make a substantial profit out of their forced sale of credit life insurance?

(The reply of Mr. Barber follows:)

Permit me to answer these questions by first stating that we know of no bank which *requires* that the borrower purchase credit life insurance. It is strictly voluntary in our bank and in fact we believe it must legally be kept on a voluntary basis. The bank agency or individuals in the bank normally act as the insurance agent and in fact so far as we know credit life insurance is not available except through such an arrangement between a lender and an insurance company.

As to the receipt of so-called kickbacks and the earnings of a substantial profit on this business, I can only state that we believe commissions on the sale of insurance are completely normal, legitimate, accepted, and desirable. We believe in the profit system and we do not apologize for being in business to earn a profit. Insurance is, in our opinion, a proper sideline for banks and credit life is a desirable service that the lender can offer the borrower.

In answer to the first part of your question (at the bottom of page 1211), I will state, as I did in my prepared testimony, that I believe banks do a good job of disclosing. Let me give you an example of what we would type on a typical note of $2,000.00 for 24 months to finance say a new automobile:

Net advance (or net to borrower)	$2,000.00
Finance charge (this is figured at the so-called 6 percent add-on rate and we now quote it as $6 per hundred)	245.45
Credit life (if he choose to have it)	45.83
Gross note	2,291.28
Monthly payment for 24 months	95.47

We do not relate the finance charge to a simple annual rate as would be required by the Truth-in-Lending Bill. It would be 11.5% or thereabouts. We believe we give the borrower all he wants to know, i.e., full disclosure.

As previously stated, the charge for credit life should not be included as part of the interest charge because interest is a charge for the use of money and is not and never has been a charge for insurance. The charge for credit life should be disclosed to the borrower and we now do this. He should not be required to buy credit life and we know of no banks that require this.

Mrs. SULLIVAN. In this connection, and at this point in the record, I should like to introduce an unsolicited letter received by a member of the staff from the First National Bank of Washington. It is obviously a form letter. It is addressed to "Dear Customer" and is signed by an assistant vice president of the bank. Let me read portions of this letter to you. The letter begins:

This is vacation time. Whether you plan to take a trip or stay at home and make home improvements . . . or if you just need funds to pay off some nuisance bills . . . or for any sound reason . . . we are ready to serve your needs.

The letter then sets forth a number of typical loans that may be obtained. The information is set forth under the following headings: "Advance" which tells you the amount of money you will get; "Gross Loan" which tells you the amount of money the bank says you will owe

them; "Number of Equal Monthly Payments" which tells you over what period of time the loan must be repaid; and "Monthly Payment Including Credit Insurance".

Let me state that again: "Monthly Payment Including Credit Insurance." There you receive a single figure with no breakdown for principal, interest, or insurance. This is certainly a reputable bank. It is advertised as Washington's oldest national bank and yet, this single solicitation, it seems to me, demonstrates the need for truth-in-lending—and also the need for including credit life insurance in the definition of the finance charge.

(The letter referred to follows:)

THE FIRST NATIONAL BANK OF WASHINGTON,
Washington, D.C.

DEAR CUSTOMER: This is vacation time. Whether you plan to take a trip or stay at home and make home improvements . . . or if you just need funds to pay off some nuisance bills . . . or for any sound reason . . . we are ready to serve your needs.

Subject to approval of your application, we will provide you with the money requested. Processing can be handled without delay.

All you need do is fill in the brief form and promissory note on the reverse side of this letter and sign the note. When approved, we will forward the proceeds by check or deposit the funds to your account, if you have a checking account with us.

Below are several typical repayment schedules available. We suggest you review these to determine the most desirable for you.

Advance	Gross loan	Number of equal monthly payments	Monthly payment including credit insurance
$500	$537.60	12	$44.80
$600	645.12	12	53.76
$800	893.70	18	49.65
$1,000	1,117.26	18	62.07
$1,500	1,744.08	24	72.67

If your requirements are for more than $1,500.00, please call me at 737-1700, extension 264.

We value the opportunity to offer this service to you and we appreciate your business.

Sincerely,

C. A. BLEDSOE,
Assistant Vice President.

FULL NAME	DATE OF BIRTH	☐ MARRIED ☐ SINGLE ☐ SEPARATED ☐ DIVORCED	HOME PHONE
EXACT PRESENT RESIDENCE ADDRESS	LIVED HERE YRS. MOS.	PRESENT OCCUPATION (JOB TITLE & GRADE)	BUSINESS PHONE
NAME AND ADDRESS OF PRESENT EMPLOYER OR GOV'T. DEPT.			NAME OF SUPERVISOR
LENGTH OF EMPLOYMENT YRS. MOS.	PREVIOUS EMPLOYMENT	COMPANY ADDRESS	HOW LONG?
WIFE'S NAME	WIFE'S AGE	HOME: ☐ Renting—$ per mo. ☐ Buying—$ per mo.	NO. OF CHILDREN / AGES OF CHILDREN
NAME AND ADDRESS OF WIFE'S EMPLOYER		WIFE'S OCCUPATION	LENGTH OF SERVICE / BUS. PHONE
YOUR MONTHLY INCOME	WIFE'S INCOME (IF ANY)	OTHER MONTHLY INCOME / SOURCE OF OTHER INCOME	TOTAL MONTHLY INCOME
NEAREST RELATIVE NOT LIVING WITH ME: NAME	ADDRESS		RELATIONSHIP
WIFE'S NEAREST RELATIVE: NAME:	ADDRESS		RELATIONSHIP

LIST ALL OUTSTANDING INSTALLMENT OBLIGATIONS. IF NONE, LIST RECENTLY PAID ACCOUNTS
(IF MORE SPACE IS NEEDED USE SEPARATE SHEET.)

YEAR, MAKE, MODEL OF AUTO(S) NOW OWNED	NAME AND ADDRESS OF PRESENT/LAST AUTO FINANCE COMPANY	DATE OPENED	MONTHLY PAYMENT	BALANCE OWED
			$	$

NAME & ADDRESS OF CREDITORS	PURPOSE OF ACCOUNT	DATE OPENED	MONTHLY PAYMENT	BALANCE OWED

EXACT PURPOSE OF THE REQUESTED LOAN IS:

CERTIFICATION: To obtain the requested loan from you, and to permit you to rely hereon, I certify that the information contained herein is complete and correct.

Date Signed _____ Signature _____

PROMISSORY NOTE

ADVANCE	GROSS LOAN	NUMBER OF EQUAL MONTHLY PAYMENTS	AMOUNT OF EACH MONTHLY PAYMENT	The first payment is due 45 days from the date proceeds are issued. Subsequent payments are due on the same day of each month thereafter.

FOR VALUE RECEIVED, the undersigned, herein called the maker or borrower, jointly and severally promise to pay to The First National Bank of Washington, the amount of loan stated above with precalculated charges added thereto at the rate of 6% Discount per annum. Repayment of said loan shall be made in accordance with the schedule set forth above. Interest after maturity shall be computed at the legal rate.

Borrower may prepay this note in full or in part at any time. In the event of prepayment in full, or, in the event of acceleration of payment for any reason, a recalculation and/or refund of precalculated charges shall be made in accordance with the Rule of 78.

Default in the making of any payment due hereunder, or any part thereof, shall at the option of the holder, and without notice or demand for performance, render the entire unpaid amount due and payable at once.

In the event of delinquency, the lender may collect and the borrower agrees to pay delinquency charges at the rate of 5% per month, but not to exceed $5.00, on any amount in arrears. Also, in the event suit is brought for the collection of this note, the borrower agrees to pay a reasonable attorney's fee in such amounts as may be fixed by the Court.

Maker and endorser hereof, jointly and severally, waive presentment for payment, protest, notice of non-payment and protest, and consent to the extension of time of payment before, at, or after maturity.

All makers, indorsers and guarantors, jointly and severally: have given holder a lien upon all money and other property of every sort of each of them now or hereafter in custody or possession of holder, for whatever purpose delivered and in whatever capacity held, and upon any balances of any of them with holder, for the payment of this and all other obligations of every sort of each maker; waive, demand, presentment, protest, all notices of every sort and the benefit of all homestead and other exemptions and valuation and appraisement laws; and waive any impediment to suit in the District of Columbia on this negotiable note if not paid when due by irrevocably appointing Fiscal General Corporation, Washington, D.C. as their agent to receive service of any process within said District and transmit notice forthwith by certified mail to the last known address of the part(y) (ies) sued.

It is the intention of the borrower and the lender, and they hereby agree, that the construction, validity, and effect of this note shall be governed by the laws of the District of Columbia.

SIGNATURE OF MAKER (BORROWER) —► (1) _____ (Your Signature)

Date _____ (2) _____ (Spouse's Signature)
(If married, both husband and wife must sign.)

Mrs. SULLIVAN. That will be a lot to answer.

Mr. BARBER. I will be delighted to answer it. I can scarcely contain myself until I get home to write the answers. I would love to answer them now.

(Mr. Barber submitted the following comment on the unsolicited letter from First National Bank of Washington:)

The letter you cite on pages 1212 and 1213 from the First National Bank of Washington appears to me to be an ethical and legitimate solicitation for consumer credit loans. From it the borrower easily determines the number of dollars he is paying for the credit. There would be no objection on our part to breaking

down the amount that was going to interest and the amount going to pay for credit life and I would be reasonably sure that the bank in question would feel the same way. You object to their inclusion of credit life premiums and interest as a single figure and yet in your bill you would require that disclosure of interest and credit life be included as a single rate. This is all we object to. We think they should be disclosed but should be separate and we think further that credit life premiums should not be related to a percentage figure anymore than any other insurance premium should be related to a percentage figure.

Mrs. SULLIVAN. Mr. Greathouse, you can answer this question also for the record when you go over your transcript:

How do we get across to the public the full story of predatory consumer credit practices so that we can deal with them? The District of Columbia Commissioners announced yesterday that they now want to do something about the problem here in Washington but I think we need national laws with teeth, such as H.R. 11601.

Can you help us get some real support for it?

If we were to pass the Senate bill, Mr. Greathouse, with no annual percentage rate required on revolving charge, no percentage rate disclosure requirement on most transactions under $100, no disclosure of any kind required on first mortgages, no disclosure required on anything until July 1969, and then no required disclosure on an annual percentage rate on anything whatsoever until 5 years from now, what would that bill actually do for the consumer?

I wish you would answer those for the record, Mr. Greathouse. I want to say again that Mr. Annunzio was most disappointed not to be here to hear you this morning. He was most faithful, as Mr. Stephens has also been, in attending nearly all of these hearings. Mr. Annunzio has been one of the best advocates on the subcommittee of the garnishment provision of H.R. 11601 and he will be delighted with your support on this, and the support also of the industrial union department of the AFL–CIO. He was very unhappy, as were some of the others of us, when Mr. Beimiller testified about the lack of an AFL–CIO position on this.

There has been mention made here of the packaging bill. As weak as it is, it nevertheless allows the Food and Drug Administration and the Federal Trade Commission to specify the sizes of type for information required on labels. I think that is one of the most important things the packaging law does.

(Mr. Greathouse submitted the following comments in reply to Mrs. Sullivan's questions:)

I believe that the loopholes now existing in the Senate passed version of truth-in-lending would no doubt cost the American consumer hundreds of millions of dollars yearly. Total interest on consumer credit amounts to some $13 billion yearly, and a substantial portion of that credit relates to areas such as first mortgages, purchases under $100 and revolving credit accounts that are excluded from coverage in the Senate passed bill. Disclosure provisions should have the effect of compelling creditors who charge high interest rates to reduce their charges, and the availability of adequate information should lead the typical consumer to utilize credit sources with lower interest charges. These hundreds of millions of dollars will largely come out of the pockets of the disadvantaged, the least educated, those with incomes well below the poverty line, where the presence or absence of a few dollars can have a significant impact on their lives.

As I indicated in my prepared statement, the UAW and the IUD would wholeheartedly support legislation to eliminate small print in credit contracts by requiring that no type smaller than 8 point type be used in such contracts.

Mrs. SULLIVAN. Do you gentlemen think—I would like to have both of you answer this for the record—do you gentlemen think that the

Federal Reserve Board, under this bill, should be able to specify that no type size smaller than, say, 8 point type, can be used on any credit contract? Just add your thoughts on that in your transcripts.

(The reply of Mr. Barber follows:)

Concerning your question regarding type size we have no objection to specifying the type size be large enough to be clearly legible to a person with normal vision.

Mrs. SULLIVAN. Before we close, I want to take care of a few details for the record.

I received a letter from the attorney general of the State of New York, Mr. Louis J. Lefkowitz, who has been very active in behalf of consumer causes. He urges the passage of those provisions of H.R. 11601 dealing with disclosure of credit costs in preference to the provisions of the bill passed by the Senate.

Congressman Halpern, a cosponsor of H.R. 11601, has asked me to place Mr. Lefkowitz' letter in the record at this point. He was unable to be here this morning or he would have read it into the record, for it is an excellent letter from a public official with wide experience in the subject matter of this legislation.

(The letter referred to follows:)

NEW YORK, N.Y., *August 10, 1967.*

Hon. LEONOR K. SULLIVAN,
House of Representatives,
Washington, D.C.

DEAR MRS. SULLIVAN: The "truth in lending" bill, passed by the United States Senate, or the bill proposed by you, both of which are now before your committee, is a most urgently needed step toward protecting consumers and borrowers. Your bill offers, in my opinion, more protection to the public inasmuch as it calls for full disclosure of the cost of revolving credit and full disclosure on other interest rates, such as those on first mortgages. I urge your committee, if it reports out the Senate bill, to include therein a provision requiring full disclosure of the annual interest rates with respect to revolving charge accounts.

The purpose of these bills—to make sure that the borrower or installment buyer or anyone using credit will know exactly how much he is paying in interest, add-ons or other carrying charges—is essential to the achievement of adequate consumer protection.

Consumer credit is essential to the nation's economy and use of credit is responsible for much of the standard of living Americans enjoy. It is only fair, therefore, that the installment purchaser or borrower should be told by the leading institution his credit charges. This information should permit consumers to make more intelligent decisions about what they buy and borrow and on what terms.

It has been the experience of the Bureau of Consumer Frauds and Protection of my office that there is a glaring lack of knowledge on the part of most consumers of the actual cost of credit to them. Few families know how much interest they are paying and, tragically, the binge of borrowing has emboldened loan sharks and slippery salesmen to take advantage of an often too-trusting public.

The proposed legislation will be of primary benefit to the poor, who are the ones credit sharks find easiest to gouge. It won't eliminate unscrupulous salesman, but is will crimp their style and help to generate a new credit-consciousness among shoppers.

In hundreds of cases brought to the attention of my office, consumers who, being unaware of the full interest and credit charges, undertook payments far beyond their financial means. This resulted often in defaults by consumers after some payments had been made followed by the repossession of the merchandise and also the payment of deficiency judgments.

I have previously supported similar bills introduced in the Congress in recent years and I strongly urge support of the present measures with the revolving

charge accounts provision included. The passage of the bill introduced by you or the Senate bill with such included provision, will be in the public interest.

Best wishes.

Sincerely,

LOUIS J. LEFKOWITZ,
Attorney General.

Mrs. SULLIVAN. We have received numerous communications from organizations and business firms interested in this legislation, or which would be affected by it, and, to the fullest extent possible, and where appropriate, we will make sure that such material goes into the record. Some of these statements came from associations which we invited to testify but which instead decided only to file statements. We would have preferred to hear their witnesses, so that we could raise questions based on their testimony or on facts in our possession, but at least we will have their statement in the record.

Some of the members, I am sure, have or will have communications or other material they will want placed in the record and, of course, to the extent it is feasible and practical, we will be glad to cooperate on that. Let us set next Friday, August 25, for receipt of material for the record.

This concludes our scheduled hearings on H.R. 11601 and related bills dealing with consumer credit. We have been in almost continuous session for 2 weeks—about 15 sessions. We have amassed well over 1,000 pages of spoken testimony, and additional material in the form of written statements also was submitted for the record. So we will have a very substantial record to digest before going into executive session to mark up the bill.

I think an objective summary of all of the testimony we have received would show that the bill passed by the Senate by the remarkable vote of 92 to 0 on July 11 has so many exemptions in it that it would leave out a very substantial portion of consumer credit transactions, and would not require an annual percentage rate disclosure on any transactions for a period of 5 years.

I think it can safely be said that the Senate bill is the very least we should be able to get out of the subcommittee because every member of the subcommittee has introduced legislation which contains at least the provisions of the Senate bill. Most of us go some distance—and half of us a great distance—beyond the Senate bill. I sincerely hope that what we end up with is not "the least." I think that would be very little indeed, compared to what is needed.

These hearings are recessed subject to call of the Chair, in case further hearings are desired or required to help us complete action on the legislation. Again, I want to thank everyone who has helped us on this important assignment.

Mr. STEPHENS. Madam Chairman, I want to say this before you close.

I want to congratulate you first, as our chairman, in bringing up a terrific panel of witnesses in the 2 weeks in these hearings. I don't think there has been the possibility of anyone who really wanted to come who has been prevented from making a presentation.

I have said many times the job of a Congressman is a job that gives us the greatest opportunity for the greatest education that a person could possibly have. It is also a frustrating job because knowing that

you have the opportunity to be so well educated you do not have both the mental and physical ability to absorb the education at the time you need it most. But you gentlemen have been an example of those trying to educate us and I am, of course, willing to learn.

I am sorry that I was late this morning, Madam Chairman, so that I could say a special word to the members of the Independent Bankers Association because I have been friends of these gentlemen and associated with them. I think I have 42 banks in my district and only three of them are independent banks. I want to say this further, that you have a local representative, Mr. Schooley, here and he has been attending these hearings very faithfully.

Without deprecating Mr. Hanson or Mr. Bell, I would say Mr. Schooley has been a most helpful person in portraying to the members of the committee the positions of the Independent Bankers Association on legislation and that he is the kind of person you need to help. He doesn't try to tell you what you have got to believe. He just tells you his position. I appreciate that kind of help.

Mrs. SULLIVAN. Thank you.

Mr. GREATHOUSE. Before you close could I make a request?

Mrs. SULLIVAN. Yes.

Mr. GREATHOUSE. As I stated in the beginning this morning, that while our testimony had been prepared just for the UAW, and Mr. Clayman was scheduled to appear for the IUD, the Industrial Union Department, that after preparation of our testimony we went over it with the officers of the IUD and they requested that we also represent them. I would like, therefore, to request that where UAW appears in the body of the statement that I presented, that this be followed by the IUD, so it will be a joint statement.

Mrs. SULLIVAN. That will be done without objection. You have been very helpful, Mr. Greathouse.

I join Mr. Stephens in what he said about the independent banks as well as about the IBA's Washington representative, Mr. Schooley. I have known him over a period of some 15 years. The independent banks have always been among my favorites. I have worked hard for legislation to enable them to compete, and I intend to continue to work in that direction because we need good independent banks.

I thank you all for coming—for giving us your time and sharing your knowledge with us.

Before we adjourn, there is some congressional testimony to be included. A number of the Members have requested an opportunity to testify, but because of our very heavy schedule over the past 2 weeks, I persuaded the Members to prepare written statements which could be incorporated in the record, and these are excellent statements.

First, we will accept at this point the statement of the Honorable Warren G. Magnuson, chairman of the Senate Commerce Committee, and also chairman of a new subcommittee which he established this year on consumer legislation coming before the Senate Commerce Committee. Senator Magnuson has been one of the most effective leaders of the Senate on consumer issues and was responsible for initiating the section of H.R. 11601 which deals with credit advertising. We wrote that section of the bill largely on the basis of Senator Magnuson's draft of legislation on this subject, and we are delighted to have his comments on our bill.

STATEMENT BY HON. WARREN G. MAGNUSON, SENATOR FROM THE STATE OF WASHINGTON, CHAIRMAN, SENATE COMMITTEE ON COMMERCE

Senator MAGNUSON. Madam Chairman and members of the committee, I appreciate this opportunity to go on record before this distinguished committee in support of truth-in-lending legislation and, in particular, the credit advertising provisions of H.R. 11601. The disclosure provisions of your bill are identical to those in S. 2268, the Fair Credit Advertising Act, a bill which I had the honor to introduce and which is cosponsored by Senators Bartlett, Brewster, Clark, Dodd, Hart, Inouye, Kennedy of Massachusetts, McGee, Mondale, Proxmire, Scott, Tydings, and Young of Ohio.

The fair credit advertising provisions are designed to insure the meaningful disclosure of the cost of credit in any advertising which promotes a retail installment sale, an installment loan, or an open-end credit plan. With this legislation, we move another step forward toward our goal of securing the consumer's basic right "* * * to be given the facts he need to make an informed choice" when contemplating a loan or purchase—in this case a purchase under an installment sale contract.

The obligations imposed by this measure are simple. It requires that where a person advertises to make an installment loan or an installment sale to a would-be buyer, he must disclose the cash sale price; the number, amount, and period of each installment payment; the amount of the downpayment required, if any; the time sale price; and the finance charge, expressed as an annual percentage rate. Where the advertisement involves an open-end credit plan, there must be a meaningful disclosure of the details of that plan.

The scope of the legislation is narrow. It does not apply to credit sellers who do not advertise specific credit terms. It does not attempt to regulate the cost of credit. It merely requires that where specific credit terms are advertised, the advertiser must disclose enough information to enable a consumer to decide intelligently whether to buy for cash or credit, and, if he decides to buy on time, where to obtain the most favorable credit terms. In so doing, it extends to all consumers the basic protection which the Department of Defense has already afforded servicemen through the standards it has promulgated for all persons who advertise credit terms in unofficial military publications.

The need for this legislation is great. Since 1945, the outstanding amount of consumer debt, excluding long-term-mortgage debt, has multiplied nearly 17 times. Today, it totals about $94 billion—well over one-fourth the size of the national debt. A 1959 "Survey of Consumer Finance" published in the Federal Reserve Bulletin revealed that 60 percent of all "spending units" in the United States today have some amount of personal debt—which excludes mortgage debt—and nearly 50 percent of these units have installment debt. Personal debts for 30 percent of these families exceeded $500, and for those families affected by unemployment, the percentage with some amount of personal debt climbed even higher to 70 percent. As a suggestion of the large number of credit buyers who have greatly overextended themselves, we should note that families and individuals incurred 170,000 or 90 percent of all bankruptcies last year.

When credit plays such a prominent role in the lives of so many consumers, it is essential that they have some knowledge of the various credit terms available to them. Yet, studies indicate that no area of retail selling is as confusing to the American consumer, regardless of education or income level, as the cost of credit. A survey of the 10 most popular department and appliance stores in Baltimore conducted by Prof. Samuel Myers of Morgan State College and reported by David Caplovitz in his book, "The Poor Pay More," revealed, for example, that the cash price of each item "* * *, was practically the same in the various stores, but that there were wide variations in the credit terms leading to sizable differences in the final cost to the consumer." In short, those retailers who sell on credit are no longer competing on the basis of price, in the tradition of a truly competitive economy, but are taking advantage of the consumer's lack of knowledge and information, to compete on the basis of their ability to conceal what may be unconscionable time sale prices in apparent bargain credit terms. We should no longer permit such unethical business practices to prevail in the marketplace. Last month the Senate took the first step toward promoting true credit competition among retailers by passing the Truth in Lending Act.

It is the purpose of this legislation to strike at another aspect of this problem—the advertising of credit terms. In imposing minimum disclosure requirements in advertising, which today has become an integral part of most retail selling, the consumer, now hopelessly lost in the jungle of confusing credit terms, may be given enough guidance to enable him to seek out the most advantageous credit offer available to him. No longer will he be lured by the uninformative ad: "new TV—easy credit terms—just $2.50 per week," or the ad which positively misleads him in stating: "new TV—$130 cash or just $2.50 per week" without revealing that the payments will continue for 70 weeks. Instead, the consumer will be furnished with pertinent information enabling him to make an intelligent choice among differing products and terms with revised ads such as "new TV—$142 cash or $156 on time with easy payment of $3 per week for 1 year—18.77 percent annual percentage rate," or "new TV— $142 cash or $150 on time—just $20 down and $2.50 per week for one year—11.84 percent annual percentage rate."

Since the protection afforded by this legislation will complement that provided by truth in lending, I have followed very closely the hearings and debate on S. 5 in order to insure that the terminology and the disclosure requirements of these bills will be consistent. I was particularly pleased to see that the experiences of Massachusetts and Washington, under their recently enacted truth-in-lending legislation, had demonstrated that required disclosure of an "annual percentage rate" did not render their legislation unworkable. In fact, disclosure of this figure had apparently provided the most useful single standard for comparing various credit offers.

It is remarkable to me that the present credit system with its various methods for expressing—or concealing—interest rates has existed for so long. In a surprisingly analogous situation, this country discovered very early in its history, when government under the Articles of Confederation, that business could not easily be carried on when each State

established and issued its own currency—currency whose value was not uniform from State to State. The drafters of the Constitution met this problem by specifically providing that Congress would have the sole power "to coin money [and] regulate the value thereof," and one of the first actions undertaken by the newly established Congress was to create a decimal currency based on a dollar standard. In short, they assured that there would be a single national currency with a uniform value. A person traveling from State to State need not laboriously convert his money at each border as he would when traveling between foreign countries, and the prices or all commodities would be quoted in terms of a single medium of exchange—the dollar.

There are definite parallels between the development of our currency system, and the emergence of our system of credit. Just as a person shopping in Washington, D.C., or Seattle would be confused if one store offered its merchandise for pounds sterling, another for U.S. dollars, and a third for Greek drachmas, especially when there was little indication that different currencies were involved, so the credit shopper today must be baffled when interest charges are quoted to him on a monthly, semimonthly, or annual basis, particularly when these rates are complicated by discount or add-on provisions. He has no meaningful yardstick with which to compare the various credit terms actually available to him. Yet never before have so many shoppers needed such a uniform standard.

With all credit offers quoted in a single terminology—the annual percentage rate—the consumer can begin to compare easily and readily various credit terms available to him. Passage of "truth in lending" is the first step toward this goal. Full disclosure of credit terms in credit advertising is the next step. It will help a consumer to avoid many of the misleading half-truths in current credit advertising, and it will enable him to begin his credit shopping when he picks up his newspaper rather than when he arrives at a store and prepares to sign a contract.

In summary, the minimum disclosure required in all advertising by this bill will upgrade the quality of competition in the marketplace and help protect the consumer from unethical business practices. It will permit him to compare meaningfully both the cash and time prices offered him and to weigh the varying credit terms available to him. It will furnish him with the information with which he can make intelligent purchasing decisions. We cannot default on our obligation to afford this important protection to the Amercan consumer. If we do, he's the one who will pay our delinquency charges.

Madam Chairman, we are extremely pleased that you decided to incorporate the disclosure provisions of our draft proposal in your omnibus truth-in-lending bill, H.R. 11601. It was encouraging to note that on the opening day of the hearings before your subcommittee, the President's Special Assistant for Consumer Affairs, Miss Betty Furness, enthusiastically endorsed the advertising provisions of H.R. 11601. Also, the "father" of the truth-in-lending bill, former Senator Douglas, in testifying before this committee, not only welcomed the credit advertising additions to the truth-in-lending package, but praised your wisdom and courage in including these provisions in the bill. The only change which I would suggest here, would be to recommend that the authority to enforce these advertising provisions

be vested in the Federal Trade Commission which currently has the responsibility for policing false and misleading advertising. This would appear to me to be a more practicable solution than to provide for enforcement by private persons or by the Federal Reserve Board which currently has no machinery set up to undertake such activites.

We shall follow the progress of the truth-in-lending hearings in the House with great interest. I hope that the House will adopt the credit advertising provisions and that the Senate conferees can accept such provisions in conference. Should this effort fail, however, we shall certainly schedule hearings in the Commerce Committee and press for enactment.

Mrs. SULLIVAN. Next, we will have the statement of Congressman Matsunaga, of Hawaii, a member of the Committee on Rules and an outstanding Representative. Congressman Matsunaga is secretary of the House Democratic Steering Committee. He is one of our leaders in the House of Representatives, and a cosponsor of the Consumer Credit Protection Act.

STATEMENT OF HON. SPARK MATSUNAGA, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF HAWAII

Mr. MATSUNAGA. Madam Chairman and members of the subcommittee, I thank you for this opportunity to testify in support of H.R. 11806, a bill which would provide comprehensive consumer credit protection, of which I am a cosponsor.

H.R. 11806 is identical with H.R. 11601, which was introduced by the distinguished chairman and several members of this subcommittee.

It is a matter of common knowledge that billions of dollars of credit are extended to consumers every year. Some of this credit takes the form of contracts which run from payday to payday, and some of it extends over several decades of repayment with interest. Credit, however, has come to mean something more than a means for retailers to sell their merchandise. For thousands of financial institutions as well as retailers, credit itself is something to be sold at a profit which sometimes exceeds that realized from the sale of the merchandise involved.

The practices which are followed in the extension of consumer credit are designed to emphasize any features of the credit contract which will make the contract appear inexpensive and easy to pay off. Some States by statute regulate credit contracts with respect to the information which must be disclosed, and with respect to the maximum rates which may be charged. But, shocking as it may seem, many States at present do not require the creditor to tell the debtor what the total amount of his debt is, nor the number of payments he must make, nor the rate of interest he is being charged. And only in exceptional instances do the States which have disclosure statutes require disclosure of all the information which is necessary to a rational use of credit by the customer. Moreover, many States permit rates of charge for consumer credit which are unconscionable. The truly exorbitant rates which may be charged are at the very foundation of opposition to truth in lending—no questionable retailer and no questionable lending institution would want to tell a customer that it is charging him 18

percent, 30 percent, 42 percent, or even 75 percent per year for easy credit. Even if such rates are charged, the creditor would prefer to phrase the contract in such terms that the rate is not clearly stated to the consumer. Many States, either by statute or by the absence of any statute, permit the rate of the finance charge to be hidden by omission or by statement in terms of a monthly rate or a rate on the original balance of the debt. Such practices are misleading. Banks will clearly state the annual rate of interest that they will pay on a depositor's money. Businessmen who borrow from banks know exactly the annual rate of interest that they are paying on their loans. In their dealings with the consumer, however, both banks and businessmen often abandon the practice of stating the annual interest rate clearly and simply. Any statement of the cost of credit which does not include this annual rate is incomplete and deceptive.

On the other hand, the laws of some States do require disclosure of the annual rate of charge for the use of credit, and on particular kinds of credit as, for example, small loans, revolving credit, automobile credit, and installment credit on other goods.

H.R. 11806 would require such disclosures on all consumer credit transactions. The requirement is as simple as requiring meat markets to state the price per pound on veal roast, and to state the whole price of the roast. The bill would require all creditors to give the consumer the information which the laws of a few States now require to be given on a few types of credit transactions. By the enactment of this bill, the Federal Government would be able to raise the level of competition in the consumer credit field by finding the best existing practices and making them general rather than isolated practices.

I believe that the House bills relating to consumer credit are superior to the measure which the Senate has passed, especially with respect to finance charge disclosure. Proposed House legislation would allow no exemptions, whereas the Senate-passed bill allows exemptions for revolving credit, which is the fastest growing type of credit at retail stores and among banks; for payday loans, which often border on the extortionate even under State laws, and for any other credit which can be broken down into a series of credits, each of which imposes a charge of less than $10; and for first mortgages, which are both the largest single debt ever incurred by most families and a means of obtaining credit for many purposes other than home purchase.

The disclosure provisions of the House bills give the consumer the information which he needs for rational choice between paying cash or buying on credit, and for choice among competing offers of credit. It provides a foundation for individual choice as the controlling element in the use of the Nation's credit and money resources.

But it goes further than arming the consumer with information. It gives the consumer the protection of limitations on the rate which he may be charged by a creditor.

The rate which it sets as an upper limit—18 percent per annum—has been found a profitable rate by retailers on the small transactions for which revolving credit has been used. For larger purchasers on credit where a regular installment plan is used, States often set maximum rates which are substantially below 18 percent. Bank loans to finance purchases usually are below this limit, and their personal loans often

run 2 to 7 percentage points below the limit which H.R. 11806 would establish. Credit unions charge rates which are only one-half to two-thirds as high as the maximum allowed by this bill. The maximum rate is a rate under which an adequate volume of credit can be supplied to consumers. It offers protection against higher rates to the poor and to the youthful credit buyer who has not yet learned to shop for credit.

The bill protects the consumer further by withdrawing the most deadly of collection devices—the garnishment of wages. The creditor who now pushes credit sales of shoddy furniture, frozen foods, and other goods with complete disregard of the carrying capacity of the debtor because he can garnish the consumer's wages to assure repayment, would have to exercise restraint in order not to oversell credit to his customers, as he would no longer be able to get his payments from the consumer's employer.

Perhaps the most interesting innovation in the proposed consumer credit legislation is its direction to the Federal Reserve Board to set up guides to reasonable use of credit for the commodity futures markets as well as for the stock markets. The use of credit for speculation in commodity futures now is completely uncontrolled. Credit for speculation in futures is fraught with risk to the user, who can sustain considerable losses, and it is also disadvantageous to consumers as buyers of goods because it encourages the raising of prices on the commodities they buy.

Madam Chairman and members of the subcommittee, H.R. 11806 offers consumers a substantial range of protection against misuse of their money and of the Nation's credit and related economic resources. It is by no means a complete consumer credit code. But the protection which it would provide is basic to a sound economic system; all of the features have well tested and approved precedents, and all are consistent with each other.

For the reasons I have stated, I urge the early favorable consideration of H.R. 11806, or similar legislation, to provide comprehensive consumer protection to the American buying public.

Thank you very much.

Mrs. SULLIVAN. The next statement will be that of Congressman Rosenthal of New York, a sponsor of the Consumer Credit Protection Act and one of the leading spokesmen for consumer causes in the Congress. Congressman Rosenthal has conducted some very effective hearings on consumer issues for the Committee on Government Operations in connection with his bill to establish a Cabinet Department of Consumer Affairs.

STATEMENT OF HON. BENJAMIN S. ROSENTHAL, A REPRESENTATIVE IN CONGRESS FROM THE EIGHTH CONGRESSIONAL DISTRICT OF THE STATE OF NEW YORK

Mr. ROSENTHAL. Madame Chairman, I am happy to testify in favor of the truth-in-lending princples of your bill, H.R. 11601, and to commend your initiative in broadening the concept of consumer credit protection to cover garnishment of wages, limit of interest rates and advertising of credit terms. These, and other additions, make your bill a much stronger defense for the consumer than the Senate bill.

Because I sponsored legislation identical with H.R. 11601, I would like to comment on some of the principles involved.

I favor, in principle, limiting wage garnishment but I fear that such a goal might be better achieved by a complete revision of the idea of garnishment instead of by its outright abolition.

Garnishment can be made to serve the debtor instead of constituting a modern debtor's prison, as it presently does.

If we can limit garnishment, for example, to those transactions where repossession is impossible or excluded and can further limit it to a small percentage of the employee's wages, garnishment becomes a means of protecting him against even greater evils like bankruptcy and garnishment of his other assets.

To make such a revision in our present system of garnishment would reqiure—

(1) A strict limitation of garnishment of wages to the excess over a realistic and current living wage;

(2) Protection against firing workers under wage garnishment or from revealing information about such garnishment to subsequent employers;

(3) A uniform garnishment law to protect wages from garnishment in another State where the employer does business and where garnishment laws are more lax.

There are many ways to exempt, from garnishment, a wage needed to support a worker and his family. Present State laws provide, for example, a variety of exemptions. Many of these are outdated. Others are inadequate in protecting too small a percentage of wages above a meager dollar exemption.

I don't know the proper formula but I believe that one can be developed. Some of the excellent testimony your committee has heard can be the basis for such a study. The administration's current investigation of garnishment may be another source.

But whether the national minimum wage or the amounts covered by social security deductions or some other basis is used for exempted wages, I hope we do not forget that the basic problem in garnishment law revision is protection of the worker's livelihood.

No matter how we protect wages from garnishment, loss of a job or "blacklisting" for past garnishments can compound the debtor's problems beyond the possibility of solution.

Garnishments are an extra burden for employers also. I suggest consideration of a multiple-garnishment provision limiting this burden by allowing only one garnishment, perhaps payable to a creditors' pool.

Wage assignments can be an evil as great as garnishment. I believe they should be covered by similar exemptions and restrictions.

By correcting present practices, we can make garnishment a tool which can help people in debt, instead of making the court system an ally of unscrupulous creditors as it now is.

There are other very important aspects of H.R. 11601 which I would like to discuss.

In general, we should be wary of expecting too much of the "truth-in lending" provisions while insisting that the most comprehensive version be maintained.

I believe that it is possible to overstate the effects of full disclosure. For the consumer-debtor who needs help most, full disclosure may be insignificant. I speak of the poor consumer to whom debt is the way of life and for whom percentages, dollar amounts of interest and other facts are obscure and incomprehensible elements of an alien system.

The poor consumer, like many of his more affluent neighbors, often asks only: "How much a month will that be?" We can anticipate long-term educational effects of full disclosure but we should continue efforts toward wider concepts of consumer education which, among other revelations, will show consumers that there are times to avoid credit entirely.

To make H.R. 11601 the best possible disclosure law, however, it is necessary to include revolving credit which unfortunately was largely exempted from S. 5.

We have been showered with confusing, misleading, and misguided nonsense on this question. Some defenders of the exemption, who should know better, have indulged in rhetoric of a kind which should rattle the walls of even these well-constructed rooms. Simple arithmetic is denied and debased.

Schoolchildren who are taught to compute simple and compound interest would be amazed at the "new math" this committee has endured recently.

I would ask one simple question of these revolving creditors. If interest on revolving charge accounts is so difficult to compute and to express, why do banks state simply that they pay, for example, 4½ percent interest on savings accounts which are revolving credit accounts in reverse?

Savings accounts, like revolving credit, also have fluctuating balances; there are wide varieties among banks on how savings interest is computed. Some give interest from the first of the month, others from the 15th or 20th, some give a "free ride" by granting interest for the whole month if deposits are received by a certain date.

Yet despite these variations, which correspond to revolving credit systems, no bank I have ever heard of fails to state flatly that it pays a certain rate of interest on savings.

Nor does any savings depositor fail to understand that a 4½-percent rate annually means less than 4½ percent when the savings are left for only a few months. I would ask creditors to give borrowers the same credit for understanding that they already display as savers.

The inclusion of first mortgages in your bill, Madam Chairman, is also valuable. Although mortgage bankers insist they are better lenders than the rest since they describe mortgages in interest rates on the unpaid balance, home buyers should know what credit costs for the largest investment most of us ever make.

They should know, for example, that it cost $8,800 more in interest to borrow $20,000 for 30 years instead of for 20 years.

They should be advised that it costs $2,300 more to borrow the same amount for 30 years at 6 percent than it does at 5½ percent.

They should also be aware that when they borrow for 25 or 30 years at 6 percent interest they will pay about $20,000 in interest on a $20,000 mortgage.

The home buyers need these facts, some of which he will get from your first mortgage provision.

I hope that the committee will continue to insist on the inclusion of small loans and credits, including those where finance charges are less than $10. Here we are dealing again in an area of the poor, and often ignorant, borrower who is limited in his opportunities to get credit.

Are we helping the poor by stating that they need no protection when they pay "only" $10 for credit? How many $10 charges must a man pay before he deserves such protection? I submit that this small borrower needs more, not less, protection.

Another reason for including these small transactions is to help the consumer make comparisons between the varieties of credit available. If the overall goal of this bill is comparative shopping for credit, the borrower needs information on all kinds of loans.

For example, the small credit seekers might decide that it is better to borrow $100 at a true interest rate of 11 percent than to borrow $50 twice when the rate is 20 percent. Yet the latter transaction, if they cost only $9.90 each, would not be covered by the exclusion in S. 5.

I will not comment in detail on the other provisions of your bill, Madam Chairman. I believe you have produced a most progressive piece of legislation which will be remembered for its willingness to consider some of the hardest areas of consumer protection.

I believe the American consumer, and his advocates, in whose group I am proud to be counted, can take great satisfaction in your leadership.

Mrs. SULLIVAN. Next, we will have the statement of Congressman Ryan of New York, who is a cosponsor of H.R. 11806 introduced by Mr. Multer of New York which is identical to H.R. 11601. Congressman Ryan is vitally interested in the "truth-in-lending" issue and has long supported the legislation first introduced in 1960 by former Senator Paul Douglas.

STATEMENT OF HON. WILLIAM F. RYAN, A REPRESENTATIVE IN CONGRESS FROM THE 20TH CONGRESSIONAL DISTRICT OF THE STATE OF NEW YORK

Mr. RYAN. Madam Chairman, for a number of years I have introduced "truth-in-lending" legislation. I was pleased to join Senator Douglas in his early efforts for legislative action in this area. Now I have cosponsored the bill proposed by your committee, by introducing H.R. 11806.

The consumer credit bill which the subcommittee has drafted, recognizes that action must be taken in an area which has gone unregulated and in which abuse has grown as credit has expanded. The bill recognizes the necessity for a full disclosure of the facts about the cost of credit.

Consumers cannot rationally decide whether to incur debt or to save, and whether to take one credit offer or a competing offer, unless they are able to consider all the relevant facts: the total amount of the credit, the total charge for the credit, and the common denominator of the annual rate charged for the use of credit.

H.R. 11806 is superior to the credit disclosure bill passed by the Senate as a means of enabling consumers to use credit wisely; it makes no exceptions for revolving credit, for small-figure charges, or for first mortgages.

Revolving credit is becoming a leading form of consumer credit at retail stores. And within the past year, the commercial banks have been stampeding into this form of credit. A few dozen banks offered revolving credit a year or so ago; now more than one-tenth of the number of banks, and a much higher percentage in terms of bank resources, offer revolving check credit or finance retailers' revolving accounts. If extensions of this kind of credit are not required to indicate the annual rate of charge, and they are not required to state the annual rate under the Senate bill, revolving credit merchants and bankers will gain a competitive advantage, and the consumer will be uninformed about the true price of a growing segment of the credit offered to him.

H.R. 11806 makes no exceptions for small-figure credit charges, because evasion of the purpose of full disclosure can easily be achieved by breaking credits into pieces, each of which costs less than the minimum exempt amount. By not allowing exemptions for small charges, evasion is prevented.

The bill does not permit an exemption for creditors who extend credit against first mortgages—whether the mortgage finances the purchase of a house, or has been rewritten to provide the funds for education, automobile purchase, or any other purpose. The homeowner should know the total cost of his credit, so that he can figure the advantages of paying for his home as quickly as possible, and so that he can compare the cost of financing purchases through adding on to his mortgage as against other methods of finance.

Through disclosures of the facts needed for rational use of the credits available to the consumer, and of the consumer's income, the consumer credit world will begin to change from a maze of incomplete information and misinformation into a system where the efficient and inexpensive source of credit will predominate, and the deceptive and costly will be eliminated.

However, disclosure of information alone is not sufficient to protect consumers. It is not unusual to require that the maximum rate charged on credit shall be limited. Usury statutes have done this for centuries, and special rate limitation statutes of the States have been doing so in every-increasing numbers for the last half century. But the exorbitant rates, often running above 30 or 40 percent, or even higher, which the States have allowed for credit on used automobiles, payday loans, and so forth, are unjustified. A limit on annual rates of charge on consumer credit will protect the neediest debtor and also the young family, new to credit buying and unfamiliar with the range of available rates.

The consumer's income will go further by reducing excessive speculative swings in commodity futures contracts which affect consumer prices. While the speculator in stocks and bonds is required to meet margin requirements of the Federal Reserve Board, the speculator in commodities is under no such restraint. With a few hundred dollars he can buy and sell futures contract for many thousands of dollars worth of commodities. The bill takes a step towards parity of treatment of stock speculators and investors and speculators in commodity futures, by authorizing the Federal Reserve to regulate the use of credit for commodity futures trading.

The proposed legislation should contribute substantially to economic stabilization at all times. But in times of national emergency, it is

dangerous to leave private buying and selling, and use of credit, without restraint. The bill authorizes temporary controls which will restrain the use of credit to conform with the current incomes and with availability of commodities, so that excessive purchases, shortages, and rising prices may be avoided.

The burden of keeping the use of credit within such bounds as are beneficial to consumers and to the national economy is not placed entirely on consumers and on Federal regulatory agencies. The legislation also puts some of that burden on the businesses which extend credit. It does that by prohibiting the garnishment of wages. The tragedies which follow the zealous use of garnishment have been cited time and again in truth-in-lending hearings, and in the work of legal aid groups in New York and elsewhere. The bill simply prohibits the garnishment, placing upon the creditor the burden of restraining his overselling, and limiting himself to credits and rates of charge on credits which are within the reach of his customers.

Finally, the bill proposes the creation of a National Commission on Consumer Finance. Such a Commission should have been authorized years ago when the truth-in-lending movement began, but at that time there were many obstacles. With a consumer credit protection law in effect, the consumer finance industry could participate in providing the details of its operation which would assist in the formulation of regulations.

Let me commend the subcommittee for its constructive efforts in this area. Consumer interests are by nature disorganized. Therefore, they depend for their protection upon the public-mindedness of legislators such as the members of this subcommittee. It is a privilege for me to cosponsor what should become landmark legislation.

Mrs. SULLIVAN. Congressman Scheuer of New York, whose statement will follow, brings to his membership in the House of Representatives an impressive background in law, public administration, and private business. As a businessman he made a notable contribution to the redevelopment of our cities through his redevelopment and housing activities, including the Southwest area here in Washington. He is very close to the problems of moderate- and low-income families.

STATEMENT OF HON. JAMES H. SCHEUER, A REPRESENTATIVE IN CONGRESS FROM THE 21ST CONGRESSIONAL DISTRICT OF THE STATE OF NEW YORK

Mr. SCHEUER. Last month, the Senate passed S. 5, the Truth in Lending Act, which brought to fruition a proposal first advanced by Senator Paul Douglas in 1960. For years, Mr. Douglas maintained interest in and actively worked toward gaining support for this proposal. We now are the beneficiaries of his labor. The concept of truth in lending grew from an awareness of a need to enlighten consumers about the cost of their credit transactions.

The volume of consumer credit increases yearly and yet the individual consumer does not understand just how much it costs him. There have been instances where individuals have paid up to 289 percent interest on used automobiles or 285 percent on television sets. When rates are expressed on a monthly payment basis, the average person does not know the mathematics involved in arriving at a

realistic figure for their total interest. Full credit disclosure would enable the consumer to compare prices and effective interest rates in order to decide how best to spend his money. S. 5 is not a regulatory measure but an informational one.

I have serious doubts about whether this bill effectively regulates the total range of problems. For this reason, I am a cosponsor of a bill introduced by Representative Multer, H.R. 11806, which is identical to H.R. 11601 introduced by Mrs. Sullivan. The bill I support provides for credit disclosure, and more. A creditor must alert a buyer as to price, finance charges incident to credit extension, and the annual interest rate on credit transactions. This includes advertisements of such transactions as well. The bill also fixes a maximum finance charge of 18 percent a year or the rate prescribed by State law, whichever is less. It is splendid to put consumers in a position of choice but where the choice is for the lesser of two evils, the effect of the legislation diminishes in value.

The only exemption to the disclosure provisions of H.R. 11806 is with regard to commercial transactions. Disclosure thus applies to all home mortgages. While first-mortgage laws contain some disclosure requirements, there is still abuse in this area. Therefore it is advisable for the bill to include first mortgages as well as second and third mortgages.

There has been a great deal of controversy over the question of revolving credit. There seems to be no persuasive reasons for exempting ordinary revolving credit accounts from the provisions of the bill. The same explanation used to justify an exemption to the disclosure proposal can be utilized to bring revolving credit within the bill. The annual rate of interest can be determined from the time the credit charges begin and thus be exact and meaningful, as opposed to the attempt to state it from the time of purchase where the free-ride period is brought into play. To differentiate between simple revolving credit and the installment type, will lead to drawing very fine lines and will encourage the converting of the latter type to the former in order to avoid disclosure. The safeguards incorporated by the Senate bill might mitigate, but would not eliminate, this problem.

The basic purpose behind the legislation is to aid and protect the consumer from one particular pitfall in his complex environment. There is no justification for any exception to full disclosure, regardless of amount or type of credit.

Aside from disclosure, the bill has additional provisions to protect the individual debtor. Use by creditors of judgment confessions is prohibited as is garnishment of wages. The Federal Reserve Board is also given regulatory powers to limit credit extention in emergency situations.

I fully support H.R. 11806. After 7 years of struggle, Mr. Douglas' truth-in-lending concept passed the Senate in compromised form and the bill now appears before this body for approval or for restoration to its original form. Disclosure could give the public a realistic awareness of price and interest rates. The other provisions of H.R. 11806 would greatly enhance the effect of disclosure and give to it a more practical value.

The dilemma of the American consumer caused by the sophisticated techniques of the credit world in which he deals demands our sympa-

thetic concern and best efforts. We cannot afford to compromise where the consumer is involved.

Mrs. SULLIVAN. Our next statement will be from Congressman Farbstein, of New York. I am glad to see so many Members of the House from New York taking a very strong and active interest in this legislation. Congressman Farbstein serves on the Foreign Affairs Committee but does not permit his heavy workload on that committee to deter him from taking a very vigorous interest in all issues in the House which concern his constituents as consumers.

STATEMENT OF HON. LEONARD FARBSTEIN, A REPRESENTATIVE IN CONGRESS FROM THE 19TH CONGRESSIONAL DISTRICT OF THE STATE OF NEW YORK

Mr. FARBSTEIN. Madam Chairman, credit has become an integral part of our economic way of life. It allows the consumer to enjoy a variety of goods while paying for them over a period of time. However, the innumerable credit plans offer a bewildering assortment of rates and terminology. The result has been public confusion and misunderstanding. I believe it is time that the Congress passed comprehensive legislation aimed at ending this confusion by assuring the consumer easily understood credit standards.

Basic to any consumer legislation is a provision requiring full disclosure of credit terms. In my opinion, this should include disclosure of finance charges by annual percentage rates as well as in dollars and cents. Contrary to the Senate passed truth-in-lending legislation, I believe full disclosure should include such areas as revolving charge accounts and first mortgages on homes. Although revolving charge accounts represent only a small part of the total consumer debt, it is the fastest growing form of credit used, particularly by the small purchaser who can least afford excessive credit rates. Additionally, I believe there should not be a minimum limit on the dollar size of a credit transaction covered under this legislation. Again, low-income citizens would be the ones most injured by abuse of credit practices on small dollar purchases.

Full disclosure of finance charges will enable the prudent consumer to match credit plans with personal needs. It will also make it easier for him to compare different sources of credit. I believe the Congress has a responsibility to assure the American consumer adequate information on which to make wise credit decisions. Such informed use of credit can increase the competition among credit institutions to the general benefit of the consumer.

One of the most alarming trends in American life is the growth of personal financial failures. This is particularly true in States where the garnishment of wages to pay overdue credit debts is allowed. Such a practice often leads to the filing of bankruptcy by individuals, forcing them to claim poverty in court. This can disrupt a person's life. It could even cost a person his job at a time when he needs it most. It will not guarantee the creditor his money back. In my opinion, we should move to prohibit the practice of garnishment of wages as detrimental to sound credit relations.

The size and complexity of the consumer credit industry requires that we know much more about it then is presently true. I believe

the creation of a nine-man National Commission on Consumer Finance, to study the credit industry, is essential to the development of effective legislation. The appointment to the commission of three members of the Senate and three members of the House will assure the Congress a major role in proposing recommendations for future legislation.

The three legislative provisions I have outlined in this statement are basic to any sound consumer protection program. There are, additionally, issues to which the Subcommittee on Consumer Affairs should give careful consideration. They include the regulation of trading in commodity future contracts affecting consumer prices, a system of controls to prevent inflationary spirals, and the establishment of maximum rates of finance charges. These are all complicated problems. I know the subcommittee will study them carefully before acting.

Madam Chairman, the members of the Subcommittee on Consumer Affairs should be commended for the work they are doing to assure the consumer fair and understandable credit standards. I support your efforts and urge early passage of legislation aimed particularly at guaranteeing the consumer full disclosure of credit information.

Mrs. SULLIVAN. Congressman Lester L. Wolff, of New York, prepared a statement for presentation to the subcommittee on this legislation and would have appeared in person if we had been able to schedule time for congressional witnesses. Congressman Wolff has always been a strong and effective advocate of consumer causes in the Congress and we are pleased to have his statement appear at this point.

STATEMENT OF HON. LESTER L. WOLFF, A REPRESENTATIVE IN CONGRESS FROM THE THIRD CONGRESSIONAL DISTRICT OF THE STATE OF NEW YORK

Mr. WOLFF. Mr. Chairman, I am greatly encouraged to see the House consider the Senate-passed version of a long-needed truth-in-lending bill. Such legislation will be an important and necessary milestone in consumer protection and I look forward to passage of a truth-in-lending bill by this House during this session. Together with truth-in-packaging legislation the bill now before you can serve honest businessmen and consumers by ending the ancient practice of caveat emptor.

Legislation such as that now before your committee is most important. In the area of consumer credit, hidden charges, add-on rates, and low sounding "monthly rates" require acute financial understanding. It would be too much to expect all those who use our vast credit facilities to be knowledgeable in this area.

It is important to note that I do not for an instance charge intentional deception; the vast majority of credit institutions and retail stores are scrupulously honest. However the confusion created by the current credit alternatives makes it very difficult for most consumers to make an intelligent decision on where and how to borrow. Recent polls have shown that most people believe their interest rate to be only one-third of what it really it. The consumer is confused and we can and should help to correct that confusion.

Since retail credit is growing four and a half times faster than our economy and since the retail credit business now grosses $92.5 billion annually, the confusion that exists in this field is rightly the concern of the Federal Government. We are dealing here with a significant and major factor in our economy.

The solution to the very real and very serious problem facing us is not regulation—the solution is education. The small print must be clarified, the actualities explained. The consumer need not be told where and how to borrow. However, he does deserve to be informed about the borrowing options open to him and the cost of the options. This is what S. 5 does and this is what is needed.

This point helps to clarify the discussions about the inclusion of revolving credit in the House bill. The goal of the legislation, to extend what I said a minute ago, is to make the consumer aware of the range and type of credit charges and to express these charges on an annual basis for clarity and comparison. Such action should also include revolving credit.

Within the next 5 years, estimates are, revolving credit will represent 50 percent of all consumer credit. Because of its importance it is imperative that revolving credit be included in the scope of the truth-in-lending bill. Thus, I strongly support the reinstatement of full disclosure provisions for revolving credit accounts as outlined in the original version of S. 5 considered in the Senate. The public has the right to know of the credit charges involved in revolving credit. Those who take the other position are justified in urging that consumers be made aware of the "free ride" period and other means of avoiding credit charges.

But only through complete disclosure, including revolving accounts, can we properly protect the consumer, fulfill the objective of this legislation, and bring order and clarity into the confused and chaotic marketplace.

Passage of this legislation will be an important step, but it must be accompanied by an increase in public education. An excellent study by Dr. Monroe Friedman and Dr. Alfred H. Lieverly of Eastern Michigan University of the short-term effects of truth-in-lending legislation concludes that sudden, unannounced replacement of variable rate information with uniform rate information will not at first help the consumers. Borrowing decisions are currently made on such peripheral issues as location and size of the lending institution. Unless a complete and planned education campaign accompanies truth-in-lending legislation the potential good of such legislation will be long and slow in coming. Your committee, Madam Chairman, must consider the implications of the Friedman-Lieverly study. I recommend that the committee, in its consideration, make plans for the most effective and widespread education campaign to accompany passage of a truth-in-lending bill during this session.

The buyer should not be beware—he should be aware. He should be aware of the value of standardized criteria as a means for choosing among credit opportunities. Education is the key, first through the inclusion of revolving credit in the pending legislation, and second through a campaign to inform the public of the service provided by truth-in-lending legislation.

I urge your attention to these matters in your consideration of truth-in-lending legislation and when you make your report to the House.

Thank you.

Mrs. SULLIVAN. That completes the statements I have from Members of Congress for inclusion in the record at this point. There are additional statements for the record which will be inserted either at this point or in the appendix. With that, the hearings are recessed subject to the call of the Chair.

(Whereupon, at 12 noon, the subcommittee adjourned, subject to call of the Chair.)

(The following statements and letters were submitted for inclusion in the record:)

CONGRESS OF THE UNITED STATES,
HOUSE OF REPRESENTATIVES,
Washington, D.C., August 25, 1967.

Mrs. LEONOR K. SULLIVAN,
Chairman, Subcommittee on Consumer Affairs, House Banking and Currency Committee, Rayburn House Office Building.

DEAR MADAME CHAIRMAN: I am writing with respect to the disclosure terms of the Truth-In-Lending legislation now being considered by your Subcommittee. I am concerned about a change made in the original Senate bill and I want to express my hope that the same change will not be made in H.R. 11601. After studying the Senate hearings, I have come to the conclusion that exempting certain credit grantors from annual-percentage-rate disclosure is discriminatory, confusing and unjustified.

This exemption would discriminate against small, independent specialty store retailers in favor of large department and chain stores. It would be confusing to the consumer and defeat the basic purpose of the bill—to make it easier for a prospective customer to compare credit service charges. Small business should not be placed at a disadvantage particularly when the result is less protection to the consumer.

I support Truth-In-Lending legislation but I cannot support the Senate provision of differential disclosure methods. Uniform methods of disclosure would enable consumer comparison and determination of the best available rate on the market. As you know, California already has consumer protection laws insofar as credit rate disclosure is concerned, and I would oppose any federal legislation which operated in a discriminatory way against the smaller retailer.

Sincerely,

DON EDWARDS,
Member of Congress.

STATEMENT OF U.S. SAVINGS & LOAN LEAGUE

The United States Savings and Loan League[1] supports the principle of truth-in-lending and the general objectives of H.R. 11601 and H.R. 11602 (S. 5). Most Americans are not experts in computing interest rates and it is important that they be advised of interest charges on some basis of uniformity that permits comparison of the competing financing arrangements.

The U.S. League has specifically endorsed H.R. 11602 (S. 5), the Senate passed measure and would specifically endorse H.R. 11601 if it were amended to (a) exempt first mortgage lending and (b) eliminate the 18 percent usury provision.

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[1] The United States Savings & Loan League has a membership of 5,100 savings and loan associations, representing over 95% of the assets of the savings and loan business. League membership includes all types of associations—Federal and state chartered, insured and uninsured, stock and mutual. The principal officers are Otto Preisler, President, Chicago, Illinois; Hans Gehrke, Jr., Vice President, Detroit, Michigan; C. R. Mitchell, Legislative Chairman, Kansas City, Missouri; Norman Strunk, Executive Vice President, Chicago, Illinois; and Steve Slipher, Legislative Director, Washington, D.C. League headquarters is at 221 N. LaSalle Street, Chicago, Illinois; and the Washington Office is maintained at 425 13th Street, N.W., Washington, D.C. Telephone: 638-6334.

The case for exempting first mortgage real estate lending was well stated by the Federal Reserve on August 10 by Vice Chairman J. L. Robertson. The Federal Reserve, of course, is an independent agency and is obviously not a special advocate of the savings and loan viewpoint.

The Federal Reserve statement says:

"We believe first mortgage loans on real estate should be exempt, as provided in S. 5, because there is already reasonable disclosure in this field and disclosure requirements developed for relatively short-term credit are inappropriate for loans with maturities of 20 to 30 years. To require that the annual percentage rate be recomputed to reflect costs incidental to the extension of credit would involve particularly troublesome questions in first mortgage lending because of the number and variety of the costs assessed at closing, many of which would be incurred, in whole or in part, by a prudent cash buyer if no credit was extended. While it would be possible to spread discounts and other credit-related costs over tLe life of the contract as a part of the annual rate of finance charge, we feel that this might tend to mislead the borrower. Such charges are in the nature of 'sunk cost' and are borne in full by the borrower whether the loan is repaid in 1 year or 30. To require disclosure of total dollar finance charge, including interest payable over the whole life of the contract, might be more misleading than helpful. The present value of a dollar of interest to be paid 20 to 30 years hence is substantially less than one dollar, and relatively few first mortgage contracts appear to be carried all the way to maturity."

Mortgage lending has been the only major type of non-business lending which has traditionally been on a simple annual interest rate basis. The rate stated in the contract to the home buyer is either exactly or within a few hundredths of a point of the actuarially computed interest rate. It would seem most ironic if those who have aleady pioneeded in "truth-in-lending" would be blanketed in the provisions of the bill. There are about 5 million mortgages made each year and the disclosure requirements would unnecessarily place this major burden on the lending institutions and on the Federal Reserve which must administer the program.

Our objection to the 18% Federal usury ceiling is a matter of principle rather than substance. Obviously, no mortgage lenders are charging rates anywhere near 18%. However, we must respectfully raise objection to the concept of any Federal ceiling on interest rates.

State usury laws have generally proved ineffective at protecting the public interest. Where the ceiling is higher than the market rate, it is meaningless. Where the ceiling is lower than the market rate, all lenders with an option to lend in other states will tend to do so, reducing the amount of credit available in the usury state. It does no service to a prospective borrower to protect him against higher interest rates if the result is that he gets no loan at all.

More specifically, it is inevitable that those lenders affected by an 18% ceiling—"small loan" lenders—will argue that it is discriminatory to place an effective ceiling on them without placing an effective ceiling, such as 6% or 7%, on mortgage lenders. The logical conclusion would be for Congress to attempt to set appropriate ceilings on all classes and sizes of loans to which we (and undoubtedly all other lenders) would be unalterably opposed.

We believe that S. 5 or H.R. 11601, with the amendments we have recommended, will do a tremendous job in accomplishing the objectives of "truth-in-lending". Under the provisions of H.R. 11601, loans made on a "discount basis" or on an add-on basis would be converted to an approximate simple interest rate. First mortgage loans are already stated to within a fraction of the true annual interest rate. We urge that the modified bill be passed at this time and if further refinements are necessary they certainly can be made by the Congress upon the basis of experience gained under this legislation.

STATEMENT OF CHAMBER OF COMMERCE OF THE UNITED STATES BY F. TURNER HOGAN [1]

The Chamber of Commerce of the United States presents the following comments on H.R. 11601, the Consumer Credit Protection Act:

It is the view of the National Chamber that consumer credit disclosure legislation is a matter for the states rather than the federal government.

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[1] F. Turner Hogan, Staff Attorney, Banking and Monetary Policy Committee, National Economic Development Group, Chamber of Commerce of the United States.

Traditionally, state governments have exercised authority for regulating consumer credit. Legislation relating exclusively to one or more aspects of consumer credit is in force in every state. Forty states have enacted retail installment sales acts. These laws provide extensive protection to over 80% of the total population. Most of these statutes require everything that the Senate-passed S. 5 does except for a statement of charges as an annual rate.

Any needed changes in credit law will undoubtedly be covered in the project of the National Conference of Commissioners on Uniform State Laws to develop a model state law which will deal with all phases of consumer credit.

It is our understanding that this project is more than half completed and a model law should be ready for consideration by the state legislators no later than 1969.

The Conference has been working on this project for nearly three years in a deliberate but effective manner. Its members and workers are some of the most experience and knowledgeable people in the consumer credit field and both the consumer and extender of credit are represented. The Conference's methodical procedure for developing a uniform statute is far more likely to produce a workable, effective law than any other body or organization that has approached the problem so far.

The National Chamber, therefore, opposes H.R. 11601 since federal action is unwarranted. We also believe that all proposed consumer credit legislation should be suspended until the work of the Uniform Consumer Credit Code project of the National Conference of Commissioners on state laws is completed.

DISCLOSURE PROVISIONS

Comparison of S. 5 with H.R. 11601, the Consumer Credit Protection Act

Insofar as disclosure is concerned, H.R. 11601 goes much too far.

H.R. 11601 does not exempt first mortgages as does S. 5. Since the rate of interest on first mortgages is already clearly stated and the various charges are itemized, it is not necessary to subject this type of financing to the special requirements set forth in H.R. 11601.

Finance charges of less than $10 on consumer credit sales and loans are exempted from disclosure by S. 5, but not by H.R. 11601. To include transactions of this amount or less would be an undue burden on business and in many cases the cost of compliance would rule out the financing of small purchases.

Charges for premiums for credit life and accident and health insurance, if itemized, are excluded as finance charges by S. 5 but not by H.R. 11601. Insurance premiums are not a part of finance charges and should not be shown as such.

The statement of rate on revolving credit plans is required only as a percentage rate per period under S. 5, whereas H.R. 11601 requires the annual rate at which the charge is computed. The annual rate a revolving credit customer will pay cannot be calculated in advance since the time that will elapse between date of purchase and date of payment cannot be determined in advance. Requiring the creditor to give the annual rate in advance would force him to rely on guesswork and in many cases to quote a false rate.

Under S. 5, until January 1, 1972, the annual rate may be expressed as a percentage rate per year or as a dollars per hundred per year rate of the average unpaid balance. After this date all rates are to be expressed as percentage rates. Under H.R. 11601, all rates are to be expressed as percentage rates after June 30, 1968. We prefer that this alternative continue indefinitely, but at least it should continue until 1972.

OTHER PROVISIONS

In addition to the above disclosure provisions, H.R. 11601 differs from S. 5 in that it departs completely from consumer credit disclosure and includes provisions which should be removed from current consideration.

Among these are:

Establishment of a Federal ceiling of 18% on the annual percentage rate of any credit transaction

As with consumer credit disclosure, enactment of usury laws should continue to be the province of the states. Usury laws differ from state to state and rightfully so because each state knows its own circumstances and is entitled to write its usury law accordingly. Enforcement and administration of such laws can be handled locally. A Federal usury law such as suggested in H.R. 11601, could not

cope with or adequately adjust to the availability of funds for consumer credit in the various states. It could substantially reduce the availability of funds for consumer credit from responsible financial institutions and force poorer borrowers into the hands of loan sharks operating outside the bounds of law. This is not part of consumer credit disclosure.

Prohibition of the garnishment of wages for the satisfaction of debts

H.R. 11601 would prohibit wage and salary garnishment. Again, this has been historically considered solely within the jurisdiction of the states. If it is considered at all, it should be the subject of a separate study. This, too, is not part of consumer credit disclosure.

Creation of a National Commission on Consumer Finance to make an investigation of the entire consumer credit industry

H.R. 11601 establishes a nine-member National Commission on Consumer Finance. Its purpose would be to study and evaluate the functions and structure of the consumer finance industry. The National Conference of Commissioners on Uniform State Laws has and is continuing to make such a study for the purpose of determining what should be included in its model state code. Its study deals with all phases of consumer credit. It is not necessary to duplicate this work by establishment of a nine-member National Commission sponsored by the Federal Government.

Granting of standby powers to the Federal Reserve Board of Governors to restrict or regulate consumer credit in periods of national emergency

H.R. 11601 would give authority to regulate consumer credit along the lines of Regulation W. The National Chamber deems it vital to recognize that direct government controls of consumer credit are not justified except as a war measure for limitation of nonessential production. Consumer credit performs an essential function in the processes of production and distribution. Interference with its normal flow offers an obstruction to effective operation of the free enterprise system. In 1966 an effort was made, as part of the extension of the Defense Production Act, to reinstate consumer credit regulation, on a standby basis. This effort was overwhelmingly defeated by the House. There were greater and more immediate inflationary pressures at that time than at present. The House determined that such regulation was not needed then. The National Chamber does not believe it is needed now.

Establishment of minimum margins for trading in commodity futures

The bill authorizes regulation of credit and credit margins on commodity exchanges. In 1950, regulation of commodity exchange credit was proposed by the Administration as part of its stabilization program in the Defense Production Act. The measure was not adopted. Like consumer credit regulation this proposal has nothing to do with disclosure of cost of consumer credit.

SUMMARY

The Chamber of Commerce of the United States believes that S. 5 as passed by the Senate is preferable to H.R. 11601. However, we believe that consumer credit legislation can best be handled by the states.

STATEMENT OF THE FARM AND INDUSTRIAL EQUIPMENT INSTITUTE

This statement is submitted on behalf of the Farm and Industrial Equipment Institute (FIEI) whose 220 active member companies make more than 90% of all farm and industrial equipment manufactured in the United States. A substantial portion of this equipment is sold by dealers on an installment basis. Many of our members would be affected by S–5 or H.R. 11601 because they purchase such installment paper from dealers.

Substantial amounts of such paper are also financed through sales finance companies and banks. Even members who do no financing would be affected by S–5 or H.R. 11601 in that they want financing to be available to ultimate purchasers in satisfactory and sufficiently flexible forms regardless of who the ultimate financer is.

Section 202(n) of H.R. 11601 (which is identical with Section 8 of S–5) provides that the rate disclosure requirements of the bill shall not apply to:

"(1) Credit transactions involving extensions of credit for business or commercial purposes * * *."

Section 202(b) (which is identical with Section 3(b) of S–5) defines "credit" to mean debts contracted by the obligor:

"Primarily for personal, family, household *or agricultural* purposes."

Similarly, Section 202(c) (which is identical with Section 3(c) of S–5) defines "consumer credit sale" to include sales of goods which are purchased "primarily for a personal, family, household *or agricultural* purpose."

Commercial farmers are businessmen. The equipment manufactured by FIEI members and purchased by farmers is acquired for business or commercial purposes just as much as production equipment in any other industry. Farmers purchase equipment when they conclude that the investment is a good one in terms of greater efficiency, lower costs, or greater capacity. They are at least as astute in analyzing the needs of their enterprise and the best way to finance these needs as other businessmen who are exempted from the bills.

If Section 202(n) stood alone, extensions of credit to farmers for the purchase of equipment would clearly be exempted from the rate disclosure requirements of the Act along with other kinds of commercial credit. However, the express reference in Subsections (b) and (c) of Section 202 to "personal, family, household *or agricultural* purposes" singles out this particular commercial transaction and subjects it to rules otherwise applicable only to consumer transactions.

We think the reasons for excluding commercial credit from these bills are sound, and these reasons apply to farm credit just as much as other commercial credit. The most important reasons, as we see them, are:

(a) It is only in the consumer area that a need for regulation has been shown. The large number of different ways in which credit is offered to consumers makes it especially difficult for them to make intelligent choices—e.g., sales finance companies, banks, credit unions, Morris Plan companies, revolving credit accounts and consumer loan companies all express their charge for credit in differing ways. Since some consumers present a much greater degree of risk than others, some consumer credit carries very high rates. Therefore, it is important that consumers eligible for less expensive credit understand what their choices are. Many consumers are both necessitous and unsophisticated and may be misled by some ways in which the charge for consumer credit is sometimes expressed. For these reasons, helping the consumer compare credit costs is so important that a law requiring everyone who finances consumers to state his charge in exactly the same way may be justified.

(b) No such need has been shown in the case of commercial financing. No one has established that commercial borrowers are making unwise choices or borrowing too much because they do not understand their credit costs. There has been no showing that present methods of computing and expressing the cost of credit have misled or confused any commercial borrowers.

(c) The need for flexibility in commercial financing methods is more important than supplying the business borrower with a single yardstick for comparing credit costs. Credit procedures must fit the peculiar practices of particular industries and in our dynamic economy these are constantly changing. Innovation and imagination should not be impeded by the need to always charge for credit in a way which conveniently permits computation of a rate per annum.

We therefore urge that Sections 202(b) and 201(c) be amended by omitting the specific reference to agricultural credit so that agricultural financing will be included in the exemption of business and commercial credit contained in Setion 202(n).

(The following statement was submitted by The Reverend Shirley E. Greene, director for economic concerns, Department of Social Justice, National Council of the Churches of Christ in the U.S.A., of which The Honorable Arthur S. Flemming is president, 475 Riverside Drive, New York, N.Y.:)

DEPARTMENT OF SOCIAL JUSTICE,
NATIONAL COUNCIL OF THE CHURCHES OF CHRIST IN THE U.S.A.,
New York, N.Y., August 16, 1967.

MRS. LEONOR K. SULLIVAN,
House of Representatives,
Washington, D.C.

DEAR MRS. SULLIVAN: I am pleased to enclose a statement on behalf of the National Council of the Churches of Christ in the U.S.A. regarding the "Truth-in-

Lending" Bill (H.R. 11601) which is currently in hearings before your Sub-Committee on Consumer Affairs.

This statement which, in general terms, supports the bill is for your information, and I trust that it may be made a part of the record of these hearings.

You will note particularly that it is our feeling that the modifications which were made by the Senate to their original bill, S. 5, had the effect of seriously weakening the legislation. It is our urgent hope that your Sub-Committee will bring forth a bill which is at least as strong and broad in coverage as the original S. 5; and that subsequent passage of such a bill by the House of Representatives the Conference Committee may retain essentially the stronger version.

Thank you for your attention to the views of the National Council of Churches in this important matter.

Cordially yours,

Rev. SHIRLEY E. GREENE.

STATEMENT OF THE NATIONAL COUNCIL OF THE CHURCHES OF CHRIST IN THE U.S.A.

IDENTIFICATION

The National Council of the Churches of Christ in the U.S.A. is a council composed of thirty-four Protestant, Anglican and Orthodox communions whose aggregate membership is about 42,000,000. Only the General Assembly or the General Board can approve policy statements on behalf of the Council. The General Assembly meets every three years; the General Board meets three times a year. The Assembly numbers about 800; both lay church members and clergy are represented. They are appointed as representatives by the member communions according to their own procedures. About 270 General Assembly representatives are elected by that body to sit as the General Board.

Obviously the General Board does not, nor does it profess, to speak for the constituent communions or for the millions of individual church members. It does have the authority to formulate and state the policy of the Council arrived at through a deliberative process designed to give all points of view within the churches a careful hearing.

RESOLUTION

In its meeting on February 21, 1967, the General Board passed the following Resolution on the subject of truth in lending:

Whereas consumer credit has become an important and increasing factor in maintaining the viability of the American economy; and

Whereas many Americans, and most particularly persons of limited educational attainment and low income, are regularly victimized by excessive rates of interest, by lack of information or by misinformation regarding the true cost to them of the money which they borrow; and

Whereas the National Council of Churches has affirmed that motives of economic self-interest "must be kept in harmony with concern for the welfare of the community" and that "the Church should keep under the strongest criticism any economic institutions and practices which emphasize self-interest above social responsibility";

Therefore, be it resolved: that the General Board of the National Council of Churches supports in principle the passage of legislation which will require all lenders to inform all borrowers in clear and unmistakable terms of both the dollar cost and the approximate annual percentage rate of interest on each and every loan.

COMMENTARY

In view of the position stated in this resolution, we expressed to the Senate Sub-Committee on Financial Institutions our satisfaction with S. 5 when it was before them a few months ago. We are gratified that the Senate subsequently passed S. 5, although we were regretful of the several exemptions which the Senate wrote into the bill. In our opinion the exemption of interest charges of less than $10.00, of revolving charge accounts, and of first mortgages seriously curtails the effectiveness of the bill. It is our hope that your action will result in reporting out a bill which is at least as strong and as broad in coverage as the original S. 5.

In further comment on this situation and on our resolution, permit us to spell out in a little more detail the nature of the National Council's concern for full disclosure in relation to consumer credit. Our concern is two-fold. On the one

hand, we would be prone to support full and frank disclosure of all pertinent information in any aspect of buying and selling, lending and borrowing, or other financial transaction. On the other hand, we are particularly concerned about truth in lending as it bears on the poor.

Small loan borrowing and installment buying has become increasingly the means by which the American people avail themselves of the benefits of our abundant national productivity. Nearly all levels of our society are heavily involved. We assume that your committee will be thoroughly briefed on the volume and composition of the credit market. We mention it only to emphasize the very great importance of creating and maintaining adequate safeguards around this institution which has become so vital a part of our total economy.

We are convinced that our whole society will benefit from the passage of legislation which will require lenders to provide each borrower in writing with full disclosure of the cost to the borrower of the credit being extended to him. Although we understand that nothing in this proposed legislation is designed to alter or limit the rates of interest charged by lenders, we do believe that borrowers will be greatly aided in money management if they are in possession of full information as to the cost to them of loans they may be considering.

All that we have said regarding the value of this legislation for the general population applies with peculiar force with respect to persons of low income and low educational attainment. Because of their lack of financial resources, such people may find borrowing even more necessary than do the majority of us who are more economically secure. Because of their poverty, the same rate of interest represents a higher percentage charge on their income than is the case with borrowers in higher income brackets. Because of their poverty, they constitute a higher risk to the lender. This tends to force them to patronize the type of loan company which specializes in high risk loans and charges correspondingly high rates of interest. Because these people are often of relatively low educational attainment, their ability to figure interest rates or understand them or to comprehend the implications of the often obscure and sometimes misleading interest rate quotations offered them is apt to be very limited.

For all of these reasons, we believe that the passage of legislation compelling full disclosure of true interest charges, both in dollar amounts and in annual percentage rate will be a great boon to the poor and an important weapon in the arsenal of our current war on poverty.

Poverty is essentially measured by the gap between funds available and the cost of the basic necessities of life. By this measure excessive costs contribute just as surely to poverty as do inadequate income. Oftentimes for the poor it is the cost of credit which holds them below the poverty line as truly as joblessness or lack of income. Again we realize that this legislation does nothing in itself to reduce the cost of credit to the poor. It will, however, increase the awareness of that cost on the part of the poor; and by so doing the legislation may well have a secondary influence on the rates of interest charged to them where these have been excessive.

Both the administration and the Congress have committed this nation to a total war against poverty. That war is progressing with varying degree of success on many fronts. Failure to pass such legislation as that now under consideration by this committee will be to default on a vital sector of that total war.

We appreciate this opportunity to present our views to the Sub-committee.

MORTGAGE BANKERS ASSOCIATION OF AMERICA,
Washington, D.C., August 10, 1967.

Re H.R. 11601 and H.R. 11602.

Hon. LEONOR K. SULLIVAN,
House of Representatives,
Rayburn House Office Building,
Washington, D.C.

DEAR MRS. SULLIVAN: We appreciate this opportunity to present the views of our members on H.R. 11601 and H.R. 11602.

For many years, Mortgage Bankers have favored the full disclosure of finance charges in connection with real estate financing. In fact, the practice of making full disclosure has been so widely followed in this industry that the Senate in considering similar legislation felt justified in exempting first mortgage loans from the provisions of its bill.

As you know, closing statements are universally utilized in real estate transactions. They provide a complete dollars and cents disclosure of all charges, and the loan proceeds, for both buyer and seller. The mortgage instruments set forth the simple annual interest rate to apply on the outstanding principal amount of the loan.

In earlier hearings on Truth-in-Lending which were held by the Senate Committee, it was suggested that, despite the completeness of this information, there was still some lack of public understanding of the total costs of mortgage credit. As a result, the Federal Housing Administration asked that mortgagees originating FHA insured loans attempt to provide borrowers with additional information. Mortgage Bankers have cooperated wholeheartedly with this effort and continue to do so.

Perhaps it is worth noting that what this industry is doing in this regard goes beyond any reasonable definition of "disclosure". It constitutes a form of credit counseling which benefits borrower and lender alike. A real estate loan is a good investment only if it is sound, that is to say that it is well related to the value of the property and the borrowers ability to repay. Elaborate procedures to establish the appropriateness of these relationships have been established and are followed in every case. Where deficiencies in these relationships are noted, and cannot be corrected after consultation with the affected parties, credit is not extended.

It is in light of this background that we have considered the proposed legislation.

As we understand it, the objective of this legislation is to provide users of credit with an awareness of its costs so they can make informed judgments before they are committed. Although the Senate has concurred with our belief that we have for many years followed procedures which have achieved this objective, it may be the consensus of this Committee that misunderstandings continue to exist in the minds of mortgage borrowers that might be removed by an improvement in procedures. Real estate credit, however, is so different from other forms of consumer credit that the principal benefits of disclosure lie not in comparing the costs of real estate finance with those of revolving credit or personal loans, but in making comparisons among various real estate lenders.

Real estate loans customarily involve large sums of money. For the majority of people, the home or homes they may purchase involve the largest credit transactions they will experience. Despite the magnitude of the loans, real estate credit is widely extended to people of all income groups. The principal amounts often exceed twice the borrower's annual income. No other form of consumer credit involves such major sums for the borrower, bears such a high relationship of loan to income, or is utilized so infrequently by the average person. We are, therefore, talking about something unique when we discuss real estate finance.

It is almost inconceivable that anyone would make the choice between the purchase of a house and a small item such as a TV set on the basis of relative costs of credit. (We might add that if he did he would probably purchase a house.) If then it is the Committee's judgment that further disclosure of real estate finance charges are needed, we recommend that they be designed to facilitate the borrower's consideration of the relative costs of credit offered by (1) competing mortgage lenders; (2) those providing corollary services; (3) minimum and maximum downpayments; (4) minimum and maxium term; (5) various purchase arrangements, e.g., contract for deed or an FHA-insured mortgage purchase. It is our conviction that the only value of this legislation to the American public will be in further facilitating informed judgment on these five points, rather than in comparing costs of real estate credit, consumer credit, or revolving account credit.

If real estate first mortgage credit is to be covered by full disclosure legislation, we urge that it be covered by in a separate section of the law designed to achieve the above objectives. A suggested amendment to H.R. 11601 which would accomplish this is attached. However, we wish this committee to note that while we have expressed our willingness to make disclosure in accordance with the provisions of this amendment, we sincerely believe the provisions of H.R. 11602 are sufficient to protect borrowers against any abuses which may exist in the real estate credit field. Therefore, we support the enactment of H.R. 11602.

Sincerely,

JOHN A. GILLILAND, *President.*

AMENDMENT TO H.R. 11601

In Sec. 203, on page 13 after line 21, insert the following paragraph "(e)" and reletter those paragraphs following in this section.

(e) Any creditor agreeing to extend credit secured by an interest in real property shall furnish to the borrower to whom the credit is to be extended, prior to the consummation of the credit agreement, a clear statement in writing setting forth, to the extent applicable and ascertainable and in accordance with rules and regulations prescribed by the Board, the following information—

(1) the total price of the real property being purchased and of any personal property being purchased which is included in the agreement for the purchase of the real property;

(2) an itemized list, according to the following categories, showing in dollars and cents all of the charges (other than interest) to be paid by the borrower in connection with the transaction whether or not incident to the extension of credit:

(A) those charges fixed by law and not subject to the discretion of the lender (such as real estate tax escrows, real estate transfer taxes, and front footage assessments);

(B) those charges required by the lender to be made prior to the extension of credit which are imposed to safeguard the investment (such as credit reports, surveys, appraisals, deed preparation, and title searches), and loan origination fees not exceeding in amount those permitted by the Federal Housing Administration for comparable loans;

(C) those charges on which the borrower has some option as to placement or coverage (such as casualty insurance, title insurance, and customer credit life insurance), including a statement of the minimum amount of insurance, if any, required to be carried as a condition for the extension of credit; and

(D) all other charges of any nature paid by the borrower and not specified in subparagraph (A), (B), or (C);

(3) the sum of (1) and (2);

(4) the total amount to be financed;

(5) the cash required to be provided by the borrower (the difference between (3) and (4);)

(6) the annual percentage rate specified in the note or other instrument evidencing the indebtedness of the borrower, and the annual percentage rate represented by the total amount of the charges listed under (2)(D) (converted to an annual percentage rate under a formula prescribed by the Board), computed to the nearest ¼ of 1 percent;

(7) the monthly payments required to amortize principal and interest, plus any unusual payments to be required, or any contemplated changes in monthly payments anticipated by contracts for deeds or similar arrangements; and

(8) the penalties by percentage, or dollars and cents, for late payments or prepayments; or, in the case of variable interest rate loans, the conditions under which the rate may be changed and an estimate of the dollar difference in payments per ¼ percent difference in rate.

In prescribing rules and regulations to carry out the provisions of this subsection, the Board shall give recognition to the divergent practices of creditors engaged in the business of extending credit secured by interests in real property, but insofar as possible shall prescribe uniform procedures for complying with the provisions of this subsection.

INTERNATIONAL CONSUMER CREDIT ASSOCIATION,
St. Louis, Mo., August 18, 1967.

HON. LEONOR K. SULLIVAN,
Chairman, Subcommittee on Consumer Affairs of the Committee on Banking and Currency, Rayburn House Office Building, Washington, D.C.

DEAR MRS. SULLIVAN: Thank you very much for your recent letter inviting us to file a statement pertaining to H.R. 11601, the Consumer Protection Act.

At first I planned to prepare a statement pertaining to H.R. 11601. However, due to the fact that ICCA is not a "lobbying" association, on second thought I have decided to forego your invitation. Should you desire answers to any specific questions, I shall be pleased to attempt to answer them.

I do want to express my appreciation for the kindness shown to me during the two days I was able to spend at the hearings in Washington. Unfortunately, Mrs. Blake became quite ill during my absence and it became necessary for me to return to St. Louis. She got out of the hospital on Saturday of last week. She is feeling much better, but I have to watch her very carefully.

My best personal regards.

Sincerely yours,

WM. HENRY BLAKE,
Executive Vice President.

NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS,
August 25, 1967.

HON. LEONOR K. SULLIVAN,
Chairman, Subcommittee on Consumer Affairs,
House of Representatives Banking and Currency Committee,
House Office Building, Washington, D.C.

DEAR MRS. SULLIVAN: Prof. William J. Pierce, President of the National Conference of Commissioners on Uniform State Laws, has requested me to thank you for and reply to your letter to him of August 2.

President Pierce and the National Conference appreciate your invitation to testify on the above bill, but regret that circumstances preclude the acceptance of your invitation.

In accordance with your request, this Special Committee of the National Conference is pleased to file with you the enclosed statement on the above bill.

For a summary of the work of the National Conference and of the work and views of this Special Committee, I refer you to the statement of Prof. Pierce, beginning at page 282 of the transcript of the "Truth in Lending—1967" hearings before the Subcommittee on Financial Institutions of the Senate Committee on Banking and Currency.

The Second Tentative Draft of the proposed Uniform Consumer Credit Code was considered at the recent annual meeting of the National Conference. A copy of the draft appears in the transcript of the "Truth in Lending—1967" hearings beginning at page 717.

Whatever the views of the members of the National Conference, as State officials, on the appropriateness or desirability of federal legislation on disclosure in consumer credit transactions, the imminence of federal legislation makes desirable that we render whatever assistance we can in helping to make such legislation practicable and workable.

The enclosed statement suggests various revisions in H.R. 11601 to that end.

Permit me the following general observations if there is to be federal legislation on disclosure in consumer credit transactions:

1. The legislation should have, to avoid question, the broadest constitutional basis. We approve, therefore, of the invocation in H.R. 11601 of the constitutional powers of the Congress to regulate the value of money as well as to regulate commerce among the several States.

2. To serve their maximum useful purpose, disclosure requirements should be uniform as to all classes of consumer credit transactions. We approve, therefore, of the requirement in H.R. 11601 for equivalent annual percentage rate disclosure with respect to all open end credit transactions.

3. Also to serve their maximum useful purpose, disclosure requirements should apply to advertising of consumer credit rates and terms. We approve, therefore, of the theory, as distinguished from the substance, of the provisions in subsection (j) of SEC. 203 on pages 15–17 of H.R. 11601. On the other hand, we are concerned about the requirements of that subsection and recommend the revisions set forth in Item 14 of the enclosed statement as being less detailed, more clear and unequivocal, and requiring no administrative machinery for their enforcement.

4. Annual percentage rate disclosure requirements should apply to loans secured by a first mortgage or similar lien on real estate. Otherwise, it becomes meaningless to impose a requirement for inclusion in the finance charge of "any amount payable under a point, discount, or other system of additional charges" as in SEC. 202.(d) of H.R. 11601 [at p. 5, Lines 2–3], in SEC. 3.(d)(1) of S. 5 (Report No. 392) [at p. 13, Lines 10–11], and in SEC. 3(d)(1) of H.R. 11602 [at p. 3, Lines 11–12]. We approve, therefore, the provisions of H.R. 11601 requiring annual percentage rate disclosure as to mortgage loans.

5. Dollar, but not rate, disclosure of closing costs of loans secured by a mortgage or similar lien on real estate should be required. See Item 5 of the enclosed statement.

6. The effective date of the legislation should be postponed at least until July 1, 1969, except for the provision granting authority to the Board of Governors of the Federal Reserve System to adopt implementing regulations, which should be made effective upon enactment, to conform to S. 5 (Report No. 392) and H.R. 11602. In addition, the Board should be given power to postpone the effective date of the legislation for a 12-month period to encourage the States to enact comprehensive consumer credit legislation. In this connection, it should be noted that:

a. enactment of federal disclosure legislation will require a complete review and revision by the States of their existing consumer credit legislation, preferably along the lines of the proposed Uniform Consumer Credit Code to be promulgated by the National Conference of Commissioners on Uniform State Laws;

b. The National Conference will be unable to complete the final draft of its proposed Uniform Consumer Credit Code prior to mid-1968 for presentation to State Legislatures in their 1969 sessions; and

c. the Legislatures of some States do not have sessions, with plenary authority, meeting in 1969; to enable and encourage the Legislatures of those States to enact the proposed Uniform Consumer Credit Code, either the Board should have power to postpone the effective date of the legislation until July 1, 1970, or preferably, the effective date of the legislation should be July 1, 1970.

Considerations of time have precluded the submission of this letter and the accompanying statement to the members of the National Conference of Commissioners on Uniform State Laws or of this Special Committee for their approval. Consequently, this letter and the accompanying statement must be regarded as an expression of my personal views, although I believe that the views expressed will meet with the approval of the members of this Special Committee.

I shall be happy, if you wish, to meet with you or the staff of the Subcommittee on Consumer Affairs and the Committee on Banking and Currency to discuss further the contents of this letter and the accompanying statement.

We appreciate your request to comment on the above bill.

Very truly yours,

ALFRED A. BUERGER,
Chairman.

RECOMMENDED REVISIONS OF H.R. 11601

The following recommended revision of H.R. 11601 are submitted subject to the accompanying letter of transmittal, dated August 25, 1967, to Hon. Leonor K. Sullivan, Chairman of the Subcommittee on Consumer Affairs of the House of Representatives Committee on Banking and Currency.

The recommended revisions are divided into two classes, I and II. The Special Committee believes that the recommended revisions in each class are equally necessary and desirable, but has included in Class II revisions which might prove controversial and hence might delay enactment of a "Truth in Lending Act" or a "Consumer Credit Protection Act."

The supplementary comments following the recommended revisions further explain and elaborate upon the purposes and reasons for some of the revisions.

I

Item 1

Page I—Title of Bill—Delete all after "A BILL" and insert: "To assist in promoting the stabilization of the economy and of the value of money by requiring disclosure of finance charges in connection with extensions of credit and advertisements therefor."

Purpose of Revision: 1. To conform title of bill to title of S. 5 and H.R. 11602; 2. to add reference to "stabilization of the value of money" so as to invoke the constitutional powers of the Congress to regulate the value of money; and 3. to eliminate references to provisions of H.R. 11601 proposed to be deleted.

Item 2

Page 3, Lines 14–19—Sec. 201(b)—Delete in their entirety.

Purpose of Revision: 1. To eliminate references to finding relating to provisions of H.R. 11601 proposed to be deleted.

Item 3

Page 4, Lines 11–12—Sec. 202.(c)—Revise to read: "chased primarily for personal, family, household, or agricultural purposes. The term does not include any contract in".

Purpose of Revision: To conform phraseology to that in SEC. 202.(b) at p. 4, Lines 2–3.

Item 4

Page 5, Line 12—Sec. 202.(d)(1)—Revise to read:

"(B) taxes; or

"(C) charges or premiums for insurance against loss or damage to property related to a credit transaction or against liability arising out of the ownership or use of such property; or

"(D) charges or premiums for credit life and accident and health insurance; and".

Purpose of Revision: To conform to SEC. 3.(d)(2) of S. 5 and H.R. 11602, at p. 13, Lines 18–22 of S. 5 [Report No. 392], and p. 3, Lines 19–23 of H.R. 11602

Item 5

Page 5, Lines 13–17—Sec. 202.(d)(2)—Revise to read:

"(2) if itemized and disclosed under section 203, and if the credit is secured in whole or in part by an interest in real property, the term 'finance charge' does not include amounts collected by a creditor, or included in the credit, for, in addition to the duly itemized and disclosed costs referred to in clauses (A), (B), (C), and (D) of paragraph (1), the costs of".

Purpose of Revision: 1. To require the disclosure of the dollar amount of closing costs on extensions of credit secured by an interest in real property; and 2. to conform to the revisions proposed in Item 4, above.

Item 6

Page 8, Lines 3–17—Sec. 202.(i)—Delete in their entirety and insert:

"(i)(1) 'advertisement' includes any publication, printed matter, display, broadcast, solicitation, or representation for the purpose or having the effect of promoting or inducing, directly or indirectly, any extension of credit, consumer credit sale or open end credit plan.

"(2) 'an advertisement containing specific credit terms' means any advertisement which states any of the following:

"(A) a rate or rates of finance charge;

"(B) the amount of finance charge; or

"(C) the amount of any installment or installments."

Purpose of Revision: 1. To broaden the definition of advertisement so as not to limit it to 'an advertisement in interstate commerce or affecting interstate commerce' by taking advantage of the invocation of the currency powers of the Congress in SEC. 201.(a); and 2. to define more clearly what is prohibited so that only criminal sanctions will be required for enforcement.

Item 7

Page 9, Lines 19–20—Sec. 203.(b)(7)—Revise to read:

"(7) the finance charge expressed as an annual percentage rate, if the amount of such charge is $10.00 or more;".

Purpose of Revision: To conform to SEC. 4(b)(7) of S. 5 and H.R. 11602, at p 17, Lines 22–24 of S. 5 [Report No. 392], and p. 7, Lines 23–24 of H.R. 11602.

Item 8

Page 10, Line 25—Sec. 203.(c)(4)—Revise to read:

"(4) the amount of the finance charge, unless the loan or other extension of credit is secured by a first mortgage or other first lien such as is commonly given to secure advances on, or the unpaid purchase price of, real estate under the laws of the State in which the real estate is located;".

Purpose of Revision: To eliminate as unnecessary the requirement for disclosure of the total dollar amount of interest charges on first mortgage loans for personal, family, household, or agricultural purposes.

Item 9

Page 11, Lines 1-2—Sec. 203.(c)(5)—Revise to read:

"(5) the finance charge expressed as an annual percentage rate, if the amount of such charge is $10.00 or more;".

Purpose of Revision: To conform to SEC. 4.(c)(5) of S. 5 and H.R. 11602, at p. 19, Lines 6-8 of S. 5 [Report No. 392], and p. 9, Lines 6-8, of H.R. 11602.

Item 10

Page 12, Lines 6-11—Sec. 203.(d)(2)(C)—Revise to read:

"(C) the method of determining the amount of the finance charge, any minimum or fixed amount to be imposed as a finance charge, and, if other than a minimum or fixed charge, the percentage rate or rates per period to be used in computing the finance charge to be imposed and the amount of balance to which each such periodic percentage rate applies, and the equivalent annual percentage rate of each such periodic percentage rate; and".

Purpose of Revision: 1. To eliminate the erroneous reference to "installment open ed credit plan"; 2. to make clear that a minimum or fixed amount of finance charge need not be expressed as a percentage rate; 3. to permit the disclosure of more than one percentage rate per period to be applied to specified balances (as, for example, in New York, 1½% per month on the first $500. of balance and 1% per month on the excess of balance over $500.); and 4. to require equivalent annual percentage rates to be disclosed as to all open end credit plan accounts.

Item 11

Page 13, Lines 1-10, Sec. 203. (d)(3)(D)(E) and (F)—Revise to read:

"(D) the amount of any finance charge added to the account during the period due to the application of a percentage rate or rates, if any, and the amount of any finance charge added to the account during the period imposed as a minimum or fixed charge;

"(E) the balance on which the finance charge was computed and a statement of how the balance was determined;

"(F) if an amount was added to the account during the period due to the application of a percentage rate or rates, the percentage rate or rates per period used in computing the finance charge and the amount of balance to which each such percentage rate applied, and the equivalent annual percentage rate of each such periodic percentage rate;".

Purpose of Revisions:

As to clause (D): 1. To require, as do SEC. 203.(d)(3)(D) of H.R. 11601 and SEC. 4.(d)(3)(D) of S. 5 and H.R. 11602, separate disclosures of the amounts of finance charge added a. due to application of a percentage rate, and b. as a minimum or fixed charge, but to avoid any implication of a requirement for disclosure of the total of the charges so added because such a requirement cannot be met by computers now in general use; and 2. where step rates are used depending on the amount of balance (as, for example, in New York, where ceiling rates are 1½% per month on the first $500. of balance, and 1% per month on the excess of balance over $500.), to require disclosure of both periodic percentage rates and the dollar amounts of balances to which they apply.

As to clause (E): To reletter clause (F) of SEC. 203.(d)(3) of H.R. 11601 to conform to clause (E) of SEC. 4.(d)(3) of S. 5 and H.R. 11602.

As to clause (F): 1. To make clear that a minimum or fixed amount of finance charge need not be expressed as a percentage rate; 2. to permit the disclosure of more than one percentage rate per period to be applied to specified balances (as, for example, in New York, 1½% per month on the first $500. of balance and 1% per month on the excess of balance over $500.); and 3. to require equivalent annual percentage rates to be disclosed as to *all* open end credit plan accounts.

Item 12

Page 15, Lines 3-7—Sec. 230.(i)(1)—Revise to read:

"(1) (1) Prior to January 1, 1972, whenever an annual percentage rate is required to be disclosed by this section, the rate may be expressed either as an annual percentage rate, or as a dollars per hundred per year rate of the average unpaid balance."

Item 13

Page 15, Lines 8–9—Sec. 230.(i) (2)—Revise to read:

"(2) After December 31, 1971, all rates required to be disclosed by this section shall be expressed as percentage rates."

Purpose of Revisions (Items 12 and 13): To conform to SEC.(i)(2) of S. 5. and H.R. 11602, at p. 23, Line 24 of S. 5 [Report No. 392], and p. 14, Line 4 of H.R. 11602.

Item 14

Page 15, Lines 10–25; Page 16, Lines 1–24; Page 17, Lines 1–3—Sec. 203. (j) and (k)—Delete in their entirety and insert:

"(j)(1) No person in an advertisement containing specific credit terms shall state—

"(A) a rate or rates of finance charge unless expressed in terms of an annual percentage rate or equivalent annual percentage rate; or

"(B) the amount of any finance charge, which is not a minimum or fixed amount imposed as a finance charge under an open end credit plan, or, otherwise, $10.00 or more, unless the annual percentage rate or equivalent annual percentage rate is also stated; or

"(C) the amount of any installment payment unless the number, amount, and due dates or periods, and the total amount of installment and other payments are also stated;

"(2) No person shall state in an advertisement—

"(A) that specified amounts of credit or specified installment payment terms can be arranged, unless he usually and customarily extends credit in such amounts or upon such payment terms.

"(B) that, in a consumer credit sale, no down payment is or will be required, unless he usually and customarily requires no part payment of the price; or

"(C) that, in a consumer credit sale, a down payment no larger than a specified amount is required, unless he usually and customarily requires down payments no larger than the amount specified.

"(3) This subsection does not apply to any television or sound broadcasting station or to any publisher or printer of a newspaper, magazine, or other form of printed advertising, who broadcasts, publishes or prints an advertisement."

Purpose of Revision: 1. To state clear and precise rules as to advertising which can be enforced by criminal sanctions only; 2. not to require so much disclosure in advertisements that the disclosure of the annual percentage rate or equivalent annual percentage rate will be lost in a maze of fine print and escape the attention of the reader or watcher; 3. in (j)(1)(C) to prohibit "a dollar down and a dollar a week" advertising, without disclosing the number of weeks and the total amount of installments; and 4. in (j)(3), to make the subsection inapplicable to printers, publishers and broadcasters who past experience shows will strenuously oppose any legislation which places upon them the burden of policing the content of advertisements.

Item 15

Page 17, Lines 4–13—Sec. 203.(l) and (m)—Delete in their entirety.

Purpose of Revision: 1. To delete from the bill provisions for ceilings on finance charges and prohibitions against confession of judgment provisions which many consider unwise and unconstitutional and which at the very least are highly controversial. Many of our consumers are not eligible for sales or loan credit at 18% per annum. Confession of judgment provisions in debt obligations must be considered in the light of the entire package of creditors' remedies and debtors' rights in a particular jurisdiction.

Item 16

Page 17, Line 14—Sec. 203.(n)—Revise to read:

"(k) The provisions of this section shall not apply to".

Purpose of Revision: To reletter this subsection to reflect the omission of subsections (k), (l) and (m).

Item 17

Page 20—Sec. 204.(e)—Revise Line 13 to read: "to advise and consult with it in the exercise of its functions".

Purpose of Revision: To correct typographical error.

Item 18

Page 21—Sec. 205.(b)—Revise Lines 16–20 to read:

"(b) The Board shall by regulation exempt from the requirements of this title any class of credit transactions which it determines are subject to any State law or regulation which requires disclosures substantially similar to those required by section 203, and contains adequate provisions for enforcement."

Purpose of Revision: To comform to Sec. 6.(b) of S. 5 and H.R. 11602, at p. 27, Lines 16–21, of S. 5 [Report No. 392], and p. 17, Lines 21–24 and p. 18, Lines 1–2 of H.R. 11602. The formulation of SEC. 6.(b) is considered preferable.

Item 19

Page 22—Sec. 206.(a)(1)—Revise Line 4 to read: "any provision, except subsection (j), of section 203, or any regulation issued thereunder, to disclose".

Purpose of Revision: To avoid application of civil penalties to violations of subsection (j), relating to advertising. Otherwise, conceivably, anyone who reads a newspaper or magazine or listens to or sees a radio or television broadcast containing a noncomplying advertisement might have the right to recover the prescribed civil penalty of $100 plus attorneys' fees. Moreover, a subsequent disclosure to a buyer or borrower otherwise fully complying with the title might not negate his possible right to recover the civil penalty based on a nondisclosure in an advertisement.

Item 20

Page 22—Sec. 206.(a)(2)—Revise Line 13 to read: "amount less than that required to be disclosed by any provision, except subsection (j), of section 203".

Item 21

Page 24, Lines 6–25, Pages 25–33, Page 33, Lines 1–3—Sec. 207., Sec. 208. and Sec. 209.—Delete in their entirety.

Purpose of Revision: To avoid further controversy and delay in the enactment of a "Truth in Lending Act" or a "Consumer Credit Protection Act".

Item 22

Page 33, Line 5—Sec. 210.—Renumber as SEC. 207.

Purpose of Revision: To reflect omission of SEC. 207., SEC. 208., and SEC. 209.

Item 23

Page 33, Lines 17–18—Sec. 211.—Revise to read:

"SEC. 208. The provisions of this title shall take effect on July 1, 1969, *Provided*, That the Board may by regulation postpone the effective data of this title for an additional twelve-month period on the basis of a finding that such a postponement is required to enable one or more States to enact a comprehensive revision and modernization of its laws for the regulation of consumer credit, including provisions requiring disclosures as to credit transactions substantially similar to those required by section 203 of this title and containing adequate provisions for enforcement, to take effect on or prior to the effective date of this title, and *Further Provided*, That section 204 of this title shall take effect immediately upon enactment."

Purpose of Revision: 1. To conform the effective date of the title to the effective date of S. 5 and H.R. 11602; 2. to make the powers of the Board to adopt implementing regulations effective immediately; and 3, to enable the Board to postpone the effective date of the title by twelve months and thereby to encourage those States, which do not have annual sessions of their Legislatures with plenary authority, to enact a comprehensive revision and modernization of its laws for the regulation of consumer credit. [*Note:* The Uniform Consumer Credit Code, proposed by the National Conference of Commissioners on Uniform State Laws, will not be ready for introduction in State Legislatures until Legislative sessions beginning in 1969.]

Item 24

Page 33, Lines 19–25; Pages 34–41—Delete in their entirety.

Purpose of Revision: To avoid further controversy and delay in the enactment of a "Truth in Lending Act" or a "Consumer Credit Protection Act."

II

Item 25

In lieu of Items 7 and 9:

Page 9, Lines 19–20—Sec. 203. (b) (7)—Revise to read:

"(7) the finance charge expressed as an annual percentage rate, if the amount of such charge is $25.00 or more;".

Page 11, Lines 1–2—Sec. 203. (c) (5)—Revise to read:

"(5) the finance charge expressed as an annual percentage rate, if the amount of such charge is $25.00 or more;".

In lieu of subsection (j) (1) (B) of Sec. 203. as proposed in Item 14:

"(B) the amount of any finance charge, which is not a minimum or fixed amount imposed as a finance charge under an open end credit plan, or, otherwise, $25.00 or more, unless the annual percentage rate or equivalent annual percentage rate is also stated; or".

Purpose of Revisions: To increase from $10 to $25 the amount of finance charge which need not be disclosed as an annual percentage rate. It is believed that the reasons for exempting from an annual percentage rate disclosure requirement of a finance charge of $10 or more apply equally to a finance charge of $25 or more.

SUPPLEMENTARY COMMENTS

RE ITEM 4

Item 4 proposes to amend SEC. 302. (d) (1) to exclude from the definition of "finance charge" charges or premiums for insurance against loss or damage to property related to a credit transaction or against liability arising out of the ownership or use of such property and charges or premiums for credit life and accident and health insurance, to conform to SEC. 3. (d) (2) of S. 5 and H.R. 11602.

The following excerpts from the transcript [hereinafter called "S. 5 Transcript"] of the hearings on "Truth in Lending—1967" before the Subcommittee on Financial Institutions of the Senate Committee on Banking and Currency relate to this proposal:

EXCERPTS FROM STATEMENT OF WILLIAM J. PIERCE, PRESIDENT OF NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS, AT PAGE 285

"5. The amount of credit service or finance charge to be included in the base for computing a uniform time rate to be disclosed should comprise only items like 'pure interest,' compensation for the creditor's risk of not being paid, and service charges for the credit extension and should not include other charges not directly related to these items.

"The credit service or finance charge should not include such items as governmental fees and taxes and insurance which is of benefit to the debtor. These, of course, must be carefully defined and limited in order to prevent possible overreaching. Their itemized disclosure, both as to nature and dollar cost involved, should be required. It is the opinion of the committee at this time that inclusion of charges not attributable to the cost of the credit in the credit service or finance charge would make a time rate comparison meaningless.

"For example, if these items are included in the credit service or finance charge, two auto dealers quoting the same total charges would be required to quote the same time rate although one dealer's total charges include insurance and the other dealer's only the credit service or finance charge."

EXCERPTS FROM STATEMENT OF HON. J. L. ROBERTSON, VICE CHAIRMAN OF THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, AT PAGE 665

"EXCLUSION FROM FINANCE CHARGE OF INSURANCE PREMIUMS, TAXES, AND OFFICIAL FEES

"One of the issues that has proved troublesome during these hearings has been the question of how to treat insurance premiums on policies taken out by borrowers as a condition of, and covering the amount of, the credit contract. * * *

"The fact remains, however, that any insurance provides a benefit to the borrower over and above the use of credit. To require that the finance charge

include insurance premiums would overstate the actual charge for credit. Therefore, we think that the cost of any kind of insurance is not properly regarded as part of the finance charge, and should be specifically excluded in S. 5. Similarly, we feel that the statute should specifically exclude official fees and taxes from the finance chrage, since generally they benefit neither creditor nor borrower, are not within their control, and are the same regardless of the source and terms of the credit. Both types of charge should be required to be itemized among the nonfinance charges that must be disclosed pursuant to section 4(a)(4)."

RE ITEMS 6 AND 14

Item 6 proposes to define "advertisement" and "an advertisement containing specific credit terms"; Item 14 proposes to impose requiremnets for advertisements. These provisions follow generally the provisions relating to advertising in Sections 2.303. and 3.303. of the Second Tentative Draft of the proposed Uniform Consumer Credit Code, appearing at pp. 731 and 745 of the S. 5 Transcript.

RE ITEMS 7 AND 9, AND PROPOSED SUBSECTIONS (J)(1)(B) OF SEC. 203. IN ITEM 14

These Items propose to eliminate requirements for the expression of the finance charge as an annual percentage rate and for any similar disclosure in an advertisement, if the amount of the finance charge is $10 or more.

The following excerpts from the S. 5 Transcript relate to these Items:

EXCERPTS FROM STATEMENT OF WILLIAM J. PIERCE, PRESIDENT OF NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS, AT PAGES 285–286:

"6. Where the amount involved in the credit transaction is relatively small and has a short maturity, time rate disclosure is meaningless and only dollar disclosure should be required. For example, consider the sale of a $60 vacuum cleaner with a minimum $10 credit service charge and a total time price of $70 payable in 8 monthly installments of $8.75 each. To be told that the credit service charge is at the rate of $25 per hundred of principal per year or 42.6 percent per year does not help the customer in making a value judgment."

STATEMENT OF HON. J. R. ROBERTSON, VICE CHAIRMAN OF THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, AT PAGES 663 AND 664:

"EXEMPTION OF SMALL CREDITS AND CHARGES

"I am sure that none of us wants to press disclosure of credit costs to the point where borrowers are denied access to credit at any price. But there is one area where disclosure of an annual percentage rate might do just that. In a closed end credit transaction involving a small amount, a high effective rate may be justified to compensate the creditor for the relatively high out-of-pocket costs of handling the transaction. However, he may be understandably reluctant to disclose the very high rate—perhaps 50 or 100 percent—and might decide instead simply to discontinue this type of credit transaction.

"For some borrowers, unable to obtain open-end credit accommodation or not having access to small cash loans, the need to make relatively small purchases on credit may be great indeed. It may also be argued that a small finance charge—in dollar amount—is not of great significance to the credit user regardless of the effective rate of finance charge. Therefore, we would be disposed to see closed-end credit transactions involving a small amount—perhaps under $100—and a small total finance charge—perhaps under $10—exempted from the disclosure requirements. But we think Congress should make the decision and, if it agrees, should incorporate the specific exemption in S. 5."

RE ITEM 23

Item 23 proposes to renumber SEC. 211. as SEC. 208. and to revise it to provide July 1, 1969 as the effective date of the legislation, and to grant authority to the Board of Governors of the Federal Reserve System to postpone the effective date to July 1, 1970.

The enactment of the legislation by the Congress will provide a tremendous impetus to the revision and modernization by the States of their consumer credit laws.

The National Conference of Commissioners on Uniform State Laws believes that its proposed Uniform Consumer Credit Code will provide the best vehicle for such a revision and modernization.

The scope of the proposed Code and the protection it will give consumers are indicated by the Second Tentative Draft which appears in the transcript of the "Truth in Lending—1967" hearings of the Subcommittee on Financial Institutions of the Senate Committee on Banking and Currency, beginning at page 717.

The proposed Code will not be completed until August 1968 nor ready for introduction in State Legislatures until their sessions in 1969.

Unfortunately, not all State Legislatures meet in plenary sessions in 1969; some will not meet in such sessions until 1970.

Consequently, to encourage maximum State enactment of the proposed Uniform Consumer Credit Code, either the effective date of federal legislation to require consumer credit disclosure should be postponed until July 1, 1970, or the Board of Governors of the Federal Reserve System should be given authority to postpone the effective date until that date.

RE ITEM 25

We strongly recommend that the exemption from annual percentage rate disclosure requirements be increased from $10.00, as in S. 5 and H.R. 11602, to $25.00. When smaller amounts are involved, an annual percentage rate becomes meaningless and more confusing than helpful to the consumer. The discussions of the Second Tentative Draft of the proposed Uniform Consumer Credit Code in the Committee of the Whole of the National Conference of Commissioners on Uniform State Laws support this recommendation.

STATEMENT OF PAUL J. KREBS, EXECUTIVE DIRECTOR, OFFICE OF CONSUMER PROTECTION, DEPARTMENT OF LAW AND PUBLIC SAFETY, STATE OF NEW JERSEY

Madam Chairman and members of the subcommittee, I am grateful for this opportunity to submit a statement attesting to the excellent beginning made by this Consumer Credit Protection Act in affording some measure of relief to the consumers from the predatory practices that have been common in the consumer credit field. I have deliberately chosen the word beginning because I feel this measure, however excellent, is just that—the first step on a long road to careful and considered consumer protection. I have every confidence that, given this good beginning, the Congress of these United States can take all of the steps that are necessary to make credit a useful tool of both the consumer and the business economy.

I believe the need for truth in lending legislation has been attested to by the statements of hundreds of qualified men and women who have appeared before your Subcommittee. I will not belabor this point because I believe it has been very well documented that the need for such legislation cannot be overestimated. I believe that most ethical business concerns have recognized the need for this legislation as a self-protective device. There are only so many dollars in the economy. Every dollar that is siphoned off by unethical credit merchants is a dollar lost to legitimate and ethical financing institutions. Moreover, those who have strived to remain ethical must recognize this measure as a means toward ending the unfair competition which they face from less ethical financiers. Businessmen would be secure in the knowledge that higher cost competitors cannot lure away their customers with deceptive credit information.

I should like to devote the bulk of my statement to pointing out the strengths and weaknesses of H.R. 11601 and suggesting how further legislation or amendment to the present bill can afford truly effective protection to the consumer.

DISCLOSURE PROVISIONS

The provisions of H.R. 11601 which cover the disclosure in writing of all possible charges, expressed both in dollar amounts and annual percentages, of consumer credit sales, extensions of credit and open end credit plans are com-

prehensive and show a fine understanding of the problems attendant to each of the three separate forms of financing. The inclusion of open end credit plans, a form of credit which is becoming prevalent in our economy, is probably the most significant step taken by this measure. Moreover, the inclusion of "service and carrying charges" in the definition of 'finance charge' should insure that no form of charge account plan can escape regulation under this act. The open end credit plan is one of the most unregulated forms of credit common to today's marketplace. Under no circumstances should it be deleted from this bill, or lost during conference with the Senate.

CREDIT RATE CEILING

The sponsors of this Act show great courage and understanding of the consumer credit field in limiting any finance charge to 18 per centum per annum. This is a fair rate for small loan companies whose risk is high. Even greater courage would have been demonstrated, however, if the maximum for open end credit plans was fixed at 12% and if the maximum for consumer credit sales was fixed at 8%. The same fine understanding of the three forms of credit that is displayed in those provisions regulating disclosure of finance charges has, unfortunately, been lost by the imposition of a single, inflexible national ceiling on all interest rates.

WAGE GARNISHMENTS

I can not be too strong in my support for the provision which abolishes wage garnishments. The practice of garnishment is the only remaining vestige of the archaic system that began with debtor's prisons. Legitimate businesses have long ago learned how to collect funds without relying on garnishment. The device of garnishing wages has fed the growth of unscrupulous merchants. They readily extend credit to workers who are obviously already over-extended only because they know they have a guaranteed method for collection.

REGULATION OF ADVERTISEMENTS

So far, I have addressed myself, in the main, to the strengths of this measure. As I see it, there are three major shortcomings as the bill is presently written. I would urge that serious consideration be given to amending provision (D) of Section 203 (j) (1) so that time sale differential is substituted for time sale price. If this Act is to insure "that the consumer will be able to compare more readily the various credit terms available to him," then the advertisement of finance charges is perhaps even more important than is disclosure at the time of the sale. The disclosure and advertisement of time sale differential means that the consumer is advised of the exact dollars and cents cost of the finance charge. Time sale price is a total of the cash sale price plus the finance charge and can be misleading. This error should be corrected as soon as possible.

SUBSTITUTE LANGUAGE

The second shortcoming of this bill is contained in Section 202: (4) (f) on Page 14, lines 10 through 13. This Section allows the creditor to word his disclosure of rates in any language he so desires, as long as it "conveys substantially the same meaning." Who is to determine whether or not his substitute language does indeed convey substantially the same meaning? Is he the one to decide or is the consumer? Consumers today are confused enough without letting every businessman decide on his own terminology for basically the same technical credit transaction. Every business should have to use the exact same terminology as any other business in disclosing or advertising credit rates, fees, etc.

Let me give you an example of how consumers can be confused by technical terminology. Usually, when a used car is being sold in the same condition as it was in when originally bought by the used car dealer the contract is marked with the words "as is." Recently we had a complaint in our office where such an automobile was sold with the contract marked "as traded." The dealer insists that "as traded" conveys the same meaning as does the words "as is." Our question is, conveys to whom? He may have understood what he meant, but it was pretty obvious that the purchaser had no idea what these words means. There should be no objection to requiring that all technical terminology be standardized. I strongly urge that lines 10 through 13 on Page 4 be eliminated.

ADMINISTRATION

The third shortcoming of this bill concerns the provisions for administration and is, if possible, even more important. What good is a law if the agency chosen to administer it has neither the staff nor the consumer experience necessary for fair and efficient enforcement. As this bill is presently constituted, a consumer can obtain the allowed civil penalties only by hiring an attorney and filing suit in a United States District Court. The Board of Governors of the Federal Reserve System can issue regulations and can serve orders requiring persons not to engage in the violation, but they have no authority to prosecute for criminal penalties. Criminal penalties are enforced by the Attorney General.

Would it not be far simpler and much more effective for Congress to establish a national Office of Consumer Protection within the Department of Justice? The staff of this office would be devoted not to banking interests but to consumer interests and consumer interests alone. They would have the expertise in consumer credit needed for fair and efficient administration and all of the criminal and civil penalties could be enforced by one agency. I am not suggesting that the civil jurisprudence system be abolished, but I'm suggesting that this office have the authority to file civil suit on behalf of indigent complainants.

The effects of administration by one agency are readily apparent. There would be no mounds of infamous Washington red tape for the average consumer to be bogged down in. There would be created an effective one-stop agency to which the consumer could go with his credit problems. If this measure is totally intended to aid and protect the consumer, then the present provisions for administration must be changed.

FUTURE LEGISLATION

I began this statement by calling the Consumer Credit Protection Act a beginning. Let me now enumerate a few of the many other steps which it is necessary to take before credit can truly be a useful tool for the consumer.

Computation of interest rates

It has been our experience in the New Jersey Office of Consumer Protection that even where the consumer knew full well the annual interest rate and dollars and cents cost of his loan, he experienced great difficulty in checking the accuracy of the monthly calculations made by the finance company for each payment. Let me illustrate this problem. Recently a new small loan act went into effect in the State of New Jersey. It requires disclosure of interest stated in annual terms and dollars and cents. A member of my staff, who is expert in such calculations, put herself in the position of a consumer who goes to one of the finance companies covered by this new act and borrows $1000 for two years. The manager of the company informs her that the interest rate is calculated monthly and that the total unpaid balance can be paid at any time. Monthly payments are quoted at a figure of $52.57 without creditor life insurance. As an average consumer, she would like to know whether this is the proper monthly payment so she sits down and attempts to compute it herself. After six hours of work with the computer she was still $17.24 in error. I ask you, gentlemen, if any of you, educated and intelligent men, could compute the accuracy of the quoted monthly payment? If you can not and if my staff member could not, how do we expect the average consumer to be able to do so. H.R. 11601 provides that the United States rule of actuarial method be used to calculate the normal annual rate. It is my contention that in order to ensure that the borrower not be cheated when his payments are calculated, that he be given a copy of this actuarial computation at the time his loan is transacted.

I can not emphasize how important these calculations are. The majority of complaints handled by our Office of Consumer Protection against finance companies concern the computation of interest and clearly reveal that almost no consumer could make such calculations himself.

Holders in due course

A major problem faced by consumers in credit transaction comes because of the lack of legislation regulating holders in due course. A holder in due course is a third party to a transaction who handles nothing but the financing of an installment contract.

Let us assume that I, as a consumer, contract for home improvements to my house. Mr. Smith, the contractor and I enter into a credit agreement. Unknown to me, Mr. Smith thereupon turns around and discounts this installment con-

tract to a third party, a licensed financing institution. Mr. Smith gives me a warranty on construction materials and workmanship for three years.

A year and a half later, Mr. Smith has gone out of business and I have holes in my roof. Since I can no longer contact Mr. Smith but I am still making payments to the financing institution, I go to them and seek remedy. The man at the financing institution tells me he is very sorry but handles only the financing and if the workmanship and materials have not performed as promised, there is absolutely nothing he can or will do. I still owe $2100 for work under warranty which no one will repair fore me.

This situation is the most common complaint we face in the New Jersey Office of Consumer Protection. It is my strong belief that if a financing institution is going to make a profit—and they do—out of a transaction, then they should also share the responsibility for that transaction. If such a regulation were in force, we would soon find financing institutions making the same requirements for discounting installment contracts as they now do for personal loans and mortgages. Since they now have absolutely no responsibility for the work performed by the contractor, they buy paper from anyone who has paper to sell. It is a shameful practice which is common among the most respected, upstanding and ethical financing institutions in our country.

I strongly recommend Federal Legislation that will abolish the holder in due course and make the financing institution as responsible as the contractor for the work done.

Seven year installment contracts

While I am on the subject of home improvements, let me also suggest that a national ceiling should be placed on the number of years in which an installment contract can be financed. It is presently common practice in New Jersey and many other states, for home improvement installment contracts to run as long as 7 years. Let's consider for a moment what effect these 7 year contracts have upon the consumer. In the first place, many would never have entered into the contract in the first place if they had understood how much money it would cost them over a seven year period. Mr. Smith is approached by Mr. Jones, a home improvement contractor. Mr. Jones suggests that what Mr. Smith really needs is a finished basement in his house, at a cost of $4000. Mr. Smith protests that he can not afford such a construction job. Mr. Jones claims that he can. After all, the payments would only be $70 a month. Using high pressure tactics, Mr. Jones manages to convince Mr. Smith that he can afford to make such improvements to his home. Only after a completely binding and legal contract is signed, does Mr. Smith realize that he is indebted for 7 years at 7% per annum—or total interest cost of 49%. It will cost him $1960 to finance this home improvement job worth $4000. If the 7 year contract were not available to him, I am sure Mr. Smith would never have gotten himself so deeply in debt.

Let us now take a look at Mr. Smith five years later. He was given a 48 month warranty on all construction materials and workmanship. The warranty is now expired and now the finished basement needs more work. He still has two years to go, or a total of better than $1700 to pay on the original job. But the original job is no longer good enough.

I strongly believe that if a man can not afford to pay for work done to his home in 5 years or less, then the work should not be done. I urge that Federal legislation be enacted placing a national ceiling of five years on the length of any installment contract or personal loan.

Indentures

In many cases finance institutions require dealers to obtain signatures of consumers to second mortgages on their homes as security for a loan or installment contract. The title of this piece of paper which they sign is "Indenture." Few consumers know the significance of this document and most are not apprised of the fact that it is actually a second mortgage on their home. I strongly suggest that legislation be enacted to require all mortgages be entitled "mortgage."

Madam Chairman, I want to thank you for the opportunity of submitting testimony expressing my views on H.R. 11601 and future needs. I am sure that Congress will pass this Bill and will soon recognize the need for the other legislation recommendations which I have made. The citizens of New Jersey are extremely gratified with the efforts of you and your committee to enact long overdue reforms in the field of consumer credit.

Thank you very much.

STATEMENT OF THE AMERICAN INDUSTRIAL BANKERS ASSOCIATION

The American Industrial Bankers Association is a national trade organization of sales finance companies, industrial loan companies and small loan companies. We have approximately 425 member companies with some 8,500 offices. Some of our members only have one office, some have several hundreds.

The sales finance companies primarily buy documents involving credit transactions (paper) from dealers. The industrial loan and Morris Plan companies make direct loans in larger amounts to the consumer; they also (where permitted by state law) issue certificates of investment or indebtedness to those wishing to invest in their operations. The small loan companies make direct loans to the consumer, but usually on a smaller scale than do the industrials.

The total dollar outstandings of the companies and individuals who are members of AIBA currently average about 20 billion dollars a year. In other words, the members of our association are engaged in the consumer credit business and any legislation dealing with consumer credit will have a direct effect on the business of our member companies.

In presenting this written statement with regard to H.R. 11601 and other related bills, we want to make it clear from the outset that the American Industrial Bankers Association strongly favors the full disclosure of the terms of all consumer credit transactions. Moreover, we feel that such full disclosure should be in language that consumers can easily understand. Finally, full disclosure should be made in a manner that is not at variance with the normal practices with respect to the particular kind of transaction involved.

In our Senate testimony on S.5, we have already expressed our views with respect to the preferability of State action, rather than Federal, on the subject of consumer credit. In view of the role of the States in this field, we do not think Federal legislation is necessary.

Most states today, have laws that regulate and control the type of credit transactions handled by various companies that are members of this association. We do not believe that the superimposing of Federal regulation on top of existing state regulation will help. Neither do we feel that Federal legislation requiring the merchant, the dealer, the finance company, or the bank, to state the charges involved in a credit transaction, on an annual percentage rate, will help the consumer make more intelligent decisions about the use of credit. We fail to see how the passage of a Federal law of any kind is going to cause the consumer to use any different common sense than he has been using all along. Good judgment and education cannot be legislated!

In addition, as this subcommittee is fully aware, there has been in progress for several years a detailed study by the Commissioners on Uniform State Laws to determine if a Uniform Consumer Credit Code should be established throughout the fifty states. Particularly in view of the pendency of this project, we feel that the passage of any Federal legislation at this time is unwarranted. We believe it would be for the best interests of all concerned for Congress to wait and see the results of this study—which will become available, in final form, in the near future.

As this subcommittee is no doubt aware, this Association opposed S.5 in the form it was originally introduced. We testified before the Senate Subcommittee on Financial Institutions setting forth our reasons for this opposition. We watched with a great deal of interest the progress this bill made as it moved from subcommittee to full committee to the floor of the Senate. We had naturally hoped the bill would not pass as we still feel such legislation is not necessary. However, in fairness to all concerned, we must state that S. 5, as finally passed by the Senate, is a much better bill than it was when first introduced.

We would also be less than candid if we did not add to this statement that we feel there are one or two provisions of H.R. 11601 that we feel would improve S. 5. We agree with Mrs. Sullivan and those who have been advocating this type of legislation for many years that if a Federal Act is passed it should cover every segment of the consumer credit industry. Therefore, we feel that provisions for open-end credit, along the lines provided in H.R. 11601, should be added to S. 5. We also feel that mortgage credit, whether first or second, should be added to S. 5.

Having said this, however, we must keep the record straight by expressing our opposition to some of the other provisions of H.R. 11601 that differ from S. 5; namely: A Federal usury statute—a statute imposing a ceiling on rates to

be charged; a Federal statute pertaining to garnishment and confessions of judgment; and the provision giving the Executive Branch new authority of the Regulation W type. It is our firm belief that these matters do not belong in a bill pertaining to full disclosure.

In addition, we can see no reason for the establishment of a National Commission on Consumer Affairs. If S. 5 or a similar bill should pass both Houses, we feel the Federal Reserve Board can sufficiently administer such an Act without creating an additional agency.

It has been suggested by some that we in the finance industry are not concerned about the consumer, that all we really are interested in is making a profit. Anyone who makes such a statement just doesn't understand the business world.

No one is more interested in the consumer than are members of the American Industrial Bankers Association. Our livelihood depends on the consumer being satisfied, on his being treated right, on his being fully informed. If the consumer is unhappy, dissatisfied or doesn't understand what he's doing, he is going to stop dealing with our companies. When this happens, there just won't be any finance business, any finance business profits, or any tax revenues based on such profits.

Everyone is a consumer—without exception—and the consumer is capable of speaking for himself. He does this daily as he goes about buying merchandise and services that he wants. The American consumer is capable of speaking for himself and he does in any many ways.

Nowhere on earth do consumers have access to the quantity, quality, and variety of consumer goods, services and credit as is available to the American consumer—and at prices he can afford. This has come about because the consumer is satisfied. When millions of consumers are buying billions of dollars worth of merchandise and services on time, somebody, someplace, is not too unhappy.

Once more we repeat, we remain opposed to Federal regulation of consumer credit. We are convinced that any problems that may exist in this field can most appropriately be solved at the state level. However, if such legislation is passed by Congress we strongly urge that it be kept as simple as possible and as workable as possible. We firmly believe that S. 5, with the few changes we have outlined above, would be such a bill.

STATEMENT OF THE NATIONAL AUTOMOBILE DEALERS ASSOCIATION

The National Automobile Dealers Association appreciates the opportunity to present its views on H.R. 11601, the "Consumer Credit Protection Act", and the related bills being considered by this Subcommittee, including S. 5 as approved by the Senate on July 11, 1967.

NADA is a national trade organization whose membership comprises approximately 22,000 franchised new car and truck dealers engaged in the retail sale and service of all makes of new cars and trucks, both domestic and foreign, including farm implement dealers. Dealers in every State and Congressional District in the United States are included in our membership which is composed of 69 percent of the franchised dealers in this country. As such, we are vitally interested in the various legislative proposals presently before this Subcommittee which, if enacted, will directly and significantly affect the daily business operations of our members.

At the outset, we should like to point out that NADA has in the past opposed enactment of so-called "Truth-in-Lending" bills and continues to feel that the proposed legislation is unnecessary for reasons spelled out in detail in its statement of May 12, 1967, on S. 5 to the Subcommittee on Financial Institutions of the Senate Banking and Currency Committee. However, lest our position be misunderstood, it should be emphasized that this Association has always favored a truthful and complete disclosure to a purchaser of all pertinent details of the transaction, including finance charges and a detailed itemization of all other costs and charges. But we have advocated that the full disclosure of the elements making up the total cost should be expressed in the medium which is most comprehensible to the purchaser—in terms of dollars and cents, rather than as a percentage rate.

We believe that S. 5 as passed by the Senate is a more workable measure than the bill as originally introduced. S. 5 could be further improved by amendments which we will outline later in this statement.

It is also our belief that certain concepts contained in H.R. 11601 would go far to strengthen S. 5. In this regard, we especially commend Mrs. Sullivan and her cosponsors for incorporating the principle of "Truth-in-Credit Advertising" in H.R. 11601 and for the elimination of the exemptions provided in S. 5 for open-end and revolving credit, and first mortgage credit.

Our recommendations for improvement of S. 5 are set forth below.

1. Exemption for Open-End Credit Plans and First Mortgages.

One of the basic contentions of proponents of the legislation has been that it would give consumers a uniform yardstick to compare consumer credit costs. Yet, as passed by the Senate, S. 5 exempts most open-end credit plans from the requirement that finance charges be disclosed in terms of an annual percentage rate.

Under S. 5, creditors offering "open-end" credit need disclose an annual percentage rate, basically, only in connection with plans (1) involving a security interest or (2) in which less than 60 percent of the unpaid balance at any time outstanding is repayable within twelve months. This exemption gives a preferred position to a substantial portion of loan credit and the very largest part of the credit extended by the large national merchandising chains, thus placing automobile dealers and other small merchants at a severe competitive disadvantage. To cite but one example, dealers compete directly with many large chain stores in the sale of tires, batteries and accessories, as well as automobile service. In this area of competition, the preferential position given such stores in quoting monthly percentage rates for finance charges would present obvious and potentially disastrous consequences to dealers required to state such charges in terms of an annual percentage rate.

There is no justification for this "special favor" treatment for the fastest growing segment of the credit industry. The exemption in S. 5 of revolving credit plans of large retailers represents outright legislative discrimination against small businessmen such as auto dealers who must compete against giant chains which can afford the complex computer systems, credit departments and the like required for efficient and economical open-end systems—a luxury far beyond the limited means of the small merchant.

H.R. 11601 recognizes this inequity and restores comparability of credit costs by rejecting the Senate bill's exemption for open-end credit.

We fully subscribe to the following remarks of J. L. Robertson, Vice Chairman of the Board of Governors of the Federal Reserve System, on this matter in his statement before this Subcommittee on August 7:

"In eliminating the revolving credit exemption, the sponsors of H.R. 11601 have recognized the importance of providing consumers with a standardized method of comparing credit costs, and have avoided giving one type of creditor an unfair competitive advantage over another."

For similar reasons, we believe that first mortgage credits should not be exempted from the bill, as is done by S. 5, but should be covered, as provided in H.R. 11601.

2. Treatment of Insurance Premiums.

Under both S. 5 and H.R. 11601, all insurance charges must be fully disclosed. Section 3(d) of S. 5 expressly exempts from the definition of "finance charge" amounts collected by a creditor or included in the credit for filing fees, taxes and insurance if they are itemized and disclosed to the obligor. Section 202(d)(1) of H.R. 11601 apparently includes in the definition of the finance charge:

> "(C) charges or premiums for insurance against loss of or damage to property related to a credit transaction or against liability arising out of the ownership or use of such property; and (D) charges or premiums for credit life and accident and health insurance." (Sec. 3(d)(2)(c) and (d) of S. 5)

The consequences of such inclusion are most serious. The definition of "finance charge" in S. 5 was designed to conform closely to state law concepts because the draftsmen of S. 5 recognized that expansion of the concept of "finance charge" would only confuse consumers.

Differences between applicable state law and the concepts of the bill magnify the issue of Federal preemption and prevent the reconcilation of state and Federal disclosure laws now contemplated by Sections 203(g) and 205(a) of H.R. 11601.

There was no suggestion in the hearings on S. 5 that charges for insurance against loss of or damage to collateral or against liability arising out of its

ownership or use should be treated as a part of the finance charge. Property insurance, such as automobile physical damage insurance, is a normal incident of the ownership of a motor vehicle. No existing principle of law requires that charges for such insurance be characterized as finance charges.

Credit life and accident and health insurance present somewhat different problems. Each print of S. 5 treated credit life and accident and health insurance differently. The view of J. L. Robertson, Vice Chairman of the Federal Reserve Board, was finally adopted.

In his testimony before this Subcommittee on August 7, Governor Robertson, repeating his statement before the Senate Subcommittee on Financial Institutions, said in pertinent part:

"One of the issues that has proved troublesome during consideration of disclosure legislation has been the question of how to treat insurance premiums on policies taken out by borrowers as a condition of, and covering the amount of, the credit contract. * * *

"The fact remains, however, that inclusion in the finance charge of premiums for insurance that provides a benefit to the borrower over and above the use of credit would overstate the actual charge for credit. Therefore, we think that such premiums are not properly regarded as part of the finance charge, and should be specifically excluded, as provided in S. 5. We do believe, however, that the dollar amount of any such premiums included in the credit extended should be itemized, again as provided in S. 5."

For the reasons set out above, the previously quoted exemption for insurance contained in subsection (C) and (D) of Section 3(d)(2) of S. 5 should be added to Section 202(d)(1) of H.R. 11601.

H.R. 11601 contains the same civil and criminal penalty provisions found in S. 5. As applied to automobile dealers who handle one of the highest priced products covered by the proposed legislation, the civil penalties are inordinately excessive and call for modification.

If this legislation were easily understood and complied with, some valid argument for severe penalties might be made. But this is not the case. Installment sales made by automobile dealers are for long periods, ranging from twenty-four months to forty-two months. The penalty of two times the finance charge could, considering the complexity of the proposed legislation, result in bankruptcy for many automobile dealers. The sale of a new car with an unpaid principal balance of $3,000 at a $6 add-on rate for a term of three years produces a finance charge of $540. Twice the finance charge is $1,080. Thus, the penalty of twice the finance charge—even applying the S. 5 ceiling of $1,000—results not only in loss to the dealer of any compensation for the credit extended but also a loss of principal.

The civil penalties now provided in S. 5 and H.R. 11601 fully protect consumers without the penalty of twice the finance charge. Under both bills, a consumer recovering a penalty is also entitled to reasonable attorneys' fees and court costs. If a consumer shows any violation whatsoever, he is entitled to a minimum penalty of $100. It is unjustifiably harsh to impose, in addition, a penalty of twice the finance charge. Sale of an automobile on an installment plan is a complex transaction. A dealer is required to calculate, in addition to any finance charge, insurance premiums, taxes, certificate of title, and license and filing fees. The possibility of error, or of a misunderstanding leading to an allegation of error, is great and is appreciably widened if the "Truth-in-Credit Advertising" provisions of H.R. 11601 are adopted.

We strongly urge that the penalty be limited to loss of finance charge. If so limited, the consumer will lose nothing, except the possibility of a windfall. The provisions for attorneys' fees and the minimum penalty of $100 are sufficient to encourage civil actions to enforce the purposes of S. 5. We therefore suggest that Section 206(a)(1) of H.R. 11601 be revised to read:

"Any creditor who, in connection with any credit transaction, knowingly fails, in violation of this Act of any regulation issued hereunder, to disclose any information to any person to whom such information is required to be given shall have no right to collect in connection with such transaction any unpaid finance charge and shall pay to such person or credit to his account the finance charge paid by such person to the creditor in connection with the transaction, except that the penalty shall not exceed $1,000 on any credit transaction. If the foregoing penalty is less than $100, the credit shall in any event be liable to such person in the amount of $100."

To forestall a multiplicity of nuisance suits against creditors, we would also urge that a provision be inserted in the bill which would hold an unsuccessful plaintiff liable for the defendant's reasonable attorneys' fees and court costs. Thus, both parties would be placed on the same footing and the litigious-minded would be forced to give pause before instituting a frivolous suit in the hope of a quick settlement.

This could be done by deleting the sentence beginning at line 8 of page 23 of H.R. 11601 and substituting the following:

"In any such action to recover a penalty as prescribed in paragraph (1), the losing party shall be liable for the reasonable attorneys' fees of the prevailing party and court costs as determined by the court."

Finally, as regards the civil penalities section, we would recommend the delection of the words "and prior to the institution of an action hereunder or the receipt of written notice of the error" in lines 23 through 25 on page 22 of H.R. 11601. The present civil penalties section provides an adequate remedy to all debtors without making a game out of the discovery of errors. Every creditor should be given the opportunity to correct his error as soon as it is discovered, no matter who discovers it.

4. Inclusion of Agricultural Transactions.

In the Executive Session of the Senate Subcommittee on Financial Institutions, agricultural transactions were specifically brought within the scope of S. 5 and adopted by the Senate. They are also included in H.R. 11601. The inclusion of agricultural transactions raises many problems for our dealers.

The income of most farmers is seasonal and highly variable. Repayment schedules must be adapted to income patterns. Agricultural transactions probably involve the most complex and difficult computations of any installment credits. The bill should protect farmers as consumers, and exempt farmers as businessmen. The specific addition of credits extended for agricultural purposes, whether or not for personal, family, or household purposes, would have the effect of giving businessmen who are farmers protections which they have not requested. These protections will only serve to increase the cost of credit to farmers and make it more difficult for them to obtain credit. This Subcommittee is urged to exclude from the scope of H.R. 11601 business transactions entered into by businessmen whose business is agriculture.

5. The "Truth-in-Credit Advertising" Provisions of H.R. 11601.

As mentioned at the outset, NADA is pleased to see H.R. 11601 include requirements with respect to the advertisement of credit. While we recognize that this bill will not cure all the ills of advertising, it nevertheless offers a good beginning, at least as regards the advertisement of credit to which it is specifically directed.

By the way of background, NADA has been engaged in the battle against false, misleading and deceptive automobile advertising since 1954. It has pioneered in this field and is today without peer in its programs and efforts.

The initial "Recommended Standards of Practice for Advertising and Selling Automobiles" were compiled jointly by NADA and the Association of Better Business Bureaus twelve years ago with the aid of a grant of $25,000 by NADA's Board of Directors for this purpose.

The Standards are reviewed periodically by the NADA Advertising Standards and Practices Committee with the Automobile Advertising Committee of the ABBB in order to keep them current with changing business conditions and new concepts in advertising. As an example, provisions of the code were extended two years ago to include the advertising of rental and leasing of automobiles, phases of the business which have grown considerably in recent years.

During this period, NADA has spent, by a conservative estimate, well in excess of a half million dollars promoting the adoption of its advertising standards by members, automobile dealers generally, the manufacturers, advertising agencies and the media. We have sponsored extensive advertising campaigns in the media trade press urging their adoption of these standards, or acceptable adaptations; we have provided speakers for a variety of meetings of advertising representatives of the media, explaining our objectives and seeking their cooperation; we have distributed thousands upon thousands of copies of the standards and have provided additional thousands to Better Business Bureaus throughout the country for supplemental distribution on their part.

Copies of these standards have also been made available to the public, schools and colleges, research libraries, individual consumers and others.

Our programs, aims and objectives have been made known to the Federal Trade Commission, and other government agencies, from time to time. We have had discussions with FTC officials seeking their advice and cooperation.

Our most successful operations have been conducted with the cooperation and assistance of the Better Business Bureaus in some metropolitan areas and substantial amounts of dealers' money. Probably the most successful program has been sponsored in Chicago by the Better Business Bureau of Metropolitan Chicago and the Chicago Automobile Trade Association with the full support of the local media.

Chicago dealers contribute $35,000 annually to the Bureau to underwrite the cost of "refereeing" automobile advertising in that market, using the NADA Standards as the guide for judging. A constant and keen eye is maintained by the Bureau in the Chicago market and when, in its opinion, a dealer's advertising is false, misleading or deceptive, it issues a "not-in-the-public-interest" (NIPI) objection and the media immediately withdraws the advertising deemed unsatisfactory and refuses to accept additional advertising from the offender until a corrected ad and apology is published and the Bureau lifts its "indictment."

Similar arrangements exist in several other cities, Boston probably being the next most successful example.

In all its advertising and public relations support of this program, NADA has stressed that its efforts are in the public interest, and that it is reasonable to expect similar interest on the part of the media for their readers, listeners and viewers.

Some members of the media have adopted or adapted our standards and have reported their action to us. Others have indicated very frankly that they are interested in advertising solely as a source of revenue and have no intention of judging the content unless it be so obviously false, misleading and deceptive, or otherwise objectionable, that it would be certain to cause embarrassment or legal complications to them.

The media can, and on occasion does, contribute to the deception with full knowledge. Therefore, granting the media exemption from any responsibility for the acceptance and publication of false, misleading and deceptive advertising would substantially curtail the intended objectives of the advertising provisions of this bill.

We would urge this Committee to give serious consideration to limiting the exemption granted the media by imposing a responsibility to all in the public interest in rejecting for publication false, misleading and deceptive credit advertising.

Having indicated our long-term efforts and progress in the field of automobile advertising, generally, we now come to the specific provisions of H.R. 11601 as they affect the advertisement of credit and we recommend the following constructive and clarifying amendments.

Sections 203 (j) and 203 (k) of H.R. 11601 require all consumer credit advertising containing "specific terms" to set forth clearly and conspicuously virtually the same information required to be disclosed to consumers before any credit is extended.

S. 5 now protects a consumer after he has decided to seek credit. Regulation of advertising will supplement this basic protection by insuring that consumers have accurate information before deciding to seek credit.

All reputable creditors should support extension of the full disclosure principle to advertising. However, the advertising provisions of H.R. 11601 raise a number of technical and practical problems, including (1) improper definitions, (2) the amount of information required to be disclosed, and (3) the severity of penalties.

H.R. 11601 defines an "advertisement in interstate commerce or affecting interstate commerce . . ." (Section 202 (i)). However, the definition is merely jurisdictional; it neither defines an advertisement nor specific credit terms.

In the interest of clarity, the term advertisement should be amended to read:

"'Advertisement' means any publication, display, broadcast, solicitation or representation in connection with any credit or consumer credit sale."

The suggested definition omits any reference to interstate commerce because the declaration of purpose in Section 201 (a) (page 3, lines 4 through 8) expressly invokes the powers of Congress to establish a currency and regulate its value, thus mkaing it unnecessary to limit the scope of the act to advertisements

in interstate commerce. The definition, therefore, covers all forms of consumer credit advertising.

A definition of specific credit terms should be added to Section 202 (i):

"An advertisement contains specific credit terms if it states any of the following: (A) a rate or rates of any finance charge; (B) the amount of any finance charge; or (C) the amount of any installment or installments."

The definition is important because under the vague language of H.R. 11601 any advertisement containing any specific information must apparently disclose all of the detail required by Sections 203 (j) and 203 (k).

Creditors should not be required to add a mass of detail to all advertising. Advertisements stating only "loans to $2,500" or "terms up to 24 months" are unlikely to mislead consumers and provide valuable information about the services offered by creditors. The detailed requirements of Section 203 (j) and 203 (k) would lead creditors to limit advertising to "tombstone" notices. Consumers would, as a result, receive even less information about credit terms than they now do.

The advertising provisions of H.R. 11601 should be designed to prevent misleading credit advertising instead of requiring disclosure of detailed and often meaningless information. The suggested definition of specific credit terms accomplishes the purpose by enumerating the kinds of information which have sometimes been stated in a misleading or confusing fashion.

Section 203(j) and subsection (1) of that section require a creditor advertising "specific" credit terms to disclose in the advertisement, clearly and conspiculously: (a) the cash price, (b) the number, amount and period of each installment payment, (c) the down payment, (d) the time sale price, and (e) the finance charge expressed in an annual percentage rate.

It would be difficult for creditors to comply with Section 203(j). In automobile sales, for example, the cash sale price frequently depends upon competitive factors, the time of the year, the dealer's inventory, and the like. The cash sale price also reflects the options selected by the purchaser. It would, therefore, be difficult to state a true cash sale price in an advertisement.

The number and amount of payments depend on the needs of the customer, his credit standing and other factors. The amount of the down payment is similarly variable. The time sale price and the finance charge reflects the down payment and the number of installments. The annual percentage rate depends not only on all these factors but on additional variables such as the date of the first installment payment.

Section 203(j), therefore, should be amended to shift its emphasis from disclosure of detailed and often meaningless information to prevention of misleading credit advertising. The interpretation to 203(j) and subsection (1) of that section should be revised to read:

"No creditor in any advertisement containing specific credit terms and designed to promote or induce, directly or indirectly, any credit or consumer credit sale shall state:

(1) a rate or rates of finance charge, unless the annual percentage rate is also stated

(2) the amount of any finance charge or installment payment, unless the annual percentage rate and the number, interval and amount of installment payments are also stated."

The suggested amendment will not deprive consumers of any substantial protections. The detailed information required by Section 203(j)(1) must be disclosed by a creditor "before the credit is extended." E.g., Section 203(b). On the other hand, there is likely to be more advertising of helpful information if creditors are relieved from the overly detailed requirements now contained in Section 203(j)(1).

Failure of a creditor to comply with Sections 203(j) or 203(k) is, apparently, a violation of Section 206. Under Section 206, any creditor who, in violation of Section 203, fails to disclose, to any person to whom information is required to be given, is liable to such person for $100 or twice the finance charge required by the creditor in connection with the transaction, whichever is greater, plus attorneys' fees.

The civil penalty section, thus, raises the possibility that anyone who reads a newspaper or watches a television program containing an advertisement which does not comply with the requirements of Section 203 would have a right to a penalty of $100 and attorneys' fees. In addition, any obligor able to show that

a credit transaction was preceded by an advertisement which violated the law, apparently, could recover the civil penalty even though the creditor disclosed to him before the credit was extended all the information required by Section 203 and had thereby, cured any defects in the advertisement.

The advertising provisions of H.R. 11601 were copied from Senator Magnuson's proposed "Fair Credit Advertising Act." Senator Magnuson's proposal contains no civil penalties. It would, therefore, seem that application of civil penalties to advertising violations was inadvertent. H.R. 11601, like Senator Magnuson's Act, should rely exclusively on criminal penalties for enforcement of its advertising requirements.

The introduction to Section 206(a)(1) should, therefore, be amended to read:

"Any creditor who, in connection with a credit transaction, knowingly fails in violation of Section 203 (*except subsections 203 (j) and (k)*), or any regulation thereunder. . . ." (New matter italicized.)

We believe that the net result of legislative action along the lines suggested in this statement will be a measure which would deal with the realities of the situation to which both S. 5 and H.R. 11601 are addressed. We strongly recommend, however, that such legislation should not include sections of H.R. 11601, not found in S. 5, providing for a statutory interest rate ceiling, prohibiting the garnishment of wages or confession of judgment, and authorizing the imposition of selective controls on consumer credit. Nor do we see any clear need for a National Commission on Consumer Affairs. Finally, the effective date of the legislation should be that prescribed by S. 5 rather than H.R. 11601.

We have attempted in this statement to treat what we regard as the more important provisions of S. 5 and H.R. 11601 as they affect our members.

By way of summation, we remain unconvinced that the anticipated benefits to the consumer from enactment of legislation in this field will be realized. And we continue to believe that the burdens imposed on small independent businessmen who sell automobiles, trucks and farm implements will far outweigh the supposed benefits accruing to consumers.

Nevertheless, if there is to be legislation, we would hope that the final version would include amendments to S. 5 proposed above along with the incorporation in S. 5 of those provisions of H.R. 11601 which we have presented and supported in this statement.

STATEMENT OF AMERICAN ASSOCIATION OF UNIVERSITY WOMEN, WASHINGTON, D.C.

Madam Chairman and members of the committee, the AAUW welcomes the opportunity to support enactment of a Truth-in-Lending or Consumer Credit Protection Act.

The rise in consumer debt over the past quarter of a century in its relation to either the Federal debt or to the disposable income of this country's wage earners has been astonishing. The rise in the cost to the consumer of such debt is in many instances equally amazing. Even the otherwise sophisticated fall prey to hidden charges, to misleading advertising and to small print in contracts. Many seemingly astute home buyers believe they are paying 6% interest a year, when in fact, they are paying 12%. Many otherwise "educated" purchasers of commodities fail to translate 2½% a month in finance charges into something that can be costing 30% a year.

While credit, used wisely and properly extended, can be useful both the the consumer and producer, we in AAUW, believe many current consumer credit practices are insupportable and harmful both to the stability of the economy and to the welfare of the public.

We believe the buyer has a right, when making a purchase on credit under contract, to information in writing on the total dollar amount of the credit charge, and to this dollar charge expressed as a true annual percentage rate on the outstanding or unpaid balance. In other words, we believe the consumer has a right to know, indeed, that the seller has an obligation to reveal the difference between the cost of an article sold for cash and the final cost of one sold on credit when paid for within a stipulated time. We believe that any incidental charges, such as charges for servicing the loan or for life insurance should be disclosed in writing to the borrower. We also believe that the disclosure requirement should be extended to cover the advertising of credit in order that consumers be in a position to make a comparison of the costs of different kinds of credit.

We have referred to those "who should know better" as victims of bait advertising and "easy credit" but the plight of the underemployed, the poorly paid and the undereducated is desperate since they rarely have money for cash purchases and resort to credit buying for almost every commodity which they purchase except food. These are the consumers who cannot afford to shop for their credit, who cannot understand the technical language even when able to read a contract, and who fall most frequently into the trap of fraudulent or grossly misleading information, and overselling, and who accept as inevitable exorbitant interest rates.

These are the people that suffer most from the garnishee process. We believe regulation of collection practices such as tying up the debtors wages in garnishment or threatening disclosure of debt to an employer or to the welfare agency as a collection device (a threat which to the debtor becomes a threat of loss of his job or being taken off welfare rolls) would reduce to a measurable degree the practices of overextension of credit to the poor and the subsequent repossession (and frequently resale) of partially paid for merchandise.

While we recognize the difficulties of stating accurately on an annual basis the interest charges on fluctuating "revolving" charge accounts we believe those consumers whose charge accounts are rarely paid in full should be made aware of the yearly cost of the credit they use—or in other and simpler words, of the money they rent. We also see as a possibility that more and more businesses might resort to revolving accounts as a loophole by which to avoid full disclosure unless these revolving accounts are covered in the legislation under consideration. For this reason we prefer the language of the Administration Bill and H.R. 11601, Mrs. Sullivan's bill, to that of the Senate passed bill. We have noted that the Senate passed bill exempts transactions of $10 or less. We believe, like the "revolving" charge account, the small loan transaction should not be exempted as in the latter case regrettable and usurious practices are frequently reported.

We also are at a loss to understand why S.5 excludes first mortgages and loans to businesses from its disclosure provisions.

We are gratified that the legislation before this Committee calls for the drafting of detailed regulations by the Federal Reserve Board to put Truth-in-Lending into effect and that the Board is to be given powers of administrative enforcement to secure compliance.

We thank you for the privilege of having this statement included in the record of the hearings of this subcommittee.

CONSUMER CREDIT INSURANCE ASSOCIATION,
Chicago, Ill., August 22, 1967.

Hon. LEONOR K. SULLIVAN,
Chairman, Subcommittee on Consumer Affairs, House Banking and Currency Committee, Rayburn House Office Building, Washington, D.C.
(Attention: Mr. Charles Holstein).

DEAR REPRESENTATIVE SULLIVAN: Enclosed is a statement of the Consumer Credit Insurance Association with respect to H.R. 11601 and related bills which bills have been the subject of Hearings before your Subcommittee.

We appreciate your giving this statement consideration and making it a part of the Hearing record.

Very truly yours,

WALTER D. RUNKLE,
General Counsel.

STATEMENT OF CONSUMER CREDIT INSURANCE ASSOCIATION WITH RESPECT TO H.R. 11601 AND RELATED BILLS

This statement is filed on behalf of the Consumer Credit Insurance Association (CCIA), a national trade association composed of 94 insurance companies which write insurance in connection with credit transactions of all types. The CCIA was organized in 1951 specifically as a trade association of insurance companies engaged in the business of underwriting insurance in connection with loans and credit transactions and has confined its activities to these areas up to the present time. We recognize H.R. 11601 is principally a proposal with respect to finance or loan practices but we feel it is desirable to express our views with regard to

the treatment of credit insurance that might be affected by H.R. 11601 and the related bills being considered by your Committee.

Our Association does not believe that any responsible spokesman for the insurance industry would oppose separate disclosure of the facts of an insurance transaction consumated in connection with a credit transaction, as now required by S. 5, also under consideration by your Subcommittee. This disclosure, we believe, should be a basic prerequisite to the transaction itself. This is the concept expressed in the so-called Model Bill to Provide for the Regulation of Credit Life and Credit Accident and Health Insurance developed by the National Association of Insurance Commissioners in 1957 and subsequently enacted in a majority of the states.

Serious problems could be created by enforcement of H.R. 11601 if insurance is included in the definition of "finance charge." The basic concept of "disclosure" as presently set forth in H.R. 11601 would be contrary to the principles of the NAIC Model Bill and other state insurance and finance laws and regulations. H.R. 11601 would require the cost of credit life insurance, credit accident and health insurance and property insurance in connection with a credit transaction to be included in the computation of the "annual percentage rate." We do not believe this should be required. The primary benefits from insurance provided in connection with a credit transaction flow to the debtor. If the debtor dies without credit insurance his estate is responsible to discharge the indebtedness. If the borrower is sick or injured and does not have credit accident and health insurance he remains fully responsible for the payments. With credit insurance the underlying obligation is reduced or discharged in accordance with the terms of the insurance policy. Although it is recognized the creditor's collections may be facilitated from the insurance obtained by its borrowers, nevertheless, the primary benefits do inure to the protection of the debtor or his estate.

J. L. Robertson, Vice Chairman of the Board of Governors of the Federal Reserve System in his statement on S. 5 discussed the subject of insurance and concluded "to require that the finance charge include insurance premiums would overstate the actual charge for credit. Therefore, we think that the cost of any kind of insurance is not properly regarded as part of the finance charge, and should be specifically excluded in S. 5." Subsequently, the Senate adopted Mr. Robertson's recommendations, as evidenced by the final version of S. 5 as passed by that body.

More recently Mr. Robertson, in his statement on H.R. 11601 and related bills, again discussed insurance emphasizing that "inclusion in the finance charge of premiums for insurance *that provides a benefit to the borrower over and above the use of credit* would overstate the actual charge for credit" and concluded "that such premiums are not properly regarded as a part of the finance charge, and should be specifically excluded, as provided in S. 5." (emphasis supplied) We strongly endorse this recommendation. We believe the inclusion of insurance costs in determining the annual percentage rate would distort the true expression the sponsors of the bill seem to be seeking.

Meaningful comparisons of percentage rates with insurance included become extremely difficult when it is recognized that similar types of lending institutions charge different rates for similar insurance and offer different plans of insurance with a wide range of premium charges. In credit accident and health insurance, for example, there are numerous variations in benefits with consequent variations of rates being charged. When property insurance is added as a further consideration, the problems are significantly multiplied. Attempting to include insurance costs in the calculation of percentage rates without regard to benefits being provided would only compound confusion where comparison is to be made by debtors, creditors or regulators.

In keeping with the recommendations of the NAIC we believe a more beneficial concept of complete disclosure is accomplished by breaking down, in dollar amounts, insurance costs, if any, so that the purchaser or borrower can see what he is paying for each type of insurance. In this manner and only in this manner can the customer evaluate his insurance costs and coverages. If lumped in generally with "finance charges" the lack of separate identification of insurance costs tends to defeat the real concept of disclosure in that the *customer may never be aware that he has insurance much less know what it costs.*

Insurance, particularly where written in connection with credit transactions, must stand on its own merits in the eyes of the debtor who pays for the coverage and in the eyes of the creditors and regulators. Insurance must be separately

disclosed and separately evaluated, as now provided in S. 5. Any regulation which would tend to treat insurance as an integral part of a credit transaction would make it very difficult, if not impossible, to maintain adequate policing of rates charged in relation to benefits provided. Consistent with Mr. Robertson of the Federal Reserve Board we urge you to amend H.R. 11601 to exclude insurance as a component of "finance charge."

NATIONAL FOUNDATION FOR CONSUMER CREDIT,
Washington, D.C., August 3, 1967.

Hon. LEONOR K. SULLIVAN,
House of Representatives,
Washington, D.C.

DEAR MRS. SULLIVAN: I acknowledge your request for our appearance before the Consumer Affairs Subcommittee, Tuesday, August 8, 1967.

The National Foundation for Consumer Credit is composed of manufacturing, retailing, banking and other financial concerns dedicated to the purpose of making the consumer credit transaction better understood and more intelligently handled. With our membership so widely diversified and with each industrial, trade and financial group in our membership being represented specifically by the trade association or associations in its own field, we do not undertake to come to any common agreement on policy with respect to the intracacies of any legislation.

Our principal concern is with two major projects: (1) education, through the schools and colleges, in the area of consumer credit, to prepare the oncoming generation for its intelligent use; and (2) sponsorship of a nationwide network of non-profit Consumer Credit Counseling Services to help people who find themselves in credit and financial difficulty.

In more than 2,800 cities, the public schools have accepted our unit, using our credit intelligently for classroom teaching. Many parochial and other private secondary schools have done the same. Among those who edited it were fifty-five teachers, principals and superintendents who volunteered their time to help us make the study as impartial as possible.

This resulted, by the way, in 28 separate manuscripts before so many points of view could be meshed to the satisfaction of all.

In the Counseling area there are now more than seventy Services in operation with possibly 27,000 families under our wing at the moment. Private enterprise is investing close to two million dollars a year in this project alone, setting up the local Services. We believe before long there will be several hundred of these in operation.

I am taking the liberty of sending you a copy of both using our credit intelligently and the plans and working suggestions pertaining to the Counseling Service program.

These projects and the work involved in explaining them to all sorts of civic groups and to the teachers, to say nothing of persuading enterprise to support this effort take about all the time and money the Foundation has been able to generate.

So we respectfully suggest that we are really unable to contribute to the hearings on H.R. 11601 constructively; have not been instructed by our membership or officers as to their attitudes. These I expect could be varied and hardly within our province to seek to coordinate. I appreciate your thoughtfulness in suggesting that we testify.

I should like very much in the course of events to find that you may be interested personally in the work we are doing; should enjoy the opportunity to discuss it with you at your leisure.

Incidently we are not a large organization and do not assume to represent any cross-section of business and banking opinion in the manner that the large trade associations can.

Cordially yours,

W. J. CHEYNEY,
Exec. Vice President.

P.S.—I thank you for the copy of the H.R. 11601 and the accompanying July 20 release.

NATIONAL ASSOCIATION OF HOUSE TO HOUSE INSTALLMENT COS., INC.,
New York, N.Y., August 4, 1967.

Hon. LEONOR K. SULLIVAN,
Chairman, Subcommittee on Consumer Affairs, House Banking and Currency Committee, House Office Building, Washington, D.C.

DEAR CONGRESSMAN SULLIVAN: I am writing to you on behalf of the more than 370 direct selling credit companies that are members of the National Association of House to House Installment Companies, all of whom have a vital interest in the "Truth-In-Lending" Bill.

I think it is a basic concept that Federal legislation should not discriminate against one group as opposed to another. It should be basic, therefore, that all retail creditors should be treated equally and kept on equal footing. Any disclosure legislation should not, in the way terms are to be stated, discriminate against retailers using any particular method of extending credit and should not favor other retailers such as department stores using other methods of giving credit.

For example, the "Truth-In-Lending" Bill now allows typical department store revolving credit to give service charge as monthly rate only but requires revolving accounts with title-retention and conventional installment accounts to give annual percentage rates, such as 18 per cent if monthly rate is 1½ per cent. This puts independent retailers who are in competition with department stores on big ticket items at a tremendous disadvantage.

In our type of *continuous* credit relationship with a customer, there are weekly payments plus add-on sales so that it is both a practical and a mathematical impossibility to establish the so-called "true" annual rate of interest. What our customers are interested in is the dollar cost of the credit that they obtain.

The purpose of the "Truth-In-Lending" Bill is to protect the consumer. Its purpose is not to protect one class of retailers against another and discriminatory protection of this type does nothing to enhance the protection given to the consumer in any way.

Sincerely yours,

EDWARD L. SARD,
Executive Director.

NATIONAL LEAGUE OF INSURED SAVINGS ASSOCIATIONS,
Washington, D.C., August 8, 1967.

Hon. LEONOR K. SULLIVAN,
Chairman, Subcommittee on Consumer Affairs, Committee on Banking and Currency, House of Representatives, Washington, D.C.

DEAR CHAIRMAN SULLIVAN: The National League of Insured Savings Associations is a nationwide trade association serving the savings and loan industry. Its 1967 Legislative Conference in Washington, D.C. on February 14 voted to support the principle of Federal Truth-in-Lending legislation.

This action was consistent with the National League's past support of the principle of such legislation introduced in earlier Congresses.

As you know, it has been the historical practice of the savings and loan industry to quote costs of interest on loans secured by mortgage of real property in terms of a simple annual rate of interest. Nearly all other financing costs of real estate loans are payable in cash at the time of closing the loan transaction. While certain of these payments at closing may at times be destined for the lending institution, most such payments are for the benefit of third parties other than the lender or the borrower. In cases where the loan is to aid in purchase of real estate as distinguished from other uses of the loan proceeds, there are likely to be several cash payments to be made at the closing.

Again, it is a fairly common practice among our members to give the borrower-mortgagor a statement in writing at the closing setting forth the sales price, the principal sum of the mortgage, the schedule of mortgage payments, the interest rate, and amounts to be paid by the borrower at the closing.

While payments at closing form an essential part of the loan transaction, they do not themselves constitute a credit transaction, because they are handled on a cash basis.

It would appear, therefore, that in a real estate mortgage transaction, truth-in-lending is accomplished as long as the potential borrower is furnished information as to the basic cost to him of the loan he agrees to repay. He should, of

course, also be fully informed of any non-loan portions of the transaction, that will require payment of funds by him at closing or earlier. These purposes are accomplished when the borrower is furnished written statements of the type noted above.

Our members will continue to follow their present disclosure practices as a matter of policy.

We understand that the Board of Governors of the Federal Reserve System and the Under Secretary of the Treasury have recommended that loans secured by a first mortgage on real estate be excluded from the provisions of truth-in-lending legislation because adequate disclosure is already made to the borrower in this type of transaction. The National League confirms this reasoning as to its member savings and loan associations, all of which have savings accounts insured by the Federal Savings and Loan Insurance Corporation and are therefore regulated by the Federal Home Loan Bank Board, an independent agency of the Federal government.

The present main concern of National League members is that the differences between a real estate mortgage transaction and a retail credit transaction be accommodated in any statute enacted in this field. Retail credit transactions do not normally involve the type of payments at closing that have come to be customary in real estate mortgage transactions.

Some other distinctions between the two types of transactions follow. Some real estate mortgages contain provisions relating to penalties that may be optionally charged by the mortgagee or its assignee for late payments not made timely pursuant to the payment schedule. Some real estate mortgages contain provisions permitting the mortgagee or its assignee to charge a premium if the mortgagor exercises his privilege of prepaying a substantial portion of the outstanding balance due on the mortgage. While often referred to as a "penalty", this payment in reality helps reimburse the lender for the expense of finding and making use of a suitable reinvestment medium for funds in connection with which it had already incurred placement expenses when advanced as a loan to the mortgagor. This is also a charge left within the discretion of the mortgage holder if the borrower triggers the occasion for its use. The premium provision is usually not invoked if the borrower is using his own funds to exercise his privilege of prepayment rather than merely using funds borrowed elsewhere at a cost lower than the interest rate on the mortgage being prepaid.

When such late charge or prepayment premium options do exist, they are fully set forth in the mortgage document itself, so the information concerning them is available to the borrower. In addition initiation of the circumstances making such charges applicable rests not with the mortgagee or its assignee, but rather with the borrower.

Since the cause for invoking the charges may never occur, it would not seem appropriate to require any more than a caution to the borrower that he or his advisers should carefully read the mortgage instruments involved.

It is urged that suitable exclusions be made from those provisions of the bill dealing primarily with retail credit transactions, in order to recognize the differing situation prevailing in real estate mortgage loan transactions.

It is further requested that if mortgage loans are included in the legislation, the Committee report on the bill encourage the Board of Governors of the Federal Reserve System to make liberal use of the authority section 205(b) of the Federal Reserve Act as proposed to be added by H.R. 11601 and section 6(b) of H.R. 11602 would confer upon it to exempt from the requirements of the Act any credit transactions or class of transactions it determines to be effectively regulated under State laws. In fact we would encourage the Subcommittee to insert the words "or business practice substantially similar to the requirements under that section" after the word "enforcement" in proposed section 205(b) of H.R. 11601 in line 20 on page 21. The comparable amendment in H.R. 11602 would occur in line 2 on page 18. Such an amendment would permit the Federal Reserve Board to take cognizance of the fact that the disclosure practices already followed by savings and loan associations in making mortgage loans on real estate make available to the borrower the information it is the purpose of this legislation to supply to him.

We stand ready to respond to any invitation from you to work with you and members of your Subcommittee or its staff to discuss further ways to implement the ideas set forth in this letter.

It will be appreciated if these views are included in the printed record of the hearing on this proposed legislation.

Sincerely,

REX G. BAKER, JR.,
President.

CALIFORNIA FARMER-CONSUMER INFORMATION COMMITTEE,
Santa Clara, Calif., August 8, 1967.

Hon. LEONOR K. SULLIVAN,
Chairman, House Consumer Affairs Subcommittee,
House Office Building,
Washington, D.C.

DEAR CONGRESSWOMAN SULLIVAN AND MEMBERS OF THE SUBCOMMITTEE: In behalf of our half a million members of affiliated groups, organizations, cooperatives and individuals, we place our wholehearted support for passage of H.R. 11601 relating to consumer credit and truth-in-lending, legislation.

We have followed the history of the truth-in-lending bill, first introduced by former Senator Paul Douglas some seven years ago, and continue to marvel at the audacity of the powerful and well-financed lobbies who oppose such legislation which would benefit the public at large.

The time was not too distant when reputable banks loaned money to reputable customers at reasonable rates in complete trust.

Gradually this procedure changed as more and more money lenders discovered that the interest paid on consumer credit is BIG, BIG BUSINESS.

The poor and uneducated are easy victims of unscrupulous operators. However, they are not alone. The educated too, are victims of unethical bankers and misleading and fraudulent advertising covering retail credit, new or used car loans or any type of modern merchandise.

Continued abuses in consumer credit practices produce a grave demoralizing effect on the public at large, particularly if such deceptive practices are condoned from the top.

We urge an immediate "Do Pass" for H.R. 11601, so that it may reach the House for a vote in this session of the 90th, Congress.

Very truly yours,

BORGHILD HAUGEN,
Consumer Consultant.

DEPARTMENT OF BANKING AND INSURANCE,
DIVISION OF BANKING,
Montpelier, Vt., August 10, 1967.

Representative LEONOR K. SULLIVAN,
House of Representatives,
Washington, D.C.

DEAR MRS. SULLIVAN: I have been following the progress of truth-in-lending with great interest both because of my position here in the State of Vermont and for more personal reasons.

As Commissioner of Insurance, I have spoken out several times against the pernicious practices existing in the sale of credit life insurance and credit health insurance. Most recently, I was the lead-off witness at a hearing convened by Senator Hart, the Chairman of the Senate Antitrust and Monopoly Subcommittee. I enclose a copy of my statement presented there. (See p. 914.)

Naturally, I have been especially interested in the disposition of the credit life charge as it relates to interest disclosure. Governor Robertson argues that the insurance premiums provide a benefit to the borrower over and above the use of credit and inclusion of the premium in the finance charge would overstate the actual charge for the credit itself.

Obviously, there is something to this. However, if the creditor is arranging for the insurance at, say, $1 per $100 borrowed repayable in one year—a common rate in many areas—he may well be receiving as much as 60% of that charge as a commission, dividend or in other more complicated ways. Clearly, this "kickback" is hardly a benefit to the borrower.

As the bill was progressing through the Senate, it occurred to me that a useful compromise between the pros and cons for inclusion of the insurance premium in the finance charge would be to require that anything in excess of 50¢ per $100

borrowed repayable in twelve months, or its equivalent for longer or shorter durations, be included as part of the finance charge. Another way of expressing this would be to include the total insurance premium in the finance charge and then to allow a deduction of ½% for the credit life insurance.

It seems to me that such a measure would be very easy administratively and would do justice to Governor Robertson's point.

It might also have a beneficial effect on excessive rates charged for this kind of life insurance in many of our states.

The rate of 50¢ mentioned is the maximum rate permitted for credit life insurance in the small loan acts of at least two states—Massachusetts and Connecticut. Most creditors can obtain the insurance for their customers at less than this rate.

If there is any room for compromise at all on this matter it should lie along these lines. If you feel that there is any merit to the suggestion, I would certainly be glad to discuss it further with you.

Sincerely,

JAMES H. HUNT,
Commissioner.

AMERICAN BOOK PUBLISHERS COUNCIL, INC., AND
AMERICAN TEXTBOOK PUBLISHERS INSTITUTE,
Washington, D.C., August 17, 1967.

Hon. LEONOR K. SULLIVAN,
House of Representatives,
Rayburn House Office Building,
Washington, D.C.

DEAR MRS. SULLIVAN: At the request of the Reference Book Section of the American Textbook Publishers Institute, I am writing you concerning Section 205 of H.R. 11601, the truth-in-lending act. We believe that Section 205 of the bill should be modified to discourage the states from enacting their own versions of truth-in-lending laws. Subsection 205 (a) now provides that the Federal act shall not be construed to annul or exempt any creditor from complying with any state law relating to disclosures in connection with credit transactions, except where such laws are inconsistent with the provisions of the Federal act. Subsection 205 (b) allows the Federal Reserve Board by regulation to exempt from the act any credit transactions which it determines are effectively regulated by state laws. By implication, these two subsections seem to encourage the several states to enact their own credit disclosure requirements.

Most publishing firms do business in many other states other than the one in which they are principally housed. We seriously doubt that Congress would want to incur a multiplicity of requirements that would constitute a restraint of trade in interstate commerce. We would strongly recommend, therefore, that Section 205 be amended to discourage the states from enacting 50 different credit disclosure requirements. It should be made clear that compliance with the Federal act concerning credit disclosure would preempt the states in this area.

We agree with Mr. Robertson, Vice Chairman of the Board of Governors of the Federal Reserve System, that the Federal implementing agency should not be called upon to judge how effectively state laws in this field are enforced. But we also feel strongly that Congress should not be encourging the states to enact 50 different requirements for industry to satisfy. Simple reason, we think, should dictate that a properly worded Federal act resulting in a more effective disclosure of credit costs to consumers should be sufficient to satisfy the needs of all consumers, irrespective of the state in which the consumer lives; and we believe that the states should be preempted from further regulations. Placed in a national perspective, firms shipping goods across state lines ought not to have 50 contractual barriers to satisfy if they want to do business on a national level.

Sincerely,

CLIFFORD P. GRECK,
Director, Washington Office.

NEIGHBORHOOD LEGAL SERVICES CENTERS,
Detroit, Mich., August 23, 1967.

Hon. LEONOR K. SULLIVAN,
Chairman, Subcommittee on Consumer Affairs, House Committee on Banking and Currency, House Office Building, Washington, D.C.

Dear MRS. SULLIVAN: I write you as the Research Director of the Neighborhood Legal Services Program of the City of Detroit, a part of the Administration's War on Poverty.

Our office has been functioning in assisting the people of our community for somewhat less than a year. Even in that brief span of time, it has become very clear to us that among the very basic problems faced by the poor are those of consumer credit sales and financing.

The poor are untutored in the wise use of credit and are prey to that segment of the comercial community which takes advantage of this lack of knowledge to deliberately induce credit buying beyond their means.

I was most pleased to read that your credit protection bill contains a prohibition on the garnishment of wages to settle debts. I have reluctantly come to the conclusion that this somewhat drastic remedy is absolutely necessary for the protection of the people of our community. I do not mean to belittle "truth in lending", or the other protections of the bill, but my experience here convinces me and convinces my fellow attorneys from the program, that mere disclosure is not adequate protection, and that there is the evil of garnishment which makes the oppression of the poor possible.

By and large, the poor of our community have not the same freedom of choice in purchasing as many other segments of our community. They lack the knowledge of the competitive sources, they lack transportation facilities, they are lured by promises of bargain rates, they consistently pay more for merchandise of lower quality, both in food and in household furniture and goods, then other segments of our community, and are deliberately lured into extending themselves beyond their own credit capabilities. We can see from our bankruptcy practice in Detroit, that the results of these problems and the cycle generally goes as follows:

A family will buy furniture beyond which it can afford on credit, usually for a higher price than the goods are worth, and for unreasonable credit rates; then having over-extended themselves, will, because of layoffs or family illness, be unable to meet the payments. They then borrow from the small loan finance companies where the interest rates are even greater and it is garnishment which then boxes them further into this trap from which there is no proper escape.

Even bankruptcy is not an adequate remedy. In the first place, it is not fair to the sellers, in the second place, it is available only once each six years, and in the third place and most serious difficulty, sellers and lenders in our area habitually sue the bankrupt after the completion of the bankruptcy proceedings, for fraud in obtaining the credit initially, and are usually successful. Thus, the buyer finds himself helplessly meshed in this trap, owing the credit merchant and the finance company and unable to meet his obligations as they come due and is threatened with garnishment which will cost him his job with no possible way out.

I would like very much to have appeared before your committee and testified as to the problems existing in our community, but it seems that there was not sufficient available time before your Committee. I hope you will consider this letter as my testimony and distribute it to the membors of your committee.

Perhaps even stronger testimony than mine could be, was the response of the citizens of our community to the dispair which this sort of trap has led them into. Certainly, one of the large factors in causing the recent riots in our community was precisely this problem. It is significant to note as you travel down the ravaged streets of our community, that the three major types of stores which were looted and burned, frequently standing next to untouched business places, were grocery stores (where the prices were high and quality low), credit furniture stores and pawn shops. Several of the stores which were burned caught fire from the credit records being burned by desperate people in an improper attempt to avoid a despairing trap. Something must be done to give these people, most of whom are really trying hard, a better alternative than burning the credit records of our stores. And I feel that the garnishment provision of your bill is the greatest step possible in that direction.

Just two additional brief comments:

It has been our experience here in Michigan that maximum rates allowed in legislation quickly become the standard minimum rates, as has been indicated both by our small loan act and our consumer credit act. Secondly, the warning of amount as stated in your bill will probably be effective for a large mass of intelligent consumers but again, will not be effective for the uneducated, impoverished consumer who really has no alternative anyway. However, best wishes for your success with what in my judgment is one of the most important pieces of legislation ever to be presented to Congress, and one of the most needed in our country to prevent a repetition of the recent anger of our urban centers.

Very truly yours,

JOHN HOUSTON.

COUNCIL OF MUTUAL SAVINGS INSTITUTIONS,
New York, N.Y., August 25, 1967.

Hon. LEONOR K. SULLIVAN,
House of Representatives,
Washington, D.C.

DEAR CONGRESSWOMAN SULLIVAN: This Council has consistently supported the so-called truth-in-lending bills as a matter of principle, and continues to do so. In light of the fact that our members are savings, building or homestead associations, we do have some questions of interpretation with respect to this bill, as follows:

1. Paragraphs (1) and (2) of subsection (d) of Section 202 exclude from the definition of "finance charge," the items which, in first mortgage lending, are commonly termed "disbursement." To an increasing degree, however, institutions such as comprise our membership have portions of these operations performed by salaried personnel. Instances are salaried appraisers and an internal legal staff. Might not some provision be made for such cases?

2. It would also seem that some provision should be made for overhead in processing, which is not conducted for profit. To illustrate: The allowable charges permitted by the Veterans Administration in the case of a mortgage loan under the terms of the Servicemen's Readjustment Act is described as "1% plus disbursements." The Veterans Administration further allows an additional 2% for overhead in processing construction loans. I believe the Federal Housing Administration did or does employ a similar scale. In the State of New York, which has a 6% usury law, the courts have recently held that 2% was a reasonable charge for overhead and did not come within the purview of the usury statute.

3. This is not a question. I wish to make it clear that these questions do not relate to discounts, frequently called "points," which we recognize as being an added finance charge and, hence, clearly subject to the provisions of subsection (c) of Section 203.

4. We do have a question with respect to subsection (g) of Section 203, which waives disclosure of items substantially similar to those required by this bill. Might this not be extended to cover Federal requirements? For instance, Section 545.6–10 of the Rules and Regulations for the Federal Savings and Loan System provides that "Upon the closing of the loan, the association shall furnish the borrower a loan settlement statement showing in detail the charges or fees the borrower has paid or obligated himself to pay to the association or to any other person in connection with such loan; and a copy of such loan settlement statement shall be retained in the records of the association." I am informed that a similar requirement is imposed by some of the state supervisory authorities. A related question is as to who is to make the determination that such a requirement, however it may be phrased, is "substantially similar?"

5. Might it not prove feasible, either to revise subsection (g) or to provide in a separate subsection, an exception for supervised financial institutions which are required, upon the making of a first mortgage loan, to furnish the borrower with a complete settlement statement in a form simliar to that described in the regulation quoted above? In that connection, I am reminded (although I do not have its regulations at hand) that the Veterans Administration imposes a similar requirement with respect to every first mortgage G.I. loan.

Please understand that this Council supports the principle of full disclosure and that, in posing these questions, we are not seeking a favored position, but

that we understandably wish to avoid a duplication of existing requirements and added paper work, where the substance is covered by another route.

Cordially yours,

GEORGE L. BLISS,
President.

AUGUST 24, 1967.

Hon. LEONOR K. SULLIVAN,
Chairman, Subcommittee on Consumer Affairs, House Committee on Banking and Currency, Rayburn House Office Building, Washington, D.C.

DEAR CONGRESSWOMAN SULLIVAN: We are writing to you on behalf of the American Life Convention and the Life Insurance Association of America, two associations with a joint membership of 349 companies accounting for approximately 92% of the life insurance in force in the United States.

We did not request an opportunity to appear before your Subcommittee during the current hearings on the proposed Consumer Credit Protection Act (H.R. 11601, H.R. 11602, S.5). However, we wish to go on record with respect to the proposed legislation as it would apply to real estate mortgage loans.

We find merit in the recommendation made to your Subcommittee by Federal Reserve Board Governor, J. L. Robertson, that an exemption should be provided for first mortgage loans on real estate. We concur in the finding of the Senate Committee on Banking and Currency that adequate disclosure is already being made in this area of credit. (Senate Report 392).

Accordingly, we urge that first mortage real estate loans be exempted from any bill which your Subcommittee may favorably recommend.

It will be appreciated if this letter could be made a part of the hearing record.

Sincerely,

AMERICAN LIFE CONVENTION,
ARTHUR S. FEFFERMAN, *Director of Economic Analysis.*
LIFE INSURANCE ASSOCIATION OF AMERICA,
RALPH J. MCNAIR, *Vice President.*

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON CONSUMER AFFAIRS OF THE
COMMITEE ON BANKING AND CURRENCY,
Washington, D.C., August 25, 1967.

MR. ARTHUR S. FEFFERMAN,
Director of Economic Analysis,
American Life Convention,
MR. RALPH J. MCNAIR,
Vice President,
Life Insurance Association of America,
Washington, D.C.

DEAR MR. FEFFERMAN AND MR. MCNAIR: The letter you have submitted to me for inclusion in the record of the hearings on H.R. 11601 and related bills merely expresses the opposition of your two organizations to the inclusion of first mortgage credit under the legislation. Since you are familiar with the statement made by the witness from the Federal Reserve Board of Governors, Mr. James L. Robertson, which you mentioned in your letter, I am wondering if you are also familiar with the extensive testimony we received on the other side of this issue from Under Secretary of the Treasury Barr, Miss Betty Furness, the Secretary of Commerce, the Administrator of the Small Business Administration and other witnesses.

It is true that most first mortgage loans are issued by legitimate financial institutions which make full disclosure as to the terms and the rate of interest, but we are deeply concerned over the transactions which also occur in the first mortgage field by unscrupulous operators who, under the terms of S. 5 as it passed the Senate, would not have to make any disclosure whatsoever of any charges they make as long as the instrument used in the transaction could be defined as a "first mortgage."

My purpose in writing this letter is to ask if there is any reason why you would exempt from the disclosure requirements the kind of first mortgage frequently obtained by what some of our witnesses referred to as "the suede shoe boys"

who sell an elderly couple or widow an expensive furnace or siding or roofing job at unconscionable finance terms and have a piece of paper which can be filed as a first mortgage.

I am sure any first mortgages entered into by correspondents for life insurance companies are not guilty of such practices; thus, I cannot see why the industry would object to coverage under the legislation, particularly if such coverage were to make possible the prevention of the abuses which now occur in mortgages offered by the unscrupulous operators.

Sincerely yours,

LEONOR K. SULLIVAN,
Chairman.

SEPTEMBER 1, 1967.

HON. LEONOR K. SULLIVAN,
Chairman, Subcommittee on Consumer Affairs, House Committee on Banking and Currency, Rayburn House Office Building, Washington, D.C.

DEAR CONGRESSWOMAN SULLIVAN: Thank you for your letter of August 25 in regard to the treatment of first mortgage credit under H.R. 11601.

In our letter to your of August 24 urging that first mortgage real estate loans be exempted from any bill which your Subcommittee may favorably recommend, we had in mind first mortgages arising in connection with the unpaid purchase price of real estate. Since, as is generally agreed, adequate disclosure is already being made with regard to these mortgages, we believe that it would not be desirable to subject them to mandatory disclosure under the pending legislation. We have no objection to requiring disclosure of information for mortgages resulting from home repairs and purchases of appliances, if this has been found to be an area of abuse. However, we would hope that any legislation designed for this purpose could be drafted to apply only to the abuse areas and not to first mortgages generally. To apply the mandatory disclosure provisions to all first mortgages would detract from the effectiveness of the legislation by applying the requirements to areas where they are not needed and would not accomplish any useful purpose.

We are grateful to you for your letter and very much appreciate this chance to enlarge upon our views to you on this important subject.

Sincerely,

AMERICAN LIFE CONVENTION,
ARTHUR S. FEFFERMAN, *Director of Economic Analysis.*
LIFE INSURANCE ASSOCIATION OF AMERICA,
RALPH J. MCNAIR, *Vice President.*

THE COMMONWEALTH OF MASSACHUSETTS,
DEPARTMENT OF THE ATTORNEY GENERAL,
Boston, September 14, 1967.

HON. LEONOR SULLIVAN,
Chairman, Subcommittee on Consumer Affairs, Committee on Banking and Currency, House of Represetatives, Washington, D.C.

DEAR REPRESENTATIVE SULLIVAN: At the time of my appearance on August 11 before your committee in support of H.R. 11601, Representative Lawrence G. Williams asked me to make a comparison between Massachusetts truth in credit laws and the proposed Federal Consumer Credit Protection Act (H.R. 11601).

The basic objective of both Massachusetts laws and H.R. 11601 is safeguarding the consumer with reference to credit transactions by requiring full disclosure of finance charges. I believe both laws achieve this objective. There are, however, some areas of difference between the Massachusetts Retail Installment Act (G.L. Chapter 255D) and Truth in Lending Act (G.L. Chapter 140A) and H.R. 11601. They are as follows:

1. Finance Formula

Under Massachusetts General Laws, Chapter 255D Section 1, the annual finance charge formula is based on a constant ratio approach while under H.R. 11601 an actuarial method is provided for.

2. Motor Vehicles

Under Massachusetts General Laws, Chapter 255D Section 1, the term "goods" includes all things movable purchased primarily for personal, family or household purposes other than motor vehicles, which are covered by a separate law in Massachusetts. H.R. 11601 Section 202c does not appear to exclude motor vehicles from its scope of operation.

3. Cancellation of Agreement

Massachusetts General Laws, Chapter 255D Section 14 allows the consumer to cancel his retail installment agreement other than for a breach by the seller, where the seller has failed to send a written copy of the agreement signed by the seller to the consumer or where there has been no substantial performance on the seller's part. Notice of cancellation must be given by certified mail by five o'clock post meridian on the next business day following execution of the agreement.

4. Security Interests

Massachusetts General Laws, Chapter 255D Section 15 provides that the retail agreement shall create no security interest in the property of the purchaser other than on the goods sold under the agreement.

5. Protection for Buyer

Massachusetts General Laws, Chapter 255D Section 10 provides that no seller, sales finance company or holder shall at any time take or receive any retail installment sale agreement from a buyer which contains:

(1) Blank spaces for terms required by this chapter or for terms upon which the parties at the consummation of the sale have agreed to the extent of the then available information except that items 10 and 11 of subsection C of section 9 must always be disclosed;

(3) Any schedule of payments under which any one installment, except the down payment, is not equal or substantially equal to all other installments, excluding the down payment, or under which the intervals between any consecutive installments except the down payment differ substantially, unless (a) the buyer is given an absolute right upon default in any such excess or irregular installments, including that in default, revised to conform in both amounts and intervals to the average of all preceding installments and intervals, or (b) unless the time and amounts of the buyer and a statement appears in the contract to that effect.

9. Regulation of Credit for Commodity Future Trade:

Our Truth in Credit laws do not cover the amount of credit that may be extended under commodity future contracts as provided for H.R. 11601 Section 207.

10. Emergency Control of Consumer Credit:

Our credit law is in no way tied in with the economic condition of the state of Massachusetts or the county as provided in H.R. 11601, Section 208.

11. Interest Rate on Loans:

H.R. 11601 applies to all extensions of credit. In Massachusetts we have one regulation covering retail installment agreement and another which regulates the loan businesses of Massachusetts. Our Truth in Lending Laws, Massachusetts General Laws Chapter 140A, however, does not establish the rates for loans, but merely regulates the procedure under which loans are to be made. The rate setting power is in the hands of a state regulatory board.

I hope this report will be of help to you in evaluating whether H.R. 11601 provides sufficient protection for the consumer.

Very truly yours,

ROBERT L. MEADE,
Chief, Consumer Protection Division.

APPENDIX A

(The following agency reports on H.R. 11601 were received for inclusion in the record:)

SECURITIES AND EXCHANGE COMMISSION,
Washington, D.C., July 27, 1967.

Re: H.R. 11601, 90th Congress.

Hon. WRIGHT PATMAN,
Chairman, Committee on Banking and Currency,
House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your letter of July 22, 1967 requesting the Commission's comments on the above bill.

From our analysis of the bill it appears that under Section 203(n)(2) "transactions in securities or commodities in accounts by a broker-dealer registered with the Securities and Exchange Commission" would be exempt from the regulatory provisions of the bill which would apply to other parties who extend consumer credit. Since this exempted area is the only one in which the Commission has any direct or substantial concern with the extension of credit and since the bill would apparently not have any impact on any other aspects of the laws which the Commission administers, we do not care to comment on it.

Time has not permitted formal submission of our position on this bill to the Bureau of the Budget but we have been in touch with the Bureau by telephone and are advised informally that the Bureau has no objection to our position.

Notwithstanding our decision not to comment on this bill, we do appreciate your affording us the opportunity to consider it.

Sincerely yours,

HUGH F. OWENS, *Commissioner.*

THE GENERAL COUNSEL OF THE TREASURY,
Washington, D.C., July 31, 1967.

Hon. WRIGHT PATMAN,
Chairman, Committee on Banking and Currency,
House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN: Reference is made to your request for the views of this Department on H.R. 11601, the proposed Consumer Credit Protection Act.

Title I of the proposed legislation is essentially a revised version of S. 5 which has passed the Senate and is now pending before your Committee. This title would add a new title II to the Federal Reserve Act. Most of the provisions in sections 201–206 of the proposed title II relating to disclosure of the cost of credit are similar to the provisions of the Senate-passed version of S. 5, with the following notable exceptions: (1) Section 203(d) of the proposed title would require disclosure of an annual percentage rate of a finance charge rather than a percentage rate per period with regard to open-end credit plans or revolving credit. (2) The exemptions which S. 5 would provide for transactions involving less than $10 in credit charges and first mortgages in real estate transactions are omitted from H.R. 11601. (3) Subsections (j) and (k) of section 203 would extend certain disclosure provisions, including the requirement to set forth the finance charge, expressed as an annual percentage rate, to any advertisement of consumer credit. (4) The provisions of the proposed title would take effect on July 1, 1968 rather than on July 1, 1969.

The remainder of title I of the bill would make substantive changes unrelated to the disclosure of finance charges, which is the subject matter of S. 5. Section 203(1) would prohibit any finance charge for credit to natural persons which exceeds 18 percent. Section 203(m) would prohibit notes authorizing the confession of judgment against a debtor. Section 207 of the proposed title II would direct the Board of Governors of the Federal Reserve System to prescribe regulations governing the amount of credit that may be extended or maintained on commodity futures contracts. Section 208 would provide the Board with standby authority to restrict or control the use of consumer credit whenever the President determines that a national emergency exists. Section 209 would give the Board certain powers of administrative enforcement with regard to violations of the title.

Title II of the bill would prohibit the attachment or garnishment of wages or salary due to an employee.

Title III of the bill would establish a bi-partisan National Commission on Consumer Finance. The Commission would be composed of nine members: three members of the Senate appointed by the President of the Senate, three members of the House of Representatives appointed by the Speaker, and three persons appointed by the President. The Commission would study and appraise the functioning and structure of the consumer finance industry, and would be required to report to the President and the Congress, by December 31, 1969. The report would include treatment of (1) the adequacy of existing arrangements to provide consumer financing at reasonable rates; (2) the adequacy of existing supervisory and regulatory mechanisms to protect the public from unfair practices; and (3) the desirability of Federal chartering of consumer finance companies.

In his message to the Congress on February 16, 1967, on consumer protection, the President said:

"I recommend the Truth-in-Lending Act of 1967 to assure that, when the consumer shops for credit, he will be presented with a price tag that will tell him the percentage rate per year that is being charged on his borrowing.

"We can make an important advance by incorporating the wisdom of past discussions on how the cost of credit can best be expressed. As a result of these discussions, I recommend legislation to assure—

"Full and accurate information to the borrower; and Simple and routine calculations for the lender."

The original version of S. 5 would have required all revolving credit plans to disclose the annual percentage rate at the time the account was opened and on the periodic monthly statements. In the report dated April 12, 1967, to the Senate Banking and Currency Committee on S. 5, this Department fully endorsed the principle that the total cost of obtaining credit should be clearly disclosed to a potential user, both in terms of dollars and annual rate. Also, the original S. 5 would not have provided exemptions for small credit transactions and first mortgages.

S. 5 as passed by the Senate would allow such exemptions and would allow the interest rate on most revolving accounts to be stated on a monthly rather than annual basis. Thus, for example, in most instances, a creditor could state the rate on purchases charged to a revolving account at 1.5 percent a month rather than 18 percent a year.

The Department believes that all types of creditors and all types of credit transactions should be treated equally and impartially to the greatest extent possible. Accordingly, the Department supports the proposed provisions of H.R. 11601 which would require disclosure of an annual percentage rate by all creditors without exceptions or special treatment for revolving credit, transactions involving less than $10 in credit charges, and first mortgages. We also support the provisions which would extend the disclosure of credit costs to advertising. We believe that these provisions would more fully implement the recommendations of the President with regard to disclosure of finance charges.

In addition, the Department would have no objection to a comprehensive study of the consumer finance industry. However, it would appear that such a study could best be accomplished by an existing agency of the Federal Government or by the Congress. We believe that those other provisions of H.R. 11601 which are not related to the disclosure of the cost of credit should receive extensive study and that their consideration by your Committee at this time should not be permitted to delay action on effective truth-in-lending legislation. Those provisions, however, would appear to be proper topics for study.

The Department has been advised by the Bureau of the Budget that there is no objection to the submission of this report to your Committee and that enactment of legislation to provide full disclosure of credit charges would be in accord with the program of the President.

Sincerely yours,

FRED B. SMITH,
General Counsel.

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM,
Washington, July, 31, 1967.

Hon. WRIGHT PATMAN,
Chairman, Committee on Banking and Currency,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your request for the Board's comments on H.R. 11601, the "Consumer Credit Protection Act."

Most of title I of the bill is designed to provide consumers with meaningful information concerning the costs and terms of credit. The Board believes that legislation of this kind is needed, and that important social and economic benefits may be expected to flow from its enactment. With one exception, however, we believe that the disclosure provisions of S. 5 are preferable to those of H.R. 11601.

The Board believes that the provisions of H.R. 11601 as to open end credit plans are preferable to those in S. 5 as passed by the Senate. The need for a common standard to facilitate comparison shopping for credit, as well as the desirability of treating all creditors alike, argue against the Senate bill's provisions exempting certain forms of open end credit from the general rule requiring disclosure of equivalent annual rates.

In addition to disclosure provisions similar to S. 5, H.R. 11601 provides for regulation of credit advertising affecting interstate commerce, ceilings on finance charges, controls on commodity futures trading, and prohibitions against particular methods of debt collection. Presumably because of the broad scope of these provisions, section 209 of the bill incorporates authority for their enforcement through administrative proceedings leading to cease and desist orders. The Board has urged that its responsibility as to legislation requiring disclosure of credit terms be limited to prescribing implementing regulations, and that responsibility for enforcement and investigation of complaints be lodged in another agency with a trained investigative staff.

The Senate concurred in our recommendation as to the Board's role in implementing S. 5. As to enforcement, it was decided not to establish "investigative or enforcement machinery at the Federal level, largely on the assumption that the civil penalty section will secure substantial compliance with the Act (S. Report 392, p. 9)." We hope that civil sanctions, supplemented, as they are, by criminal sanctions, will prove to be adequate to assure compliance with disclosure requirements. If experience under the legislation should indicate that compliance is not being achieved, the Board would so indicate in the annual reports provided for in the bill. If, however, the Congress now determines that adequate protection for consumers warrants imposition of the broader controls embodied in H.R. 11601 in addition to the disclosure requirements of S. 5, responsibility for their administration and enforcement should be vested elsewhere than in the Federal Reserve System.

The question of whether certain of the controls added to S. 5 by H.R. 11601 are desirable is now under study by the Government agencies directly concerned. We understand that the Department of Agriculture is now reconsidering its earlier request for standby authority to prescribe margin requirements for trading in the commodity futures markets, pending analysis of additional information which it has recently received. And the President has directed the Attorney General, in consultation with the Secretary of Labor and the Director of the Office of Economic Opportunity, to make a comprehensive study of the problems of wage garnishment. The Board believes that decisions on these questions should be deferred until the results of these studies are available.

A Federal limitation on finance charges, as provided in H.R. 11601, could operate to deny credit to those who need it under certain circumstances, and to raise credit costs in other instances. A single, national statutory ceiling cannot adequately reflect the varying elements—such as risk, costs, and size of transaction—that enter into the determination of finance charges for various kinds of

credit arrangements. In some small transactions, finance charges that are low in dollar amount but exceed 18 per cent when converted to an annual percentage rate may be justified to compensate the creditor for relatively high out-of-pocket handling costs. Under those circumstances, an 18 per cent ceiling could cut off extensions of credit. For other kinds of credit needs that can be met at lower rates, an 18 per cent ceiling might tend to become a floor as well as a ceiling, resulting in higher costs to the borrower. We agree with the principle expressed in the Senate Banking and Currency Committee's report on S. 5, that "full disclosure of credit charges (should) be made so that the consumer can decide for himself whether the charge is reasonable (S. Report 392, p. 1)."

Another provision of H.R. 11601 would grant to the Board authority to impose broad controls over the use of consumer credit upon a determination by the President that a national emergency exists which necessitates such action. The Board believes that standby authority of this kind could prove useful under certain conditions, although it clearly is not needed at present. We do not regard this authority. However, as a method of protecting consumers. Rather, it is a means of curbing consumer demands at times of unusual stress when the economy could not satisfy those demands and at the same time meet higher-priority needs such as the defense of the nation. As was demonstrated only last year, authority for consumer credit controls is also a controversial matter. We hope, therefore, that your Committee will act favorably on disclosure legislation without jeopardizing its enactment by inclusion of this additional authority.

Sincerely yours,

WM. MCC. MARTIN, JR.

DEPARTMENT OF AGRICULTURE,
Washington, D.C., August 3, 1967.

Hon. WRIGHT PATMAN,
Chairman, Committee on Banking and Currency,
House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN: This is in reply to your request of July 22, 1967, for a report on H.R. 11601, the "Consumer Credit Protection Act."

This Department endorses the provisions of this bill requiring disclosure of the cost of credit.

The bill provides for full disclosure of, and maximum rates for, finance charges to consumers, authorizes regulations of credit for commodity futures trading, provides machinery for controlling credit during national emergencies, prohibits garnishment of wages, and creates a commission to study the need for further regulation of the consumer finance industry.

Farmers, as well as others, are entitled to know the actual annual percentage rate for the cost of credit incurred in the purchases of goods and services. We believe the proposed legislation can combat ignorance and exploitation in the field of credit and save farmers many millions of dollars annually. This Department defers to the Department of Treasury for comment on the details of procedures for disclosure of the cost of credit.

Section 201(b) and Section 207 of H.R. 11601 are concerned with the regulation of speculation and the use of credit in trading on commodity futures contracts. In the past this Department has advocated regulation of margin requirements on commodity futures transactions when excessive speculation is causing undue price fluctuations. In line with our concern we have recently commissioned a study related to this question. Pending a careful analysis of this study we are not in a position to make a judgment with respect to these provisions of the bill. We suggest that these provisions, and others not related to the disclosure of credit charges, be considered separately following a thorough study of the problems they pose.

The Bureau of the Budget advises that there is no objection to the presentation of this report from the standpoint of the Administration's program, and that enactment of legislation to provide for full disclosure of credit charges would be in accord with the President's program.

Sincerely yours,

ORVILLE L. FREEMAN.

SMALL BUSINESS ADMINISTRATION,
Washington, D.C., August 4, 1967.

Hon. WRIGHT PATMAN,
Chairman, Committee on Banking and Currency,
House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN: This is in reply to your letter of July 22, requesting the comments of this Agency on H.R. 11601, the "Consumer Credit Protection Act."

Congressman Leonor Sullivan, in her introductory remarks on the floor of the House on July 20, noted that many sections of this bill are controversial, but stated that it was being introduced with its multiplicity of titles "for the purpose of outlining and dramatizing the scope of this (consumer credit) issue, and as a vehicle for hearings."

The principal title of H.R. 11601 is its Title I, on "Credit Transactions"; and the principal provision therein, in our estimation, is that regarding credit disclosure. This Agency has gone on record as having strongly favored S. 5, the Senate-passed "truth in lending" measure. We therefore take this occasion to reiterate our support for the type of consumer protection which mandatory disclosure of finance charges will afford.

Mrs. Sullivan has likewise suggested that the additional and admittedly controversial features of her bill "will not be permitted to stymie effective 'Truth-In-Lending' legislation," now that that measure has already been passed by the Senate. The Small Business Administration would favor just such a balance of priorities, and would hope that—whatever the fate of the bill's other parts—a credit disclosure measure will be enacted.

The bill would also prohibit the garnishment of wages in any situation. Mrs. Sullivan's press release on the bill state the following rationale:

". . . the garnishment of wages is frequently an element in the predatory extension of credit and . . . such garnishment frequently results in the disruption of employment, production, and consumption, constituting a substantial burden on interstate commerce."

Garnishment is very often the only legitimate means in the employ of a businessman-creditor for final satisfaction of business debts due him. With regard to this section of the bill, then, as well as that proposing a National Commission on Consumer Finance, we would recommend very careful consideration before any action is taken thereon.

The Bureau of the Budget has advised that there is no objection to the submission of this report, and that enactment of legislation to provide full disclosure of credit charges would be in accord with the President's program.

Sincerely yours,

ROBERT C. MOOT, *Administrator.*

THE WHITE HOUSE,
Washington, August 4, 1967.

Hon. WRIGHT PATMAN,
Chairman, Committee on Banking and Currency, House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN: This report is in reply to your request for the comments of this office on H.R. 11601, a bill to safeguard the consumer in connection with the use of credit under prescribed conditions of disclosure and for other purposes. The bill is to be known as the "Consumer Credit Protection Act."

The bill would amend the Federal Reserve Act by adding a Title II providing for full disclosure in consumer credit transactions including advertising, a national usury law and other particulars, including the provisions of S. 5, 90th Congress, as passed by the United States Senate, but going beyond the scope of the latter bill. Among other things, H.R. 11601 also provides for the prohibition of the garnishment of wages and the establishment of a national commission on consumer finance to examine and evaluate the consumer finance industry.

Section 201 recites the need for full disclosure of consumer credit terms, a requirement to regulate the speculation and excessive use of credit in commodity futures contracts and the advisability of establishing a stand-by authority for the emergency control of consumer credit.

The definitions of Section 202 follow generally the definitions of S. 5, 90th Congress, dated July 12, 1967, except for the following additional beneficial changes for the consumer.

The definition of "finance charge" (Sec. 202(d)) includes, among other important items, the cost of any guarantee or insurance protecting the obligor's default or other credit loss. Current news reports, testimony in the Congress, as well as hearings held in several of the States, report excessive premiums charged consumers for credit insurance and illustrate the opportunity to increase the yield to the creditor at the expense of the debtor by saddling him with such high cost additions. Credit insurance amounts frequently to a substantial additional cost to the debtor when obtaining credit. Therefore, to provide true comparability as between creditors' rates, credit insurance should be an itemized and included as a line item cost factor in determining the total finance charge. H.R. 11601 provides an adequate standard of full disclosure that will be of material assistance to the prospective debtor in his quest for the most desirable or economical source of credit.

The definition section of H.R. 11601 has also strengthened the full disclosure principle by permitting no exceptions to stating finance charges on annual percentage rate basis on the grounds that some credit accounts are "installment open-end plans" as now permitted in the Senate bill. We think it important to prohibit such exceptions. While revolving credit now represents a relatively small proportion of the total consumer debt, it is growing and with such a loophole, it may burgeon even more rapidly by businesses seeing the advantage of avoiding full disclosure by converting to this form of credit plan. Treasury Department officials and others, including Massachusetts bussinessmen, have shown that revolving charge accounts can be accommodated to the system.

Section 203 requires the disclosure of finance charges as defined in Section 202 and parallels the excellent disclosure provisions of S. 5, 90th Congress, dated July 12, 1967, but with some added improvements.

First, credit charges under $10 are not excluded from the coverage of the bill. We think it important to have no exceptions by degree of the amount involved, for it is in this area that the poor and disadvantaged are subject to abuse. Their small purchases can, in the aggregate, be burdened with excessive credit charges. They are citizens to whom the cost of $5 worth of credit is just as important, if not more so, than a $50 credit charge to a more affluent member of society. If sales taxes can be readily computed on small amounts, so can the annual percentage rate.

Of great significance to consumers is the language of subsections 202(i), 203(j), and 203(k), which provide that creditors advertising and consumer credit sale in interstate commerce, extension of credit or open-end credit plan, must clearly set out the details of the offer to include the cost of the finance charge expressed as an annual rate. This requirement of H.R. 11601 allows the consumer to begin his shopping for credit at home rather than at the store. Full disclosure of terms when the family is discussing the advisability of using credit in the privacy of the home is surely more conducive to the wise use and selection of credit sources. Full disclosure in advertising should increase competition with resulting benefits to both the creditor and the borrower. Hopefully, with respect to the latter, the credit charges of the high rate lenders will tend to lower.

Section 204 provides guidelines for the issuance of regulations by the Board and includes provisions for coordination with other Federal agencies and the establishment of an Advisory Committee. We think these features of the bill will aid in providing improvements in the administration of the Act in the years ahead.

Section 205 preserves the laws of the States to the extent they are not inconsistent with the bill and appears to take cognizance, among other things, of the concern of some to preserve the time-price doctrine.

In paragraph (3) of Section 206(a) on page 23 at line 7, the time for bringing a court action is limited to one year. It is recommended that the statute of limitations be extended to four years since the laws of several States run to four years. Moreover, a long limitation period is advisable in the interests of the consumer.

Section 209 provides for administrative enforcement of Title II. The agency responsible for enforcement of this bill should have appropriate powers in order to curb the acts of the unscrupulous few. Otherwise, the benefit of this bill might well be illusory to the consumer. The drafters of H.R. 11601 are to be especially commended for making it possible for the administering agency to bring an action on behalf of the consumer by serving a complaint, stating its

charges, and then calling a hearing. Often today, the consumer is unable, does not know how, or cannot afford the cost of pursuing a claim against the creditor.

This Committee believes that several portions of H.R. 11601 are worthy of study although they do not specifically relate to the full disclosure provisions of that bill. This office recommends that the subjects advanced in subsection 203(l), calling for a national usury law; in subsection 203(m), which would outlaw the cognovit note; and Title II, which would prohibit the garnishment of wages, all be deferred for further study. Their individual significance for American consumers certainly merits full attention and complete analysis.

The cognovit note, or confession of judgment against the debtor is a creditor's remedy which is now prohibited in some States. This practice has often been used by creditors to the detriment of the legal position of consumers. The President's Committee strongly urges that it be the subject of further study so that its full implications can be completely evaluated.

Title II of the bill would prohibit the garnishment of wages. This office believes that at present garnishment as it affects debtors, employers, and creditors should also be the subject of intensive investigation. Therefore, we welcome the study now being conducted by the Attorney General, the Secretary of Labor, and the Director of the Office of Economic Opportunity. It is our hope and expectation that the study will point the way to a proper and equitable solution to this problem which particularly affects low-income groups.

While this office believes that the objectives of Title III to study the consumer finance industry are laudable, we also believe that such a study should be separated from H.R. 11601. It could provide valuable data and suggestions for action in such areas as deficiency judgments, unconscionable contracts, licensing requirements and debtors' remedies. However, we should first determine if the study can be better and more economically performed by an existing agency.

Therefore, since it is our desire to advance the full disclosure portions of H.R. 11601, we wish to strongly support all such provisions of the bill. The legislative philosophy of H.R. 11601, which recognizes that the consumer, to effectively fulfill his role in the marketplace, must be an informed consumer, is in full accord with the viewpoint of the President's Committee on Consumer Interests.

The Committee has been advised by the Bureau of the Budget that there is no objection to the submission of this report to your Committee and that enactment of legislation to provide full disclosure of credit charges would be in accord with the program of the President.

Sincerely,

HOWARD FRAZIER,
(For Betty Furness, Special Assistant to the President for Consumer Affairs).

DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE,
August 4, 1967.

Hon. WRIGHT PATMAN,
Chairman, Committee on Banking and Currency,
House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN: This letter is in response to your request of July 22, 1967, for a report on H.R. 11601, a bill "To safeguard the consumer in connection with the utilization of credit by requiring full disclosure of the terms and conditions of finance charges in credit transactions or in offers to extend credit; by establishing maximum rates of finance charges in credit transactions; by authorizing the Board of Governors of the Federal Reserve System to issue regulations dealing with the excessive use of credit for the purpose of trading in commodity futures contracts affecting consumer prices; by establishing machinery for the use during periods of national emergency of temporary controls over credit to prevent inflationary spirals; by prohibiting the garnishment of wages; by creating the National Commission on Consumer Finance to study and make recommendations on the need for further regulation of the consumer finance industry; and for other purposes."

The bill, which is considerably more comprehensive than bill S. 5, would provide for the full disclosure of the terms and conditions of credit in connection with consumer credit transactions by requiring each creditor to furnish to each borrower information in accordance with regulations prescribed by the Board of Governors. In the case of consumer credit sales and extension of credit the

creditor would be required to furnish the details of the transaction including the total amount to be financed, the amount of the finance charge expressed as an annual percentage rate, the number, amount and due dates or periods of payments scheduled to repay the indebtedness and the default, delinquency or similar charges payable in the event of default. With respect to open-end credit plans, the creditor shall disclose to the person to whom credit is extended information concerning the conditions under which a finance charge may be imposed, the method of determining the balance upon which a finance charge will be imposed, the method of determining the amount of the finance charge, the annual percentage rate of the finance charge and in the case of an installment open-end credit plan, the equivalent annual percentage rate and the conditions under which any other charges may be imposed.

H.R. 11601 also provides that no creditor may state or otherwise represent in any advertisement in or affecting interstate commerce that specific terms are available with the purchase of goods or services or the obtaining of a loan or the extension of credit under an open-end credit plan unless the advertisement clearly and conspicuously sets forth details including the finance charge expressed as an annual percentage rate or in the case of open-end credit plans the percentage rate per period and the annual percentage rate of the finance charge to be imposed.

The bill provides that no creditor may demand or accept any finance charge in connection with any extension of credit which exceeds the maximum rate under applicable State law or 18% per annum, whichever is less, and that no creditor may demand or accept in connection with any extension of credit any note or other document authorizing the confession of judgment against the debtor.

Regulation of credit for commodity futures trading by the Board of Governors is authorized by this bill and the Board is further authorized to issue regulations to control the extension of consumer credit whenever the President determines that a national emergency exists which necessitates such action.

Title II of the bill would outlaw the garnishment of wages by providing that no person attach or garnish wages or salary due an employee or pursue in any court any similar legal or equitable remedy which has the effect of stopping or diverting the payment of wages or salary due an employee.

Title III provides for the establishment of a National Commission on Consumer Finance, which shall study and appraise the functioning and structure of the consumer finance industry and make recommendations to the Congress.

In regard to the Department's Federal Credit Union Program the requirements of the bill for disclosure of finance charges as an annual percentage rate would not impose a burden upon Federal credit unions. From the beginning the Federal Credit Union Act has limited interest charges to a rate not exceeding 1 percent per month inclusive of all charges incident to making the loan. The conversion to an annual percentage rate would pose no problems. The requirements concerning the advertising would likewise present no difficulty for Federal credit unions.

While some Federal credit unions in some States utilize cognovit notes the prohibition of their use as prescribed in this bill would not be a hardship. Neither would the prohibition of the use of garnishments or wage attachments seriously adversely affect the operation of Federal credit unions.

In summary, we endorse the provisions of the bill which will provide the consumer with a full disclosure of the terms and conditions of finance charges and permit him to make an informed judgment concerning the use of credit. We have no comment on the other administrative and procedural aspects of H.R. 11601.

We are advised by the Bureau of the Budget that there is no objection to the presentation of this report from the standpoint of the Administration's program.

Sincerely,

WILLIAM J. COHEN,
Under Secretary.

EXECUTIVE OFFICE OF THE PRESIDENT,
OFFICE OF EMERGENCY PLANNING,
Washington, D.C., August 10, 1967.

Hon. WRIGHT PATMAN,
Chairman, Committee on Banking and Currency,
House of Representatives, Washington, D.C.

DEAR MR. CHAIRMAN: This is in reply to your request for an expression of the views of this Agency concerning H.R. 11601 of the 90th Congress, entitled "Consumer Credit Protection Act."

The primary responsibility of this Agency with respect to the stabilization of credit and similar measures involves the development of preparedness plans designed to be effectuated in the event of any extraordinary national emergency situation. However, most of the provisions of H.R. 11601 deal with safeguarding consumers in the use of credit as a general proposition and this proposed legislation is commonly referred to as the "Truth-In-Lending Bill." In view of the foregoing, we are restricting our comments concerning this bill to Section 208 which would provide express authority for the imposition of consumer credit controls in emergency situations.

Shortly before the U.S. entered World War II, President Roosevelt issued Executive Order No. 8843 which directed the Federal Reserve Board to impose controls on consumer installment credit. That Order was issued pursuant to Section 5(b) of the Trading with the Enemy Act. Pursuant to that authority the Board issued Rule W. The First War Powers Act approved and ratified actions taken pursuant to the Trading with the Enemy Act and broadened the scope of Section 5(b).

Section 5(b) of the Trading with the Enemy Act is now operative as a result of the National Emergency declared by the President in Proclamation No. 2914 of December 16, 1950. Consequently, it appears that adequate general standby emergency authority for the control of consumer credit now exists. Accordingly, we do not feel that more specific standby authority, such as Section 208, is needed at this time. If, however, the Congress decides to enact more specific standby consumer credit control legislation, we strongly recommend that no restriction, such as the restriction contained in the last sentence of Section 208 with respect to controlling real estate credit be included in such legislation.

The Bureau of the Budget advises that it has no objection to the submission of this report, and that enactment of legislation to provide full disclosure of credit charges would be in accord with the President's program.

Sincerely,

FARRIS BRYANT, *Director.*

U.S. DEPARTMENT OF LABOR,
OFFICE OF THE SECRETARY,
Washington, August 11, 1967.

Hon. LEONOR K. SULLIVAN,
Chairman, Subcommittee on Consumer Affairs, Committee on Banking and Currency, House of Representatives, Washington, D.C.

DEAR MADAM CHAIRMAN: This is in reply to your request for our comments on H.R. 11601, the proposed "Consumer Credit Protection Act."

The Department of Labor has long supported legislation requiring full disclosure of consumer credit financing charges, the terms and conditions of credit purchases and the annual percentage rate of the finance charge, as is proposed in Title II of this bill.

I regard disclosure of the terms and conditions of consumer credit as a first step in protecting consumers against excessive charges which many of them now pay because they do not understand the complex charges and calculations involved in these transactions. A clear itemization of all of the charges, including a statement of the annual percentage rate, would enable buyers more readily to compare terms and costs offered by various lenders and to seek the most advantageous terms. It would also provide a basis for more effective consumer education to avoid overuse of consumer credit.

H.R. 11601 differs in a number of important respects from S. 5 as it passed the Senate. This Department prefers the stronger provisions of H.R. 11601 which require the statement of an annual percentage rate rather than a periodic (i.e., monthly) rate on revolving credit accounts and which would not exempt credit charges of less than $10 or first mortgages on real estate from the requirement to disclose the annual percentage rate charged.

This Department also believe that "come-on" advertising which lures unwary customers by failing to disclose the true cost of credit has been an important factor in overextension of consumer credit, and should be curbed by appropriate measures.

The Department recognizes that disclosure of credit costs and terms is only a first step in consumer protection against abuses. It would welcome a comprehensive study of the problems of consumer financing but believes that the study

could be made more effectively by an appropriate agency of the Executive Branch or Committees of the Congress.

The Department is especially interested in two other provisions of this proposed Act which would affect wage earners directly—the prohibition of the garnishment of wages in Title II, and the prohibition of notes authorizing the confession of judgment against the debtor (cognovit notes) in Title I, Sec. 203 (m). Your Committee is to be commended for recognizing the gravity of this situation and bringing it to public attention by including it in H.R. 11601.

The loss of wages through garnishment has worked great hardship on wage earners and the growing number of personal bankruptcies has become a serious problem. As the President said in his message to Congress on the War on Poverty, delivered March 14, 1967, "Hundreds of workers among the poor lose their jobs or most of their wages each year as a result of garnishment proceedings." He stated that he was "directing the Attorney General, in consultation with the Secretary of Labor and the Director of the Office of Economic Opportunity, to make a comprehensive study of the problems of wage garnishment and to recommend the steps that should be taken to protect the hard-earned wages and jobs of those who need the income most." This study is now in progress and, although no final conclusions have been reached, I appreciate the opportunity you have given me to discuss this general problem before the Committee.

In summary, the Department of Labor strongly supports "truth-in-lending" legislation. It is our hope that final action can be taken in the present session on the provisions for the full disclosure of consumer credit charges which we have all sought for so long.

The Bureau of the Budget advises that it has no objection to the submission of this report from the standpoint of the Administration's program.

Sincerely,

W. WILLARD WIRTZ,
Secretary of Labor.

OFFICE OF THE DEPUTY ATTORNEY GENERAL,
Washington, D.C., August 18, 1967.

HON. WRIGHT PATMAN,
Chairman, Committee on Banking and Currency,
House of Representatives,
Washington, D.C.

DEAR MR. CHAIRMAN: This is in response to your request for the views of the Department of Justice on H.R. 11601, a bill entitled "Consumer Credit Protection Act."

The bill consists of four titles. Title I would require the disclosure in a simple form of actual finance charges or interest rates on credit extended to consumers. Title II would prohibit the attachment or garnishment of the salary of any employee. Title III would create a Commission on Consumer Finance to study and report to the Congress and the President on the functioning and structure of the consumer finance industry. Title IV contains a severability provision.

The Department of Justice favors the enactment of the provisions of Title I of the bill which are consistent with the "Truth-in-Lending" recommendations contained in the President's message "American Consumer Protection." (H. Doc. No. 57, 90th Congress)

Inasmuch as Titles II and III are not directly related to the purposes of this legislation, we recommend that they be separated from the bill in order that they not delay consideration of consumer credit disclosure legislation by your Committee.

The Department believes that the penalty provisions of the bill could be strengthened in two respects. Section 206(b) provides that any person who "knowingly and willfully" fails to make required disclosures shall be subject to criminal penalties. This requirement of specific proof of willfulness substantially increases the difficulty of establishing criminal violations of the Act. Where the nature of the acts prohibited is clearly defined in the statute, criminal intent may be presumed from the fact that the prohibited acts were committed. It is not a requirement of fairness or constitutionality that the Government prove specific intent to commit the acts prohibited by this bill in order to impose criminal penalties. Special proof of willfulness is not required in other welfare regulations enforced by criminal sanctions. See, e.g., the Federal Food Drug and Cosmetic Act, 21 U.S.C. 333(a).

Section 206(a) requires a plaintiff seeking recovery of a civil penalty to show that an offending creditor "knowingly" failed to disclose required information. The requirement of proof of specific knowledge, which the Department does not believe is required in a criminal proceeding, is certainly not required by fairness in a civil proceeding. The burden of proving specific knowledge by an offending creditor might frustrate prospective plaintiffs, and thereby weaken the enforcement provisions of the act.

The Bureau of the Budget has advised that enactment of legislation to provide full disclosure of credit charges would be in accord with the Program of the President.

Sincerely,

WARREN CHRISTOPHER,
Deputy Attorney General.

FEDERAL HOME LOAN BANK BOARD,
Washington, D.C., September 1, 1967.

HON. WRIGHT PATMAN,
Chairman, Committee on Banking and Currency,
House of Representatives.

DEAR MR. CHAIRMAN: In response to your request, the Federal Home Loan Bank Board submits this report on H.R. 11601 of the present Congress, which if enacted would become the Consumer Credit Protection Act.

This report is presented from the point of view of the functions now vested in the Board under Federal statute. The Board supervises the Federal Home Loan Banks, twelve in number, which provide reserve credit for their member institutions. All Federal savings and loan associations, which are chartered and supervised by the Board, are required to be members, and membership is extended on an optional basis to State-chartered associations and to savings banks and insurance companies engaged in making long-term home mortgage loans. The Board also administers the Federal Savings and Loan Insurance Corporation, which insures up to a statutory limit of $15,000 savings in all Federal savings and loan associations and in such State-chartered associations as apply and are admitted to insurance.

(1) Disclosure of Finance Charges. The bill would add to the Federal Reserve Act a new title II requiring disclosure of finance charges where credit is granted by a creditor to a person other than an organization and the debt is contracted by the obligor primarily for personal, family, household, or agricultural purposes. The Board strongly urges the enactment of legislation along the lines of these provisions.

It is desirable that there be clarity as to the effect of those provisions on loans by the institutions which are supervised by the Federal Home Loan Bank Board to individuals where the amount or rate of the finance charge may be uncertain. Although the incidence of these examples is small in relation to the total number of transactions affected by this legislation, an example of a loan having an uncertain amount or rate of finance charge would be construction loans which are to be disbursed in progress payments that can vary in timing with weather conditions and other factors, or loans which have an interest-rate adjustment or escalation clause. We are not entirely certain that the provisions of subsection (c) of the proposed new section 204 of the Federal Reserve Act are fully adequate for this purpose. We therefore suggest that at page 20, line 2, immediately before the period, language such as the following be added:

> ", or in the judgment of the Board are necessary or appropriate to accommodate the requirements of section 203 to the characteristics of the class of transactions dealt with".

We note that H.R. 11601 does not contain a provision analogous to subdivision (4) of section 8 of the Senate bill (S. 5) as passed by the Senate, which provides that the provisions of the act shall not apply to "transactions involving extensions of credit secured by first mortgages on real estate", the term "first mortgage" being defined in subdivision (i) of section 3 of that bill as meaning "such classes of first liens as are commonly given to secure advances on, or the unpaid purchase price of, real estate under the laws of the State in which the real estate is located". While the Board sees no impelling need for the inclusion of such mortgages in the disclosure provisions, it recognizes that such coverage is not unreasonable.

With respect to the disclosure compliance provision for extensions of credit other than consumer credit sales or transactions under an open-end credit plan, we suggest that at page 11, line 10, the language "in the note or other evidence of indebtdness to be signed by the obligor" be changed to read "in the contract or other evidence of indebtedness, or in the mortgage or other security instrument, to be signed by the obligor". We make this suggestion because it might be inadvisable, for reasons relating to negotiability, for such material to be included in the note or other evidence of indebtedness, as distinguished from the mortgage or other security instrument, which is to be signed by the obligor.

(2) Advertisement of Credit Terms. Subsection (j) of the proposed new section 203 of the Federal Reserve Act would prohibit any creditor (which term is defined in subdivision (e) of the proposed new section 202) from advertisement in or affecting interstate commerce that specific credit terms are available unless they are set forth as provided in the bill. Subsection (k) of said section 203 contains similar provisions as to open-end credit plans. The Board would favor such provisions.

(3) Usury. Subsection (l) of the proposed new section 203 would provide that no creditor may demand or accept any finance charge in connection with any extension of credit to a natural person which exceeds (1) the maximum rate or amount permitted under applicable State law or (2) 18% per annum, whichever is less. The base to which the 18% rate is to be applied (original amount, declining balance, or otherwise) is not clear, and no account is taken of minimum charges which might be perfectly legal under applicable State law but might produce a rate higher than the 18% rate. In the light of the foregoing, and without undertaking to consider the arguments which might be made for or against usury laws as a general matter, the Board recommends against enactment of this provision.

(4) Confession of Judgment. Subsection (m) of the proposed new section 203 provides that no creditor may demand or accept in connection with any extension of credit any note or other document authorizing the confession of judgment against the debtor. A ban on provisions for confession of judgment could cause difficulties in mortgage foreclosure in some jurisdictions. The Board recommends that this provision not be enacted.

(5) Control of Consumer Credit. The proposed new section 208 which the bill would add to the Federal Reserve Act would authorize the Board of Governors of the Federal Reserve System, whenever the President determines that a national emergency exists which necessitates such action, to issue regulations to control, to such extent as the Board of Governors deems appropriate, (1) the extension of consumer credit is specified respects, including among others the amounts, purposes, and maximum maturity, and such other elements "as may, in his [sic] judgment, require regulation in order to carry out the purposes of this title", (2) the extension of credit to finance directly or indirectly the extension of consumer credit, which controls "may be related to the borrower's financial history, or to the lender's other loans and investments, or to such other factors as the Board may deem appropriate", and (3) in the case of any lender engaged both in the extension of consumer credit and in other types of financing, the proportion of such lender's assets which may be devoted to the extension of any type of consumer credit.

The Federal Home Loan Bank Board expresses no view as to the need for or advisability of the enactment of this section.

(6) Garnishment of Wages. Title II of the bill would provide that no person may attach or garnish wages or salary due an employee, or pursue in any court any similar legal or equitable remedy which has the effect of stopping or diverting the payment of wages or salary due to an employee, and would provide criminal penalties for violation. The Board recommends against the enactment of any garnishment provision until the inter-agency study of garnishment is completed and recommendations are developed.

The Bureau of the Budget has advised that there is no objection to the submission of this report, and that enactment of legislation to provide full disclosure of credit charges is in accord with the program of the President.

With kindest regards, I am

Sincerely,

JOHN E. HORNE,
Chairman.

(Mr. Joseph W. Barr, Under Secretary, Department of the Treasury, submitted the following material for inclusion in the record:)

EXAMPLES ILLUSTRATING THE APPLICABILITY OF THE DEPARTMENT OF DEFENSE RATE TABLE TO H.R. 11601

No. 1—Equal payments, no deferment.[1]

NOTE.—Examples 1–9 are taken from the Treasury Department's "Annual Rate Tables."

No. 2—Odd final payment, no deferment.
No. 3—Equal payments plus deferment.
No. 4—Odd final payment plus deferment.
No. 5—Single payment (short term).
No. 6—Balloon payment.
No. 7—Skipped payments with odd payment.
No. 7a—Skipped payments with odd payments.
No. 8—Irregular single payments.
No. 9—Add-on purchase.
No. 10—Multiple disbursement case.
No. 11—Single payment loan (30 months).

Example 1—Equal payments, no deferment

The amount financed in the purchase of an automobile is $2000. The finance charge is $419.92. The monthly payments are $67.22 each for 36 months. What is the annual rate of finance charge?

Form No. I

For level payments which are irregular only because of deferment or odd final payment (provided the odd final payment is not more than twice as great as a regular payment). Use in connection with Defense Department Rate Table.

Step 1—Move decimal 2 places to the left in the amount to be financed and divide it into the finance charge. This gives the finance charge per $100 of amount to be financed. (=$21.00)

Step 2—(a-) Double the initial payment period, round it to the nearest whole month, and subtract 2.

(b) Add (a) to the *total* number of payments. (=36)

Step 3—Read down left hand column of the Defense Department Rate Table to number of payments found in Step 2(b). Read across to locate finance charge per $100 (Step 1) and read up to find rate. (=13%)

Note: This form incorporates the assumption of Section 202(f)(1)(B) of H.R. 11601 regarding an odd payment. It has been suggested that Section 202 (f)(1)(C) could easily be revised to embody the Step 2 correction for deferment of the first payment.

Example 2—Odd final payment, no deferment

A TV is purchased for $395 plus a finance charge of $39.50. It is to be financed by 17 payments of $24 each plus a final payment of $26.50. What is the annual rate?

Form No. I

For level payments which are irregular only because of deferment or odd final payment (provided the odd final payment is not more than twice as great as a regular payment). Use in connection with Defense Department Rate Table.

Step 1—Move decimal 2 places to the left in the amount to be financed and divide it into the finance charge. This gives the finance charge per $100 of amount to be financed. (=$10.00)

Step 2—(a) Double the initial payment period, round it to the nearest whole month, and subtract 2.

(b) Add (a) to the *total* number of payments. (=18)

Step 3—Read down left hand column of the Defense Department Rate Table to number of payments found in Step 2(b). Read across to locate finance charge per $100 (Step 1) and read up to find rate. (=12%)

Note: This form incorporates the assumption of Section 202(f)(1)(B) of H.R. 11601 regarding an odd payment. It has been suggested that Section 202(f)(1)

[1] In the case of monthly payments deferment is the time by which the first payment period exceeds the usual 1 month. (When the time to first payment is less than 1 month, the deferment is negative.)

(C) could easily be revised to embody the Step 2 correction for deferment of the first payment.

Example 3—Equal payments plus deferment

A personal loan is arranged for $200. The finance charge is $16.00. There are to be 12 payments of $18.00 each. The first payment is due in 3 months 24 days. What is the annual rate?

Form No. I

For level payments which are irregular only because of deferment or odd final payment (provided the odd final payment is not more than twice as great as a regular payment). Use in connection with Defense Department Rate Table.

Step 1—Move decimal 2 places to the left in the amount to be financed and divide it into the finance charge. This gives the finance charge per $100 of amount to be financed. (=$8.00)

Step 2—(a) Double the initial payment period, round it to the nearest whole month, and subtract 2. (=6)

(b) Add (a) to the *total* number of payments. (=18)

Step 3—Read down left hand column of the Defense Department Rate Table to number of payments found in Step 2(b). Read across to locate finance charge per $100 (Step 1) and read up to find rate. (=10%)

Note: This form incorporates the assumption of Section 202(f)(1)(B) of H.R. 11601 regarding an odd payment. It has been suggested that Section 202 (f)(1)(C) could easily be revised to embody the Step 2 correction for deferment of the first payment.

Example 4—Odd final payment plus deferment

A $195.50 appliance is financed with 10 payments of $20.00 each and a final payment of $7.80. The finance charge is $12.30. The first payment is due in 21 days. What is the annual rate?

Form No. I

For level payments which are irregular only because of deferment or odd final payment (provided the odd final payment is not more than twice as great as a regular payment). Use in connection with Defense Department Rate Table.

Step 1—Move decimal 2 places to the left in the amount to be financed and divide it into the finance charge. This gives the finance charge per $100 of amount to be financed. (=$6.29)

Step 2—(a) Double the initial payment period, round it to the nearest whole month, and subtract 2. (=−1)

(b) Add (a) to the *total* number of payments. (=10)

Step 3—Read down left hand column of the Defense Department Rate Table to number of payments found in Step 2 (b). Read across to locate finance charge per $100 (Step 1) and read up to find rate. (=13½%)

Note: This form incorporates the assumption of Section 202(f)(1)(B) of H.R. 11601 regarding an odd payment. It has been suggested that Section 202(g)(1)(C) could easily be revised to embody the Step 2 correction for deferment of the first payment.

Example 5—Single payment

The purchase of $250 of merchandise is to be financed by a single payment of $257.50 in 3 months 21 days. Find the annual rate.

Form No. I

For level payments which are irregular only because of deferment or odd final payment (provided the odd final payment is not more than twice as great as a regular payment). Use in connection with Defense Department Rate Table.

Step 1—Move decimal 2 places to the left in the amount to be financed and divide it into the finance charge. This gives the finance charge per $100 of amount to be financed. (=$3.00)

Step 2—(a) Double the initial payment period, round it to the nearest whole month, and subtract 2. (=5)

(b) Add (a) to the *total* number of payments. (=6)

Step 3—Read down left hand column of the Defense Department Rate Table to number of payments found in Step 2 (b). Read across to locate finance charge per $100 (Step 1) and read up to find rate. (=10%)

Note: This form incorporates the assumption of Section 202(f)(1)(B) of H.R. 11601 regarding an odd payment. It has been suggested that Section 202 (f)(1)(C) could easily be revised to embody the Step 2 correction for deferment of the first payment.

Example 6—Balloon Payment

An item priced at $610 is paid for as follows, each series beginning at the indicated time from contract date.
10 pmts. of $50 each, beginning at 1 mo. 28 days. Total, $500.
1 pmt. of $150, at 11 mos. 28 days. Total, $150.
The total finance charge is $40. Find the annual rate.

Form No. II

For all irregular cases not covered by Form No. I. Use in connection with Defense Department Rate Table.
Step 1—Move decimal 2 places to the left in the amount to be financed and divide it into the finance charge. This gives the finance charge per $100 of amount to be financed. (=$6.56)
Step 2—For each sub-schedule within the main schedule fill in the following:

(A) Initial period doubled, to nearest month	(B) Number of payments	(C) Amount of each payment	(D) Total amount of payments (B×C)	(E) Equivalent payments (A+B−2)	(F) (D×E)
4	10	$50	$500	12	$6,000
24	1	150	150	23	3,450
Total			650		9,450

Divide total of column F by total of column D and round to the nearest integer. This is the equivalent number of payments. (=15)
Step 3—Read down left hand column of the Defense Department Rate Table to number of payments found in Step 2. Read across to locate finance charge per $100 (Step 1) and read up to find rate. (=10%)

Example 7—Skipped payments with odd final payment

An item priced at $346 is paid for by the following groups of payments, each series beginning at the indicated time from contract date.
3 pmts. of $20 each, beginning at 1 mo. 5 days. Total, $60.
8 pmts. of $20 each, beginning at 7 mos. 5 days. Total, $160.
7 pmts. of $20 each, beginning at 18 mos. 5 days. Total, $140.
1 pmt. of $30, due at 19 months 5 days. Total, $30.
The total finance charge is $44.00. Find the annual rate.

Form No. II

For all irregular cases not covered by Form No. I. Use in connection with Defense Department Rate Table.
Step 1—Move decimal 2 places to the left in the amount to be financed and divide it into the finance charge. This gives the finance charge per $100 of amount to be financed. (=$12.72)
Step 2—For each sub-schedule within the main schedule fill in the following:

(A) Initial period doubled, to nearest month	(B) Number of payments	(C) Amount of each payment	(D) Total amount of payments (B×C)	(E) Equivalent payments (A+B−2)	(F) (D×E)
2	3	$20	$60	3	$180
14	8	20	160	20	3,200
36	7	20	140	41	5,740
38	1	30	30	37	1,110
Total			390		10,230

Divide total of column F by total of column D and round to the nearest integer. This is the equivalent number of payments. (=26)

Step 3—Read down left hand column of the Defense Department Rate Table to number of payments found in Step 2. Read across to locate finance charge per $100 (step 1) and read up to find rate. (=11%)

Example 7a—Skipped payments with odd payments.

A farmer and his wife (who is a schoolteacher) in purchasing an automobile borrow $2786 for which the finance charge is $444.21, and the payment schedule is as follows:

Contract date—7/12/67
9 monthly payments of $50 each starting 10/3/67
1 monthly payment of $50 on 10/3/68
1 monthly payment of $550 on 11/3/68
7 monthly payments of $50 each starting 12/3/68
1 monthly payment of $50 on 10/3/69
1 monthly payment of $550 on 11/3/69
7 monthly payments of $50 each starting 12/3/69
1 monthly payment of $880.21 on 7/3/70

Form No. II

For all irregular cases not covered by Form No. I. Use in connection with Defense Department Rate Table.

Step 1—Move decimal 2 places to the left in the amount to be financed and divide it into the finance charge. This gives the finance charge per $100 of amount to be financed. (=$15.94)

Step 2—For each sub-schedule within the main schedule fill in the following:

(A) Initial period doubled, to nearest month	(B) Number of payments	(C) Amount of each payment	(D) Total amount of payments (B×C)	(E) Equivalent payments (A+B−2)	(F) (D×E)
5	9	$50	$450	12	$5,400
29	1	50	50	28	1,400
31	1	550	550	30	16,500
33	7	50	350	38	13,300
53	1	50	50	52	2,600
55	1	550	550	54	29,700
57	7	50	350	62	21,700
71	1	880	880	70	61,600
Total			$3,230		152,200

Divide total of column F by total of column D and round to the nearest integer. This is the equivalent number of payments. (=47)

Step 3—Read down left hand column of the Defense Department Rate Table to number of payments found in Step 2. Read across to locate finance charge per $100 (Step 1) and read up to find rate. (=7½%)

Example 8—Irregular single payments

An item priced at $400 is paid for by the following single payments, each payment due at the indicated time from contract date.

1 payment of $100.00 at 1 month 9 days.
1 payment of $100.00 at 2 months 1 day.
1 payment of $75.00 at 4 months 10 days.
1 payment of $65.00 at 5 months 9 days.
1 payment of $25.00 at 8 months 6 days.
1 payment of $51.83 at 10 months 8 days.

The total finance charge is $16.83. Find the annual rate.

Form No. II

For all irregular cases not covered by Form No. I. Use in connection with Defense Department Rate Table.

Step 1—Move decimal 2 places to the left in the amount to be financed and divide it into the finance charge. This gives the finance charge per $100 of amount to be financed. (=$4.21)

Step 2—For each sub-schedule within the main schedule fill in the following:

(A) Initial period doubled, to nearest month	(B) Number of payments	(C) Amount of each payment	(D) Total amount of payments (B×C)	(E) Equivalent payments (A+B−2)	(F) (D×E)
3	1	$100	$100	2	$200
4	1	100	100	3	300
9	1	75	75	8	600
11	1	65	65	10	650
16	1	25	25	15	375
21	1	52	52	20	1,040
Total			417		3,165

Divide total of column F by total of column D and round to the nearest integer. This is the equivalent number of payments. (=8)

Step 3—Read down left hand column of the Defense Department Rate Table to number of payments found in Step 2. Read across to locate finance charge per $100 (Step 1) and read up to find rate. (=11%)

Example 9—Add-on purchase

An item priced at $142 was added to an existing contract. In order to set a uniform total payment for the account over the next 12 months, the payments for this item were to be made as follows, each series beginning at the indicated time from contract date.

10 pmts. of $10.50 each, beginning at 1 month. Total, $105.
2 pmts. of $24.50 each, beginning at 11 months. Total, $49.

The finance charge is $12.00. Find the annual rate.

Form No. II

For all irregular cases not covered by Form No. I. Use in connection with Defense Department Rate Table.

Step 1—Move decimal 2 places to the left in the amount to be financed and divide it into the finance charge. This gives the finance charge per $100 of amount to be financed. (=$8.45)

Step 2—For each sub-schedule within the main schedule fill in the following:

(A) Initial period doubled, to nearest month	(B) Number of payments	(C) Amount of each payment	(D) Total amount of payments (B×C)	(E) Equivalent payments (A+B−2)	(F) (D×E)
2	10	$10.50	$105	10	$1,050
22	2	24.50	49	22	1,078
Total			154		2,128

Divide total of column F by total of column D and round to the nearest integer. This is the equivalent number of payments. (=14)

Step 3—Read down left hand column of the Defense Department Rate Table to number of payments found in Step 2. Read across to locate finance charge per $100 (Step 1) and read up to find rate. (=13%)

Example 10—Multiple Disbursement Case

Disbursements:
$100 on 5/1/67
$300 on 6/1/67
$600 on 9/1/67

Repayments: 12 of $90.02 each beginning 10/1/67.

Form No. I

For level payments which are irregular only because of deferment or odd final payment (provided the odd final payment is not more than twice as great as a regular payment). Use in connection with Defense Department Rate Table.

Step 1—Move decimal 2 places to the left in the amount to be financed and divide it into the finance charge. This gives the finance charge per $100 of amount to be financed. (=$8.02)

Step 2—(a) Double the initial payment period, round it to the nearest whole month, and subtract 2. (=3*)

(b) Add (a) to the *total* number of payments. (=15)

Step 3—Read down left hand column of the Defense Department Rate Table to number of payments found in Step 2(b). Read across to locate finance charge per $100 (Step 1) and read up to find rate. (=12%)

Note: This form incorporates the assumption of Section 202(f)(1)(B) of H.R. 11601 regarding an odd payment. It has been suggested that Section 202 (f)(1)(C) could easily be revised to embody the Step 2 correction for deferment of the first payment.

Example 11—Single Payment Loans (30 months)

Loan: $100.

Repayment: 1 payment of $209.76 at end of 30 months.

Form No. I

For level payments which are irregular only because of deferment or odd final payment (provided the odd final payment is not more than twice as great as a regular payment). Use in connection with Defense Department Rate Table.

Step 1—Move decimal 2 places to the left in the amount to be financed and divide it into the finance charge. This gives the finance charge per $100 of amount to be financed. (=$109.76)

Step 2—(a) Double the initial payment period, round it to the nearest whole month, and subtract 2. (=58)

(b) Add (a) to the *total* number of payments. (=59)

Step 3—Read down left hand column of the Defense Department Rate Table to number of payments found in Step 2(b). Read across to locate finance charge per $100 (Step 1) and read up to find rate. (=36%) (34.74% by interpolation)

Note: This form incorporates the assumption of Section 202 (f)(1)(B) of H.R. 11601 regarding an odd payment. It has been suggested that Section 202 (f)(1)(C) could easily be revised to embody the Step 2 correction for deferment of the first payment.

Definitions of Terms Used in Under Secretary Barr's Statement on H.R. 11601

ADD-ON

Dollar add-on is synonymous with the finance charge. That is, it is the amount added to the initial unpaid balance to cover the cost of credit. The important point about dollar add-on is that it is often expressed as a percentage (or dollar per hundred) of the initial unpaid balance. For example, in a 6 percent add-on loan for $1000 for 12 months, the add-on is $60, resulting in an annual percentage rate of 10.9 percent. (See statement on H.R. 11601 by J. L. Robertson, Vice Chairman, Board of Governors of the Federal Reserve System.)

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*Months from 5/1 to 10/1=5× $100= 500
Months from 6/1 to 10/1=4× 300=1200
Months from 9/1 to 10/1=1× 600= 600

$1000 2300

Average time until first payment=$\frac{2300}{1000}$=2.3 months.

Double 2.3 to get 4.6. Round to 5 months and subtract 2.

*The true rate in this example is 30%. Obviously the level payment table is not well suited for longer term single payments. A matching "single payment" table (of same size and form as the existing table) is necessary and can easily be prepared.

Taking credit life and credit health together, we arrive at the following estimates for 1967:

1. Premiums Earned	$750, 000, 000
2. Losses including expenses of adjusting losses	400, 000, 000
3. Expenses of Insurer other than Commissions, Profit and Dividends to Creditor (Note A)	70, 000, 000
4. Commissions (3%)	22, 500, 000
5. Profit to Insurer (3%) (Note B)	22, 500, 000
6. Compensation to Creditor	60, 000, 000
7. Balance	175, 000, 000

NOTE A.—Some of the larger companies have aggregate commission ratios on Group Life as follows: Aetna, 2%; Allstate, 0%; Metropolitan, 1%; New York Life, 2%; Occidental of California, 2%; Prudential, ½%; Travelers, 2%. Thus, 3% has been taken as an approximation to the average true selling expense. While the smaller companies would necessarily have higher ratios, they would not exert much effect on the average—thus 3% seems reasonable.

NOTE B.—Similarly for profit, here are a few margins for larger companies: Aetna, 0%; Allstate, 1½%; Continental Assurance, 2%; Occidental of California, 1½%; Old Republic, 0% Travelers, 2%. A source of important additional profit to the insurer is investment income which explains why a company can operate on a 0% profit margin. Again 3% does not seem unreasonable.

If, somehow, creditors were prevented from profiting *excessively* on the insurance, annual savings of perhaps $175 million would be possible. My estimate of $100,000,000 of a year ago was timid.

Actually, the analysis above may even understate the facts because:

a.) At least one company, Old Republic, reports to Spectator on a premium basis net of dividends. Their annual financial statement reveals they paid dividends of $5,856,000 which do not show up in Spectator; rather their premiums have been reduced by that amount.

b.) The analysis assumes the companies *not* reporting to Spectator—about 15% of the business—have a loss ratio of about 50%. Most likely it is close to 25%.

c.) The analysis omits credit property insurance.

THE DILEMMA OF THE RESPONSIBLE INSURER

As evidenced by the New York Life incident related earlier, where that company lost a case because they refused to raise their premium to "meet the competition", companies which pride themselves on low cost service to the public are on the horns of a dilemma—either they play the game, or they lose the business.

Many such companies are reluctant to be a party to gouging the public and are not aggressively seeking business. Some of our largest group life companies—very efficient operators due to the economies of large scale—are only modest participants in credit insurance.

Of itself, this is a serious indictment of the credit insurance industry for it tends to breed a myriad of inefficient companies whose administrative and other expenses would choke them if they had to compete on a price basis.

CONCLUSION

These central facts seem to emerge from a review of the credit insurance industry:

(1) Fantastic profits are being made from the incidental sale of insurance in connection with loans and other credit transactions.

(2) In large measure, these profits are being captured by the finance industry, directly and indirectly, not the insurance industry, although many insurers are doing right well.

(3) They are made possible because competition works against the debtor to raise his cost.

(4) Someone must protect the debtor, who is in an inferior position to the creditor.

(5) This protection must come from government but state governments have been slow to act. This is not necessarily the fault of the insurance commissioner because he may be unable to secure legislation due to pressure exerted by creditors. Maryland and Iowa were unable to pass the model credit life bill this year for this reason, I understand.

(6) The citizens of many of our states need help.

on the basis advocated has been collected and studied. They also advocate that the experience for each state be collected separately. This means that in many instances the experience will be so fragmented that it will take several years at least to obtain meaningful data. The obvious purpose is to delay any reduction of the charges to the public and therefore any reduction of the creditors and insurers profits for as long as possible. Such reductions could and should be accomplished promptly by using the data produced by the NAIC's 1964 Study of credit life insurance experience to establish prima facie maximum rate standards, coupled with deviation procedures for cases with poor experience, which would produce loss ratios of at least 50% when the maximum rates are charged. This is substantially what the NAIC recommended a year ago, but no state has since acted upon that recommendation.[10]

HOW MUCH ARE CONSUMERS BEING OVERCHARGED FOR CREDIT INSURANCE?

We have discussed how competitive forces tend to keep premium rates high in credit insurance. What would the savings be if normal competition prevailed? By normal competition we mean the kind of competition found in regular group life insurance of the employer-employee variety where state laws require that the employer pay a portion of the net cost of the insurance and, therefore, he seeks out the insurer with the lowest bid.

A year ago I made the following statement:

"One thing is clear, if normal competition, rather than reverse competition, could exist there would be a tremendous reduction in cost of credit insurance passed on to borrowers. I would estimate that, based on current premium income, savings would exceed $100,000,000 nationwide annually."

This statement has been criticized as grossly exaggerated and harmful to the credit insurance industry. Therefore, perhaps a new estimate with a few details is in order.

Statistics on credit insurance are hard to come by and one task the Subcommittee should set for itself is to search out all companies writing this business and develop meaningful data.

The best, and latest, source of reasonably complete information is the October 1966 issue of Spectator magazine, which contains an article entitled "The Rebirth of Credit Life Insurance". Therein are included statistical tables for both credit life and credit health insurance. The author estimates that the data covers about 85% of the premiums written in the year shown, 1965.

The aggregate figures for items 1, 2 and 3 below come from that magazine and have been divided by .85 as an estimate of the total business in 1965 and then increased by 15% as an approximation to the business being written as of mid-1967. This assumes a growth rate of 10% per annum, a conservative projection as the business has grown faster than that in recent years.

As discussed earlier, commissions and insurer's profit (net gain from operations), items 4 and 5 below, in the case of most companies included in Spectator's statistical table, grossly overstate the amounts necessary to conduct the business of credit insurance since the creditor achieves his profit through these sources, as well as from dividends. Therefore, the estimates given are intended to approximate what the commissions and profits would be if the creditor were looking for the lowest premium to pass on to his debtor.

Item 6, compensation to creditor, is arbitrarily set at approximately 10% of the estimated reduced premium volume currently if excess compensation were eliminated. I am confident 10% exceeds the creditor's marginal cost of administering the insurance. Thus, it would not eliminate his profit.

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[10] In June, 1966, meeting in Richmond, Virginia, the NAIC passed a resolution recommending among other things enactment of the Model Bill in those states where it has not been enacted and implementation of the requirement that benefits be reasonable in relation to premiums through the promulgation of maximum rate standards by the Commissioners of those states which had not done so.

York limited charges to 64¢ per $100 for the smallest creditors reducing to 44¢ per $100 for the largest cases (over $5,000,000). New Jersey adopted the same scale and, currently, Vermont and California are considering similar regulations.

Five other states setting maximum rates have adopted the 50% loss ratio test recommended by the National Association of Insurance Commissioners in 1959 as a guideline to state insurance commissioners. By loss ratio we mean the ratio of benefits incurred to gross premiums earned. The resolution adopted says:

"The Committee in executive session recommends to all insurance supervisors that a rate for Credit Life or Credit Accident and Health producing a loss ratio of under 50% should be considered to be excessive."

As the underlying mortality cost in Credit Life averages about 30¢, this implies a maximum rate of about 60¢, although three of the five states mentioned above use 64¢. (Michigan and Pennsylvania are at 60¢; Connecticut, Maine and New Hampshire premit 64¢.)

The other states which have promulgated maximum rates adopted 75¢ which should produce a loss ratio of just in excess of 40%, thereby excessive according to the NAIC recommendation.

Thirty-four states, of course, have no rate standards. Undoubtedly investigation would show that a tremendous volume of credit insurance is being written at loss ratios under 40%.

WHAT IS A FAIR LOSS RATIO?

Virtually the whole credit insurance industry has embraced the 50% minimum loss ratio principle; at least that is their public position. Two questions are pertinent: first, is this a fair return and, second, is it being achieved?

To a life insurance actuary, familiar with the efficiency of group life insurance, the suggestion that 50% is an appropriate loss ratio is upsetting. I know perfectly well that loss ratios can run as high as 80%, perhaps 85%,[8] in credit insurance and still allow the creditor to receive a modest dividend and the insurer to make a profit. There are a number of companies who achieve such loss ratios—Aetna Life, to name one.

Further, the credit insurance business in Vermont is written at premium levels producing a loss ratio in total averaging 65% to 70%.

Thus, I am unable to conclude that 50% of the premium is reasonable. It seems to me that a rate producing a minimum return to the consumer of something like 65¢ of each $1 is more appropriate. This ties in with the loss ratios expected in auto insurance where policies are distributed one-by-one without any of the group insurance efficiencies. A minimum 65% loss ratio still leaves plenty for the creditor. For these reasons Vermont will adopt the New York/New Jersey concept which produces an average loss ratio of something like 65% for those creditors charging the maximums.

Even assuming the 50% principle is a good one, and it sure is better than anything lower than 50%, a tremendous volume of business is being written at rates producing loss ratios of 40%, 30%, 25% and probably lower. In other words, the 50% principle is not being achieved except in a handful of states cited earlier.

There is a running tug of war in the industry between those who feel the consumer needs protection and favor the adopting of a set of maximum rates—rates which, at the minimum, will achieve the 50% loss ratio test meaning a rate of about 60¢—and, lead by the Consumer Credit Insurance Ass'n.,[9] those who are fighting to preserve the status quo, meaning no maximum rate standards or a 75¢ rate.

Those who resist meaningful rate standards tend to suggest that the 50% minimum loss ratio test should be applied on a company by company, policy form, class of business, class of creditor, or a case by case basis and that no prima facie maximum rates should be promulgated by the Commissioner until experience

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[8] It is interesting to consider that when the Internal Revenue Service requested the life insurance industry to provide the Service with a schedule of rates for group life insurance in order to establish the economic value for tax purposes of this coverage when provided free of charge by an employer for his employees, an 85% loss ratio was assumed.

[9] That is not their public position for this trade association has endorsed the 50% loss ratio principle. However, a reading of their counsel's testimony in Wisconsin in 1966 leads me to conclude that they are primarily devoted to resisting attempts to establish maximum rate standards.

significant. For example, a $3000 car financed over three years at $7 per $100 would call for average $450 refund, approximately, if death occurred in the first year.

The foregoing is not an academic matter. Even in Vermont, I found one of our largest banks pocketing the difference between the amount of insurance and the net amount necessary to prepay the debt even though the debtor had paid the full insurance premium. As a result, Vermont's finance laws have been amended to make it crystal clear refunds on prepayment by life insurance proceeds are required.

HISTORY OF STATE REGULATION OF CREDIT INSURANCE

The first point to make is that life and health insurance pricing traditionally has been subject to no review[5] by state authorities, in contrast to fire and casualty insurance where rates have to be just, reasonable, adequate and non-discriminatory. Therefore, state authorities are powerless to deal with excessive premiums for credit insurance absent specific legislation.

In the late 40's and early 50's some of the abuses cited earlier began to gain attention and, in 1954, this Subcommittee conducted an investigation in Kansas into the tie-in sale of credit insurance in connection with small loans and other financial transactions and issued a report threatening federal intervention if corrective action were not taken.

Spurred on by this development and other studies, the National Association of Insurance Commissioners assisted representatives of the industry, worked out a model credit insurance bill which effectively deals with problems such as lack of disclosure, pyramiding of coverage, failure to make refunds of unearned insurance charges and the more flagrant sales of excessive amounts of insurance. The bill also contains a provision allowing the Commissioner to disapprove any policy form in which benefits are not reasonable in relation to premiums.

The model bill is a good one[6] but, like much legislation, requires implementation and enforcement to be effective. While about 30 states have enacted the model bill, only 16 states, as far as I can determine, have established maximum premium rates.[7] Even among these states, there is a wide variation in rate standards promulgated ranging from a low of 44¢ per $100 initial indebtedness repayable in 12 equal monthly installments for larger cases in New York and New Jersey to a high of 90¢ for so-called individual policies in Texas.

In those states which do not regulate credit insurance pricing, $1 per $100 is not unusual—in fact, it is frequently the standard rate. Sometimes the rate even runs higher than $1. These are extraordinary rates when contrasted with the General Motors Acceptance Corporation (GMAC) rate in my state of 37½¢ per $100 for essentially the same insurance. And you can be sure GMAC receives a modest refund even at this low rate.

Lest it be said that GMAC achieves such a low rate because it is so large, there are several modest-sized banks in Vermont charging about 40¢ per $100. The prevalent rate of $1 per $100 in many parts of the country is shocking—more than twice the amount necessary for those creditors with a respectable volume.

The matter of what constitutes a reasonable relationship between premiums and benefits has been a hot topic in the credit insurance field. The battle got off to a good start when New York promulgated a scale of maximum rates varying by the creditor's volume of insurance. Recognizing that the administrative costs of a group case decline on a per unit basis as the size of the case increases, New

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[5] Except indirectly through New York's Sections 213 and 213a limiting certain expenses of a life insurance company doing business in New York.

[6] One deficiency of the model bill is that it is limited in scope to credit transactions of 5 years or less. The financing of mobile homes, in particular, as well as other costly items such as garages and home improvement loans, often exceeds 5 years and, even in those states with the model law, the debtor is afforded no protection against excessive charges for the life insurance, as well as some of the other abuses cited. Vermont, at my urging, eliminated the 5 year limitation this year so that our credit insurance law now covers all credit transactions except first real estate mortgages. I would urge other states to make this change for the amounts of insurance and, thereby, the premiums are much larger than in the usual credit transaction.

[7] In the discussion that follows, it should be understood that the term "maximum rates" means that higher rates may be charged only upon presentation to the insurance commissioner of evidence that a particular creditor's insureds offer a risk significantly higher than normal, presumably due to a higher average age of the group, such that a higher rate is justified. Thus, the rate standards promulgated are "prima facie maximum rates". If a company receives permission to charge a higher rate, that is known as a deviation.

been no insurance despite the fact that the addition of the insurance decreases the risk of loss on the credit transaction.

(5) *Failure to Refund Finance Charges on Prepayment of a Debt Due to the Death of an Insured Debtor*—As mentioned, state law requires refunds of finance charges to be given if the debtor prepays his debt prior to maturity. Frequently, however, if the debt is prepaid by the proceeds of a credit life insurance policy, the refund is not made to the beneficiary or estate of the deceased debtor. I have a feeling this abuse is more widespread than any of us realize. It is particularly deplorable because the debtor pays the entire cost for the insurance, often at an excessive rate, and should be entitled to every penny not legally owed to the creditor.

Some detail will be necessary to explain how the creditor, in the absence of specific state laws to the contrary, manages this bit of larceny.

In making consumer loans or financing the purchase of goods and/or services, it is virtually the universal practice to add the total finance charges for the entire repayment period to the principal of the debt and then to insure the sum of these two items. Thus, at any time prior to maturity, the life insurance is in an amount inclusive of unearned finance charges. On death, the insurance company pays to the creditor, as beneficiary, the sum insured and leaves it to the creditor to refund that portion of the insured finance charge which is unearned.

That these amounts can be significant is illustrated by the following example derived from a complaint I received in Vermont from a young man who had financed a mobile home over a seven year period and had been required to buy life insurance. His complaint went to the excessive credit life insurance charges, rather than to the possibility of his not receiving the full proceeds of the policy on his death. However, since the instrument evidencing his debt had been sold to an out-of-state bank and since the insurance company told me that they merely paid the proceeds to the bank and left it up to the bank to make any refunds of excess insurance proceeds, I suspect the worst.

Here is the breakdown of the charges on the installment sales act agreement signed by the young man:

1. Cash Price	$4,150.00
2. Less: Down Payment	−300.00
3. Unpaid Balance	3,850.00
4. Comprehensive and VSI Ins	253.00
5. Credit Life Insurance	273.89
6. Principal Balance (3+4+5)	4,376.89
7. Finance Charge	2,144.03
8. Total Time Balance (6+7)	6,520.92

(The other insurance charge—Item 4—is probably reasonable and is not a matter for consideration here except to say that the $7 per $100 per year finance charge—12.16% true interest—added to this insurance charge represents an additional gain to the creditor while the existence of the insurance decreases his risk.)

Here is the schedule of the indebtedness, amount of life insurance, amount necessary to prepay the debt and the excess proceeds of the life insurance policy:

Beginning of month	Indebtedness including unearned finance charge	Credit life insurance in force	Amount necessary to prepay indebtedness	Excess amounts of insurance
1	$6,521	$6,521	$4,112	$2,409
13	5,589	5,589	3,820	1,769
25	4,658	4,658	3,415	1,243
37	3,726	3,726	2,927	799
49	2,795	2,795	2,349	446
61	1,863	1,863	1,683	140
73	932	932	884	48

While credit transactions of lesser amounts and shorter durations do not offer the potential windfalls shown in Column 5, the amounts are nonetheless

amined the monthly reports from Old Republic, deposited its monthly receipts, and prepared its annual statements to the Indiana Insurance Department with the help of information furnished him by Old Republic and Alinco's consulting actuary. On the average he was able to perform these duties in the space of approximately one day each month.

"Despite the simplicity of this operation, Alinco's financial success during the period 1953 through 1959 was striking. Its net gain from operations during that period, before Federal income taxes but after paying its expenses and share of death benefits, was in excess of $28,500,000."

The process by which a credit life company operating in many states in effect stands in place of the creditor's captive reinsurer can be described as a "fronting" arrangement. The primary insurer's cut of the bsuiness is sometimes known as a "fronting fee". Its size depends on the relative strengths of the creditor and the insurer. Earlier we described how competition tends to keep premiums high in credit insurance. The real competition is between the creditor, on behalf of his captive reinsurer, and the insurer as to who gets what share of the action.

As time passes, the alert creditor will demand "more and more of the pot", as the expression goes, by threatening to move his insurance to a carrier who will provide the desired arrangement.

This squeeze play by the creditor often reduces the insurer's net profit nearly to the vanishing point. For example, one "pot" I am aware of is split 39 parts to the creditor's captive company and one part to the "fronting" insurer.

I have heard of deals where the fronting company writes the business for no profit at all save the investment income it can generate from the premium income. Some insurers, I am told, will write the business at no profit for the volume of insurance tends to inflate the annual financial statement, making it much easier to run up the company's stock.

Further, without going into detail, there are important tax advantages to having the creditor's share of the pot flow to a subsidiary life company rather than be received directly as commissions or dividends. The advantages, however, are much less significant than they were prior to 1959 when the method of taxing life insurance was changed.

The villain of the piece begins to emerge then. The big profits are not going to the life insurance companies who provide the service (except where the insurer is owned by the creditor) but rather to the creditors—small loan companies, finance companies, banks, merchants who sell on time, anyone in the business of extending credit for profit.

WHAT ARE SOME OF THE OTHER ABUSES PREVALENT IN CREDIT INSURANCE?

The big money in credit insurance is made by the creditor by capturing a large share of an excessive premium, as we have just described. Among other schemes by which the creditor profits at the expense of the debtor are the following:

(1) *Failure to Refund the Unearned Insurance Premium on Refinancing or Repayment of the Debt*—State laws require refund of unearned *finance* charges on prepayment by the debtor. Since the insurance premium is paid in advance as well, the unearned portion of it should be refunded on prepayment. But many states have no law on this and the creditor often pockets the insurance refund himself.

(2) *Pyramiding of Policies*—Often debts are refinanced or renewed. If so, a new insurance policy is issued and paid for. The proper procedure is to cancel the old policy and make a refund but some lenders leave the old policy in force. Thus the debtor ends up with two or more expensive policies for amounts in excess of his debt.

(3) *Excessive Coverage Sold at the Inception of the Credit Transaction*—Level term policies may be sold to cover a loan repayable in installments rather than decreasing term insurance. The debtor ends up paying too high a price for more coverage than is necessary.

(Those states with credit insurance legislation or effective regulations have pretty well put a stop to the three practices above, but, as we will see, many states have no control over the business.)

(4) *Profit from Finance Charges Added to the Insurance Premium*—The normal method for calculating the finance charge is to add the single premium for the insurance to the principal amount borrowed *before making the calculation.* Thus, the creditor's interest income is increased over what it would be had there

Note that in a larger case, commissions may well average a fraction on one per cent. Clearly, commission rates of 30%, 40% and more are merely a device to pass on a significant portion of the premium to the creditor.

(2) *Dividends or Retrospective Rate Credits*—A second method, either supplementary or in lieu of commissions, is through the payment of dividends or, as they are often called in group insurance, retrospective rate credits.

These payments are merely the amount left over after paying all necessary expenses and profits of the insurance company including death and disability claims. While the amount of the dividend depends on the mortality or morbidity experience of the group, in larger cases the dividends are predictable within a narrow range.

When I first heard about credit insurance, I naively assumed the dividends were returned to those who paid the insurance premium, the debtors. It came as some surprise to me that the creditor picked them up even though he contributed nothing to the cost.

(In regular employer-employee group life insurance, the dividends are returned to the employer but it is not lawful for him to recoup more than he contributed to the cost of the insurance.)

Some states, including Vermont, passed laws requiring that these dividends be used to reduce the cost to borrowers in the following year. Such laws don't work for they merely serve to increase commissions or can be circumvented by either of the methods below. Vermont repealed this requirement shortly after enacting it.

(3) *Captive Life Insurance Companies—Direct*—Obviously, it is possible for a larger creditor to set up his own insurance company as a subsidiary and thereby capture the profits directly. However, it is time consuming to gain admittance to the states in which the creditor does business and the economies of large scale makes this method too expensive for all but the largest creditors. Further, a modest degree of expertise is required. The reinsurance route is generally preferred.

(4) *Captive Life Insurance Companies—Reinsurance*—While the methods above are rather prosaic, the reinsurance deals which criss-cross the country can be intriguing.

The Subcommittee is undoubtedly aware that reinsurance is a most useful device in the insurance business to spread the risk—laying off the bets, in the bookmaker's parlance. In this way, a company can take on almost any size risk by limiting its exposure to a predetermined amount and reinsuring the balance with one or more reinsurers.

In credit insurance, reinsurance has an entirely different function—to pass profits through to the creditor. Because of the small amounts insured, and the fact that the debtors are well dispersed, it is usually unnecessary to spread the risk.

The creditor merely forms a life insurance subsidiary which need not apply for admission to do business in any state but its own. The subsidiary enters into a "reinsurance treaty", as it is called, with a company licensed to do business in at least those states in which the creditor does business, or reinsurance treaties may be negotiated with more than one company.

Commissioner Fletcher in the Alinco case mentioned earlier describes the arrangement better than I can. Old Republic wrote the credit life insurance covering the debtors of Associates Investment Company, the creditor. Alinco was a life insurance company which was wholly owned by Associates. Alinco's only function was to reinsure a portion of Old Republic's direct writings roughly equivalent in amount to the coverage written by Old Republic on Associates debtors.

"The Alinco-Old Republic reinsurance arrangement was typical of reinsurance arrangements generally in that Old Republic as the primary carrier handled all administrative details of the insurance including the supervision, investigation, defense against and payment of all claims, and thereafter made its claim against Alinco by way of monthly statements for Alinco's share of the losses.

"From birth to liquidation, Alinco's only business consisted of reinsurance under the Old Republic-Alinco treaty. As might be expected from the fact that Old Republic handled the myriad details incident to the insurance contained in the Alinco Reinsurance Pool, Alinco's operations were quite simple and inexpensive. Alinco had no office or salaried employees. An accountant employed by another subsidiary of Associates took care of Alinco's books and records, ex-

lies in the consummation of the primary transaction of loan (or installment sale), he is not likely to go out 'shopping' elsewhere for a lower premium rate assuming he is interested in acquiring any credit life insurance at all. Thus, it is reasonable to anticipate that, in most instances, a borrower desiring to cover his loan with credit life insurance will consummate the entire transaction with his creditor in preference to making any independent analysis or comparison of credit life premiums available elsewhere."

In other words, the debtors form a captive market for the insurance and have no ability to evaluate the reasonableness of the insurance charge.

But it might be asked, "Does it really matter what the source of the creditor's profit is? What difference is there if he makes it on the insurance, the finance charge, or both?"

The answer is that it usually does matter. First, the states all have various laws to protect borrowers and those who buy on time. These laws—usury laws, small loan acts, installment sales acts, revolving charge account maximums, etc.— are necessary due to the inferior bargaining position of the debtor. It is not at all unusual for small loan companies, finance companies, even banks, to operate at the maximum rates permittd by law. Creditors who charge the maximum rate for the extension of credit and profit in addition on the same transaction from the sale of insurance to their captive debtor are, as a practical matter, circumventing the intent of state's finance laws.[4]

Having explained how overcharging for credit insurance arises and why it is a serious matter, let us examine the manner in which the creditor captures a large share of the credit insurance dollar.

COMMISSIONS, DIVIDENDS, CAPTIVE INSURERS AND REINSURANCE IN CREDIT INSURANCE

There are perhaps four methods by which the creditor gets his "piece of the action". All are quite legal and well-accepted.

(1) *Commissions*—The simplest way to pass on a portion of the insurance premium to the creditor is by paying him a commission rate in excess of that which normally would pertain.

It is, of course, an easy matter to sell the creditor on the need to cover his debtors with life insurance. It is very valuable to him in his operations and, further, he is able to make a profit from its sale far in excess of the marginal expenses of adding the service. In fact, I would argue that the creditor would be quite willing to offer the insurance without any form of compensation whatsoever because it relieves him of the expensive, and sometimes impossible, task of collecting the unpaid balance on death from the debtor's estate. Further, the marginal cost of asking the question about insurance, and of filling in an additional line on the application, is negligible.

Often commissions in credit insurance run to 30%, 40% or higher. That this is far in excess of typical commission rates in group insurance can be seen from the following table:

REPRESENTATIVE GROUP COMMISSION SCHEDULE[1]

[In percent]

Portion of premium	1st year	9 renewals
1st $1,000	20	5
Next $4,000	20	3
Next $5,000	15	1½
Next $10,000	12½	1½
Do	10	1½
Next $20,000	5	1½
Next $50,000	2½	1
Do	1	½
Next $350,000	½	½
Next $500,000	¼	¼
Next $1,000,000 and over	1/20	1/10

[1] Source: Group insurance study notes published by the Education and Examination Committee of the Society of Actuaries.

[4] That insurance profits are hardly insignificant is dramatically illustrated by a careful review of a recent Credithrift Financial prospectus received in our Securities Division. After taxes and preferred dividends, this finance company earned 3.13 million of which about 1.65 million came from writing insurance on their customers. In other words, they made more on the insurance than they did on their basic business. These figures are for the company's fiscal year 1966.

handling techniques are employed in either case, the two methods differ only in form, not in substance. Thus, we can refer to all credit life insurance as a specialized form of group term life insurance.

It is important to point out that, in the vast majority of cases, there is no direct contact between the insurance company and the insured. The creditor controls the sale entirely.

Except in specialized coverages, the cost of credit life insurance is the same regardless of the age of the debtor. The reason for this is primarily administrative convenience. Further, it makes it much easier to insure older persons who otherwise might resist the substantially higher cost.

Credit life insurance is generally single premium term insurance which decreases as the debt is repaid. Sometimes, level term insurance is issued to cover loans repayable in lump sums.

In summary, credit insurance is a form of group insurance sold more or less automatically in connection with credit transactions with a minimum of administrative expense to either the creditor or the insurance company.

It is a vital adjunct to consumer credit for it protects the creditor against loss through the death or disability of the debtor and protects the debtor's family against claims for debts outstanding at the time of the breadwinner's death or disability.

Despite these advantages, credit insurance is subject to widespread abuse, in my opinion, and, with this background information, it is now possible to describe the nature of these abuses and how they arise.

COMPETITION IN REVERSE

Recently I was discussing credit insurance with the president of New York Life who told me his company had recently lost a large bank's credit life program to another insurer whose price was 60% higher than New York Life had bid.

Does this sound like free enterprise gone haywire? Not at all in the credit insurance field. New York Life was simply unwilling to "meet the competition" by raising the price of its product, the cost of which was to be borne entirely by the bank's customers.

Of course, it is quickly realized that the creditor accepts the highest bid rather than the lowest because he gets the difference in kickbacks of one form or another which we will go into later.

Normal competitive forces, then, tend to *raise* the price of credit insurance to the consumer and this phenomenon is known as "reverse competition" in the credit insurance field. The process needs to be described in greater detail.

Credit insurance is offered in either of two ways: (1) without an identifiable charge, its cost being included as part of the finance charge, or (2) the debtor is assessed a separate extra charge for the insurance.

In the first instance, the creditor will wish to minimize his insurance cost so as to maximize his return from the finance charge. If all creditors used this method, we would not be here today for the insurer with the lowest bid combined with the best service would carry the day.

However, most credit insurance is sold as an extra cost item. In this event, the higher the price the greater the return to the creditor. The question arises, "Does not the debtor tend to seek out the lowest cost life insurance?" Commissioner Fletcher in his report to the United States Court of Claims in the Alinco[3] tax case gives us the answer:

"Due to the method by which credit life insurance is sold, a unique situation has been observed by persons knowledgeable in the industry. Since the premium for credit life insurance is generally paid by the borrower, and since the lender's remuneration is generally a percentage thereof, the higher the gross premium, the greater will be the profit to the lender who procures the policy. Therefore, some lenders (or sellers) in seeking to increase their remuneration for the procedurement of such insurance tend to place their business with the insurance company that charges the *highest* gross premium. An experienced lender (or seller) can generally foresee that, since the borrower's (or purchaser's) interest

[3] In U.S. Court of Claims No. 77–63 (Filed March 6, 1966)—Alinco Life Insurance Co. v. the U.S.—Report of Commissioner to the Court.

I would urge the Subcommittee to study this tax case carefully. Although it was decided against the Government, and in favor of a credit life insurer, it nevertheless offers a penetrating insight into one of the more imaginative ways in which a creditor maximizes his profits from the insurance sale.

CREDIT LIFE INSURANCE GROWTH IN THE U.S.

Credit *life* insurance which, to repeat, is sold in connection with loans or other credit transactions in order that the debt may be extinguished at the death of the debtor, was first sold with small loans in 1917. Of course, the requirement of life insurance as additional security for a loan goes back much further than 1917, but its systematic application began then.

The growth of credit life was modest until after World War II, when it began to grow rapidly. By 1950, credit life insurance in-force had reached only $4 billion. Today, the in-force figure is somewhere around $65 billion.[1]

Since 1954, when the Senate Antitrust and Monopoly Subcommittee held public hearings in Kansas regarding abuses in credit life insurance, the business has more than quadrupled to cover an estimated 85% of all consumer installment debt (excluding charge accounts, credit cards and residential mortgage debt).

Thus, there is no question that credit life insurance is pervasive in our economy and any inquiry into consumer credit generally must not omit the "hidden insurance, as one writer has labeled credit life.

In addition to small loans and installment purchases of autos, appliances, etc., credit life is also sold in connection with other credit transactions such as:

1. Installment loans by banks;
2. Credit card debts;
3. Revolving charge account balances;
4. Front end load, or contractural plan, mutual fund purchases;
5. Debit balances in margin accounts of brokerage firms;
6. Real estate mortgages;
7. Education loans;
8. Production Credit Association loans to farmers.

The ease with which it is sold, the simplicity of administration, and the large profits to the creditor from its sale have combined to make credit life immensely popular. As there are about 70 million [2] policies or certificates outstanding it is estimated that about 50,000,000 people in the U.S. are covered by credit life insurance in some form.

CREDIT HEALTH INSURANCE GROWTH IN THE UNITED STATES

Credit health insurance, which picks up the debtor's monthly payments during his disability, probably covers only about 10% of consumer installment debt, as opposed to an 85% penetration for credit life. The unit cost is about four times that of credit life which may be a factor in its slower growth. Further, claims administration is considerably more difficult. Also, the disability experience of a group is much less predictable than its mortality experience and insurers have not been as anxious to offer it.

Nevertheless, credit health is now growing rapidly in popularity with creditors and its growth rate in the future will probably exceed credit life.

(From this point on, it will be less confusing to limit the discussion to credit *life* insurance. Whatever remarks are made with respect to credit life will generally apply to credit health unless otherwise stated.)

CREDIT LIFE INSURANCE—HOW IS IT SOLD? WHAT ARE ITS DISTINGUISHING CHARACTERISTICS?

Credit life insurance is offered by life insurance companies to creditors whose job it is to sign up the customer for the insurance as an incidental part of the credit transaction. Often the insurance is required as a condition precedent to the extension of credit, but some states permit the debtor to substitute his own insurance if he requests to do so. As a practical matter, it is not difficult to add the insurance charge for the cost does not appear to be high in relation to the finance charge plus the principal balance.

Credit life insurance is written in two ways: (1) under an individual policy issued to the debtor with the creditor named as beneficiary or (2) under a group policy issued to the creditor who is beneficiary as well. Under the latter plan, the debtor is given a certificate evidencing the insurance. Because mass

[1] Source: Life Insurance Fact Book 1966 extrapolated.
[2] Source: Life Insurance Fact Book 1966 extrapolated.

(Hon. Jonathan B. Bingham, member of the Consumer Affairs Subcommittee, submitted the following statement of James H. Hunt, commissioner of banking and insurance for the State of Vermont, before the Senate Antitrust and Monopoly Subcommittee, on the subject of credit life and health insurance:)

STATEMENT TO THE SENATE ANTITRUST AND MONOPOLY SUBCOMMITTEE REGARDING CREDIT LIFE AND HEALTH INSURANCE BY JAMES H. HUNT, FELLOW, SOCIETY OF ACTUARIES, COMMISSIONER OF BANKING AND INSURANCE, STATE OF VERMONT

As the only Commissioner of Insurance in the United States who is a life insurance actuary, I am possibly well situated to comment on credit insurance. Equally important, I am also the Banking Commissioner and this responsibiilty includes supervision of sales finance and small loan companies. It is the combination of actuary, insurance commissioner and consumer credit administrator that compels me to appear before this distinguished committee today.

My task will be to bring before the Subcommittee certain background information concerning credit insurance which is necessary to an understanding of the need for effective regulation.

In addition, this statement will reveal my own view of credit insurance, which might be summarized at this point by saying that, in *most* states, the debtor is paying excessive premiums and needs help.

Since my remarks will include rather serious allegations about the credit insurance business, I wish at this point to place them in better perspective.

First, I have spent my working life in the life insurance business prior to becoming Commissioner and have great respect for the contributions it makes to the economic security of millions of Americans. Moreover, the tremendous capital formation provided by the life insurance industry (but not the credit insurance industry) is a vital factor in our steadily increasing standard of living. Thus, my statement should not be interpreted as a criticism of the life and health insurance business generally but only a specialized segment of it.

Secondly, since my comments are mainly directed to excessive premium rates, I wish to make it clear that I am not one who thinks profit is a dirty word. In Vermont, we have had some serious pressures on automobile rates and I have taken a strong position that the auto insurance companies must have adequate rates, rates which give them a reasonable chance to make a profit, in order that they can bring good service to our residents. This strong support of the need for higher auto insurance premiums in my state nearly cost me my job, for the Senate confirmed my appointment by the Governor last February only after much debate and a close vote.

My position has been, is, and will continue to be that where plenty of competition exists among insurance companies for the premium dollar, the insurance commissioner has little business interfering in the rate-setting process. However, such is not the case in credit insurance and that is why I am here.

CREDIT INSURANCE—WHAT IS IT?

Credit insurance is that form of insurance sold in connection with loans or other credit transactions generally providing, in the case of credit life insurance, a death benefit at least large enough to prepay the outstanding balance of the loan at the time of death of the debtor and, in the case of health insurance, a periodic benefit (almost always monthly)—equal to the periodic installment payment on the debt—for as long as the debtor is disabled or until the maturity date of the debt.

The sale of fire and casualty insurance in connection with credit transactions is known as credit property insurance. As credit property insurance is not sold in Vermont, I will leave discussion of this topic to other witnesses.

The insuring of accounts receivable by a merchant against extraordinary losses due to business failure of his customer is also referred to as credit insurance. This hearing is not concerned with that specialized field.

Throughout this statement, the term "creditor" will be understood to mean a lender, in the case of a loan of money, or the holder of an installment sales agreement, in the case of a time sale transaction. The term "debtor" will include the borrower or the buyer as the case may be.

precomputed charges made for the full term loan. The following table shows how this result is achieved:

8/78 (portion of aggregate charge allocated to 5th installment period)
7/78 (portion of aggregate charge allocated to 6th installment period)
6/78 (portion of aggregate charge allocated to 7th installment period)
5/78 (portion of aggregate charge allocated to 8th installment period)
4/78 (portion of aggregate charge allocated to 9th installment period)
3/78 (portion of aggregate charge allocated to 10th installment period)
2/78 (portion of aggregate charge allocated to 11th installment period)
1/78 (portion of aggregate charge allocated to 12th installment period)

Total 36/78 (portion of aggregate charge allocated to scheduled installments which have been prepaid).[80]"

Service charge

This expression is more or less synonymous with "finance charge".

Finance charge

This term is specifically defined in H.R. 11601 as well as in S. 5.

In addition, the following definition is given from Neifeld's Guide to Installment Purchases:

> *Finance charge:* That part of the total price in the retail installment contract of sale in excess of the cash price; difference between the commodity's cash and time-sales price. In motor vehicle transactions, the finance charge includes, unless otherwise specified, the insurance premium, if any.

Interest

The following definition is given by Neifeld: The money charge made by the lender for use by the borrower of a certain sum of money for a specified period of time; in law, compensation allowed or fixed by the parties for the use or forbearance or detention of money or its equivalent; the rate percent derived from money loaned by another, or from debts remaining unpaid.

Time price differential

Neifeld defines the time price differential as the difference between time payment price and cash price when goods are sold on credit.

Sale price vs cash price

Neifeld defines the retail installment sale as a retail installment contract in which the purchase price may be paid in installments over a period of time. The difference between the retail installment sale price and the cash price is the time price differential, defined above.

---

[80] The language most commonly used to express refunds based on the Rule of 78 in small loan laws is set forth in the N.Y. Small Loan Law, *N.Y. Banking Law* § 352(d)1:

> [R]efund [shall be] . . . an amount which shall be at least as great a proportion of the precomputed interest . . . as the sum of the remaining monthly balances of principal and interest combined scheduled to follow the installment date nearest the date of prepayment bears to the sum of all the monthly balances of principal and interest combined originally scheduled by the contract.

It should be noted that the statutory language designates that the fraction to be used in determining the refund is equal to the relation of the sum of the *amounts* of the monthly balance due after the date nearest the date of prepayment to the sum of the *amounts* of all scheduled monthly balances under the contract. If prepayment in full were made on the fourth installment date on a contract scheduled to be repaid in 12 monthly installments of $10 each, the refund would be calculated as follows:

$$\frac{\$80+70+60+50+40+30+20+10}{\$120+110+100+90+80+70+60+50+40+30+20+10} = \frac{\$360}{\$780} \text{ or } \frac{36}{78} \text{ of total charges.}$$

The result is the same as would be produced under the approach described in the text. That is, as long as the installments are substantially equal in amount and period, the results are the same whether one uses *number* of installments or *amount* of installments in the calculations with the Rule of 78. If installments are unequal in amount, then the method described in the text continues to produce the same result in the example shown, but the language of the statute will produce a larger or smaller fraction depending on whether the larger installments are scheduled to be repaid after the date of prepayment. See Ayres, *op. cit. supra* note 74, at 166–167.

RULE OF 78

Barbara Curran's "Trends in Consumer Credit Legislation" defines the Rule of 78 as follows:

"The Rule of 78 is merely a mathematical formula for determining the amount of the charge to be allocated to each installment period. The amount of the charge to be allocated to any particular installment period bears the same relation to the aggregate charges computed for the entire loan as the number of installments scheduled to be paid on and after the expiration of such installment period bears to the sum of the numbers designating all of the installment payments contracted for. Thus the charge applicable to the third installment period of a 12-installment contract would be 10/78 of the total charge.[78] The "10" represents the number of installments scheduled to be paid on and after the date the third installment period terminates, and the "78" represents the sum of the numbers of all the installments contracted for (i.e., 1+2+3+4+5+6+7+8+9+10+11 +12=78). Under the Rule of 78, 10/78 of the total charge is earned during the third installment period.[79] The refund for a loan prepaid in full will equal the aggregate of the charges to be allocated for each installment period following the date of prepayment. In other words, if the borrower prepays the loan in full on the fourth installment due date, he is entitled to 36/78 of the aggregate of

"TABLE II.—METHOD REFERRED TO IN NOTE 56 SUPRA (UNIFORM PAYMENTS OF PRINCIPAL AND INTEREST COMBINED BUT NOT ON BASIS OF PRECOMPUTATION)

"Balances	Interest	Principal	Total payment
$300.00	$6.00	$47.56	$53.56
252.44	5.05	48.51	53.56
203.93	4.08	49.48	53.56
145.45	3.09	50.47	53.56
103.98	2.08	51.48	53.56
52.50	1.05	52.50	53.55
----------	21.35	300.00	321.35

Id. at 205.

"Precomputation: Add the total of the Interest column under either Table I or II above to total of the Principal column and then divide by number of payments in the Total Payment column. For Table I, amount will be $53.50; for Table II, $53.558."

[56] If charges are computed monthly on the outstanding principal balance and if monthly installment payments of principal are to be equal in amount, then the total amount of each monthly installment payment (which includes the charge for credit) will be less than the amount of the total installment payment for the preceding month. Such is the case because the credit charge is computed on the basis of the outstanding principal which decreases as each monthly installment payment is made. Since the act does not require that installments of principal be equal in amount (only that no installment can be substantially greater than the preceding installment), small loan companies are able to devise repayment schedules which provide for installment payments which combine principal and charges but which are equal in amount (except for the last installment payment, which may be somewhat less than preceding installments) and which do not violate the maximum rate provisions of the law. See Ayres, Instalment Mathematics Handbook, "Uniform Payments Under Small Loan Laws" 202–208 (1946). This method is not to be confused with "precomputation" described subsequently in the text. The two are distinguished in note 74 infra following the textual discussion of precomputation.

[78] Ayres, *op. cit. supra* note 74, at 160–170.

[79] It is to be noted that the third installment is due and payable at the *end* of the third installment period. That is, the first installment period runs from the date the loan is made to the date of the first scheduled installment payment, the second installment period runs from the date of the first scheduled installment payment to the date of the second scheduled installment period, etc.

DISCOUNT

Dollar discount is similar to dollar add-on except that the proceeds to the borrower are reduced by the amount of the discount, but the full amount is repaid. For example, considering a $1000 one year loan again, if the discount is 6% the amount received by the borrower is $1000 less $60. However the amount repaid would be $83.33 per month, or $1000. The annual percentage rate would be about 11.6%.

PRECOMPUTATION

Precomputation is a procedure authorized by many states to facilitate clerical operations. Essentially, the operation appears to consist of adding the finance charge (however determined) to the amount to be financed and dividing by the number of payments to find the amount of each payment.

Excerpts from Barbara Curran's "Trends in Consumer Credit Legislation" are given below. They explain the device in greater detail.

"Charges are precomputed in the following manner: after the lender and the borrower arrange the amount of the loan and determine the schedule for installment payments of principal, the lender computes the charges which would accrue over the term of the loan if the borrower were to repay the principal amount exactly in accordance with the installment schedule agreed upon; he then adds the charges so computed to the principal and divides by the number of installments scheduled to determine the amount of each installment payment which now represents charges and principal combined.[72] The advantage in using the precomputation method lies in the fact that not only will the amounts of all installment payments be substantially equal but the lender will not be put to the trouble of allocating principal and charges as each installment payment is made.[73]

---

[72] It is not suggested here that a lender follows the precise steps indicated in the text for each loan. Not only is there a redundant step in the procedure as described in the text but, as a practical matter, most lenders would have charts for speedy reference by clerks which would give the necessary information about charges for a particular loan.

[73] It would seem most lenders would have charts available for use by clerical help which would show the allocation information for loans paid on schedule, and the actual computation would not need to be made each time, even for non-precomputed loans. However, the dollar allocation of principal and charges would, under the uniform act. have to be entered on the loan records.

[74] Precomputation is not to be confused with the method described in note 56 supra. The method described in note 56 is merely a means by which the lender selects a different amount for each monthly installment of principal so that when each such installment of principal is added to the charges computed for the principal outstanding during the preceding month, the sum of principal and charges will be the same for all installments, even though the amount allocated to principal and the amount allocated to charges for all installments is different. The following tables taken from Ayres, Instalment Mathematics Handbook (1946), should illustrate the difference:

"TABLE I.—STANDARD METHOD (UNIFORM PRINCIPAL PAYMENTS WITH INTEREST ON DECLINING BALANCES)

"Balances	Interest	Principal	Total payment
$300	$6	$50	$56
250	5	50	55
200	4	50	54
150	3	50	53
100	2	50	52
50	1	50	51
----------	21	300	321

Id. at 202.

In the report of the 1954 Subcommittee, Senator McCarran is quoted in reference to the McCarran Act, Public Law 15, which delegated to the states power to regulate the business of insurance, subject to the ultimate authority of the Federal government. Senator McCarran said in part:

"In enacting this law Congress held out an invitation to the States to deal *affirmatively* and *effectively* with the activities and practices of the insurance business which might otherwise be the subject of Federal regulation. . . . The Congress, therefore, has the duty to be vigilant of the public interest. . . . We must recognize that silence on the part of Congress depends primarily, not upon the extent or type of regulation imposed by the various states, or by any state, *but rather upon the success of such regulation.*" [Italic supplied.]

The Subcommittee concluded with an admonition that they would "not forever accept 'attempts' at regulation as a substitute for regulation of the business of insurance by the states. The patience of the Federal Government with those who would abuse the good name of insurance may come to an end."

It certainly is time for the Subcommittee to take another look at credit insurance for there is serious doubt whether the states, as a group, are dealing affirmatively and effectively with this problem thirteen years after the Subcommittee's warning.

Those who must borrow or buy on time are, in a financial sense, "the least among us," hardly in a position to pay exhorbitant credit insurance premiums on top of all their other burdens. They need and deserve your assistance.

[From the Washington (D.C.) Wall Street Journal, July 14, 1967]

SENATE UNIT STUDYING NEW YORK BANKS' ALLEGEDLY EXCESSIVE LOAN INSURANCE FEES

By Stanford N. Sesser, Staff Reporter of The Wall Street Journal

NEW YORK.—A Congressional committee is known to be investigating allegations that major New York City banks are reaping a windfall from the installment loan business by charging rates for life insurance on these loans that exceed the maximum permitted by the New York State Insurance Department.

The investigation is being conducted by the Senate Antitrust subcommittee. The group chaired by Sen. A. Hart (D., Mich.), held hearings in May that exposed widespread credit life insurance abuses in the dealings of finance companies with insurers. The hearings are scheduled to resume in the fall.

While the charges against the New York banks aren't considered as serious as many of the abuses uncovered by the committee in May, they still could have widespread repercussions. An indication that credit life malpractices have spread to some of the nation's largest financial institutions could spur the drive toward Federal regulation of insurance sales.

No details of the committee's investigation of the New York banks could be learned, but conversations with banking and insurance executives and New York State regulators indicate that the controversy centers on the pricing of life insurance for secured loans—loans against which something is pledged. The most common type of secured loan is for the purchase of an automobile.

New York banks offer auto and other secured loans at the rate of $4.75 a year, deducted in advance, for each $100 borrowed. If the borrower asks for credit life insurance, as almost all do, he's told that the charge for his loan will be $5.25 per $100.

This would indicate a charge for life insurance of 50 cents per $100. However, New York State insurance regulations specify a maximum rate of 44 cents for large-volume institutions.

Banks place their credit life business with insurance companies, and technically the 44-cent maximum applies only to the rate that the insurer can charge the bank. But the state's banking law specifies that the bank is governed by the same restrictions in its dealings with the borrower.

The New York banks don't pay the entire 50 cents to the insurance companies with which they deal; they pay only the rate that the insurer has filed with the state insurance department. These rates sometimes are even lower than the 44-cent maximum; it's believed they range all the way down to 38 cents.

Thus, it's being alleged that the banks charge the borrower 50 cents per $100 in credit life insurance, pay their insurance companies from 38 cents to 44 cents, and pocket the difference. Borrowers in New York State paid $31 million in credit life premiums in 1965; it's not known what portion of this business was done through New York City banks.

According to the American Bankers Association the five largest New York banks with instalment loan operations are First National City Bank, Manufacturers Hanover Trust Co., Bankers Trust Co., Chase Manhattan Bank, and Chemical Bank New York Trust Co. The first three place their credit life business with Prudential Insurance Co. of America; Chase Manhattan deals with Equitable Life Assurance Society of the United States; and Chemical gives its business to New York Life Insurance Co.

Executives at the five banks were asked to comment on the alleged credit life overcharges. Four of the banks replied that the loans at $4.75 and $5.25 weren't directly comparable, so the assumption that the charge for credit life insurance is 50 cents isn't necessarily accurate.

The banks explained, for example, that an auto loan is made at $4.75 without life insurance. However, if the borrower wants insurance coverage, he's instead given a $5.25 "personal loan." They're different types of loans; they can't be compared," George Beatty, vice president of Bankers Trust, stated.

In a personal loan, Mr. Beatty explained, the banks give no breakdowns of the basic loan charge and the charge for credit life insurance.

At least one banker, however holds that the difference is largely a legal technicality, rather than a change in provisions. "It's still a secured loan, even if you have credit life insurance," said an official of First National City Bank, referring to auto loans.

An executive at the fifth bank, who asked not to be identified, conceded that the bank is, in effect, charging 50 cents for its credit life. He said the rate exceeds the 44-cent maximum because the bank incurs extra bookkeeping charges even though the policies are issued by an insurance company. Among the extra charges, he mentioned the "cost of handling the life insurance premiums, passing them on to the insurer, and processing the death claims."

The banks that issue $5.25 "personal loans" with credit life don't give a breakdown of what part of the charge represents the insurance. "We throw in the life insurance—it's not an identifiable charge to the customer," one executive said.

John K. Lundberg, first deputy superintendent of the New York State Banking Department, said he couldn't comment on credit life insurance practices without give the matter study. If the department were to consider the issue, it would undoubtedly have to rule on a key question: Whether the banks' pricing practices become legal simply because "they don't include credit life insurance as an identifiable charge in their $5.25 loan.

Section 108 of the New York banking regulations says that the banks may charge borrowers for credit life insurance "at a rate not in excess of the premiums chargeable . . . in accordance with rate schedules then in effect and on file with the Superintendent of Insurance for such insurance by the Insurer."

John Kittredge, a Prudential vice president, said the company has had "discussions with several of the New York banks." He said that Prudential told the banks that some people have the "impression they were, in fact, charging 50 cents" on their credit life insurance. He emphasized that Prudential was only "bringing this impression to their attention" and not drawing any conclusions.

John F. Ryan, senior vice president of New York Life, said he also has had "conversations" with a bank. He added that New York Life is studying the pricing of credit life insurance, but hasn't yet reached a conclusion.

Insurance executives have privately expressed fears that Senator Hart's credit life hearings will prove so damaging to the industry it will provoke widespread demand for Federal regulation. The fact the investigation has been extended to New York is considered significant: New York is widely reputed to have the nation's strictest insurance regulations.

The committee's hearings disclosed that in most other states the rate usually charged for credit life insurance is $1 per $100, and often the rates aren't regulated by the state insurance department. The committee detailed charges of kickbacks among some finance companies and their allegedly dummy insurance subsidiaries on their credit life business.

It's understood the committee soon will be investigating the question of whether the practices attributed to the New York banks also apply to finance companies operating in New York.

Although the standard credit life rate outside New York is $1, apparently New York insurance companies and banks are finding business profitable at half that rate. One banker tells of a New York bank that used to pay employees a commission if they'd sell auto loans that included credit life insurance. The banker says he's not sure if the practice still exists.

Most New York banks also offer life insurance with "passbook loans"—when the borrower uses the money in his savings account as collateral. Some bankers and insurance executives sharply question the practice of selling life insurance when the loan is fully backed by cash in the bank.

In the May Congressional hearings James Hunt, Vermont's commissioner of banking and insurance, estimated that borrowers nationwide are being overcharged $175 million annually for insurance.

(Mr. Paul H. Douglas, Chairman, Commission on Urban Problems, submitted the following exhibits for inclusion in the record:)

THE FOLLOWING INFORMATION IS LACKING:

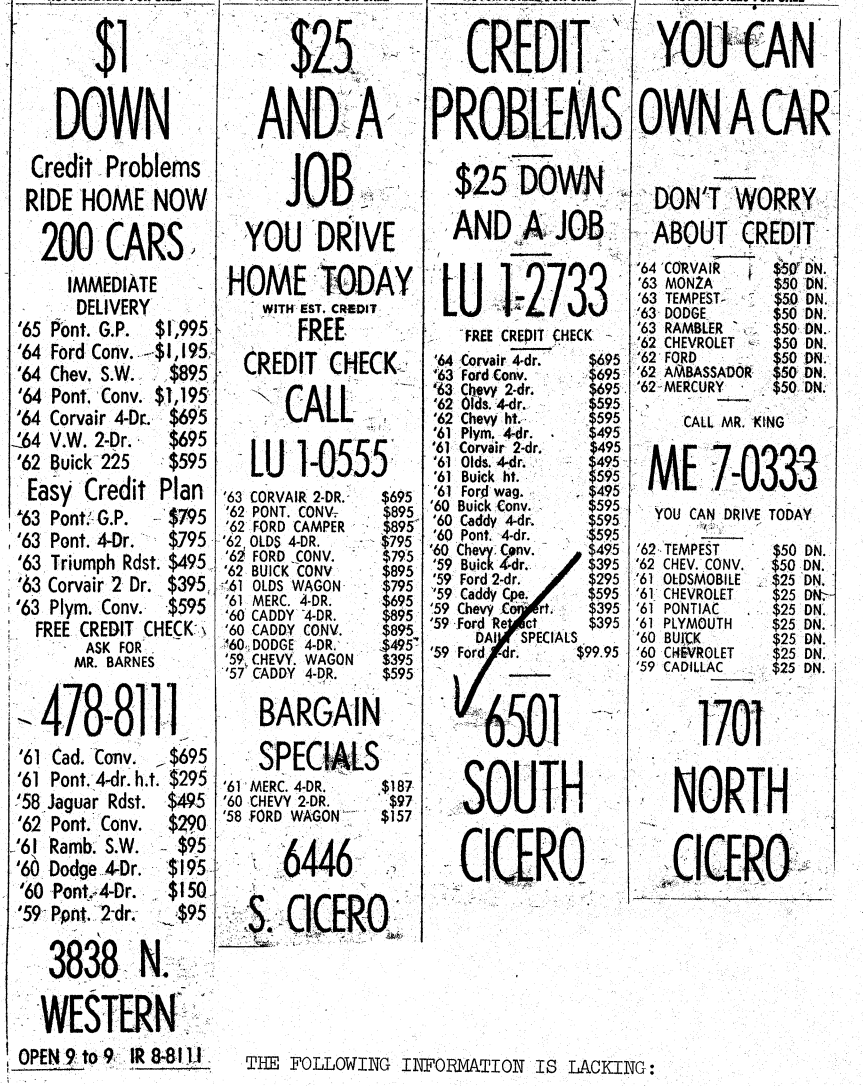
(1) Specific downpayment for each advertised auto
(2) Amount to be financed
(3) Number of payments
(4) Amount of each payment
(5) Total finance charge
(6) Annual percentage rate

THE FOLLOWING INFORMATION IS LACKING:

(1) Amount of loan
(2) Total finance charge
(3) Annual percentage rate

THE FOLLOWING INFORMATION IS LACKING:

(1) Cash price for each pictured appliance
(2) Number of payments
(3) Total finance charge
(4) Annual percentage rate



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'61 MERC. 4-DR.	$695
'60 CADDY 4-DR.	$895
'60 CADDY CONV.	$895
'60 DODGE 4-DR.	$495
'59 CHEVY. WAGON	$395
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'62 Chevy ht.	$595
'61 Plym. 4-dr.	$495
'61 Corvair 2-dr.	$495
'61 Olds. 4-dr.	$495
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'61 Ford wag.	$495
'60 Buick Conv.	$595
'60 Caddy 4-dr.	$595
'60 Pont. 4-dr.	$595
'60 Chevy Conv.	$495
'59 Buick 4-dr.	$395
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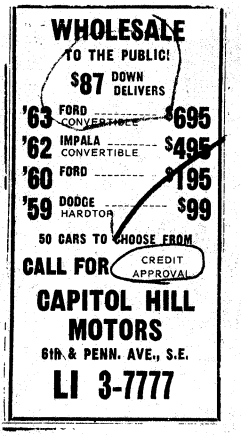
'61 PONTIAC	$25 DN.
'61 PLYMOUTH	$25 DN.
'60 BUICK	$25 DN.
'60 CHEVROLET	$25 DN.
'59 CADILLAC	$25 DN.

1701 NORTH CICERO

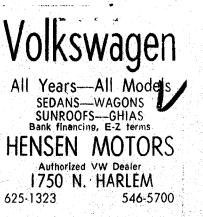
THE FOLLOWING INFORMATION IS LACKING:

(1) Number of payments
(2) Amount of each payment
(3) Total finance charge
(4) Annual percentage rate

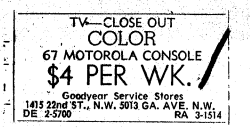
The following information is lacking:
(1) Amount to be financed
(2) Number of payments
(3) Size of each payment
(4) Total finance charge
(5) Annual percentage rate



The following information is lacking:
(1) Amount to be financed
(2) Amount of each payment
(3) Number of payments
(4) Total finance charge
(5) Annual percentage rate



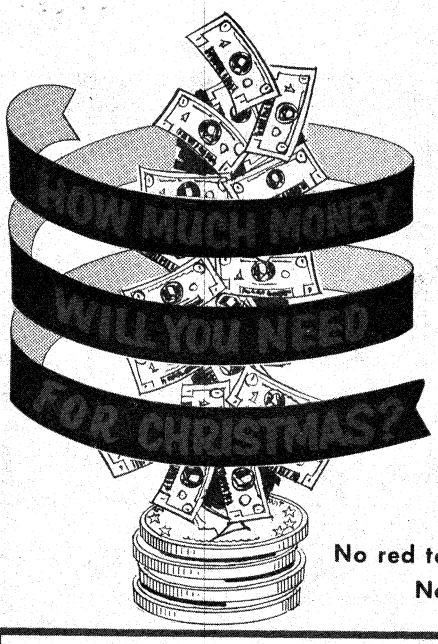
The following information is lacking:
(1) Downpayment requirements
(2) Annual percentage rate



The following information is lacking:
(1) Cash price
(2) Downpayment
(3) Amount to be financed
(4) Number of payments
(5) Total finance charge
(6) Annual percentage rate

THE FOLLOWING INFORMATION IS LACKING:

(1) Downpayment
(2) Amount to be financed
(3) Number of payments
(4) Total finance charge
(5) Annual percentage rate



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THE FOLLOWING INFORMATION IS LACKING:

(1) Size of payments
(2) Number of payments
(3) Total finance charge
(4) Annual percentage rate

(Hon. Frank Annunzio submitted the following article for the record:)

[From U.S. Department of Labor, Bureau of Labor Standards, May 1967]

AMOUNT OF EARNING EXEMPTED FROM GARNISHMENT UNDER STATE LAWS *

Alabama.—75% of wages or other compensation of State residents, due or to become due. (Alabama Code T. 7, sec. 630.)

Alaska.—$350 income from any source within the preceding 30 days for a family head, $200 for a single man, if necessary, for his use or the use of his family supported in whole or in part by his labor. Amounts which he has been ordered to pay for child support are also exempt. (Alaska Statutes, secs. 09. 35.080(1); 9.35.085.)

Arizona.—50% of earnings for the preceding 30 days if necessary for the use of the debtor's family supported in whole or in part by his labor. (Arizona Revised Statutes Anno., secs. 12–1594; 33–1126.)

Arkansas.—100% of wages of a resident laborer or mechanic for 60 days, provided his wages plus other personal property do not exceed $500 for a married person or family head or $200 for a single person; with an assured minimum exemption for all laborers and mechanics of the first $25 a week of net wages. (Arkansas Constitution, Art. 9, sec. 2; Arkansas Statutes, sec. 30.207.)

California.—50% of the preceding 30 days' earnings. 100% if necessary for the use of the debtor's family residing in the State and supported wholly or in part by him; 50% if the debts are for necessaries of personal services. (California Code of Civil Procedure, sec. 690.11.)

Colorado.—70% of earnings due the head of a family and 35% of earnings due single persons, except for payment of taxes. (Colorado Revised Statutes, sec. 77–2–4; 77–2–5.)

Connecticut.—Court may set the amount to be paid, taking into consideration the circumstances of the debtor. If he fails to obey the order, amounts over $50 per week plus taxes may be taken as a continuing levy until paid. (Connecticut General Statutes, sec. 52–361.)

Delaware.—100% in New Castle County, except that 10% may be taken for debts for necessaries or State taxes. 60% of earnings of residents of Kent and Sussex Counties. In all three counties the exemptions do not apply to claims up to $50 for board or lodging. (Delaware Code Anno., T. 10, sec. 4913.)

District of Columbia.—90% of the first $200 per month; 80% of the next $300; 50% of the balance due or to become due. The attachment is a lien and continuing levy until the judgment is paid. (D. C. Code Anno., sec. 16–572.)

Florida.—100% of earnings due the head of a family residing in the State. (Florida Statutes, sec. 222.11.)

Georgia.—$3 per day plus 50% of the balance. Garnishment is a lien on present and future wages. (Georgia Code Anno., sec. 46–208.)

Hawaii.—95% of the first $100 per month; 90% of the next $100 per month; and 80% of the balance of wages due or to become due. (Hawaii Revised Laws, sec. 237–1.)

Idaho.—50% if the debt is for necessaries, otherwise 75% of the preceding 30 days' earnings if necessary for the use of the resident debtor's family residing in the State, supported in whole or in part by his labor. Maximum $100 at any one time. (Idaho Code Anno., sec. 11–205.)

Illinois.—$45 per week or 85% of gross wages, whichever is greater, but not exceeding $200 per week. (Illinois Revised Statutes, Ch. 62, sec. 73.)

Indiana.—$15 per week and 90% of the balance of income and profits of a resident householder. (Indiana Anno. Statutes, sec. 2–3501.)

Iowa.—$35 per week of wages or salary due the head of a family, exclusive of deductions for taxes, plus $3 for each dependent under 18. No creditor may garnish for more than $150, plus costs (Iowa Code, sec. 627.10.)

Kansas.—90% of 1 month's earnings of a resident debtor (less court costs up to $4) if necessary for the use of a family supported in whole or in part by his labor. (Kansas General Statutes Anno., sec. 60–2310.)

Kentucky.—50% of earnings is exempt if the judgment is for debts for necessaries (food, clothing, medical expenses, rent, or public utilities) otherwise 75% of net earnings in any pay period (earnings due less deductions for govern-

*Such references as "earnings for the preceding 30 days" mean earnings for 30 days prior to the service of a writ of garnishment on the employer. Exclusions for such debts as taxes, alimony, or support orders are listed only when they appear in the exemption provision itself.

mental fees and taxes, union dues, medical insurance, and retirement programs). Not applicable to garnishments for child support. (Kentucky Revised Statutes, secs. 427.010; 425.210.)

Louisiana.—80% of earnings; minimum $100 monthly. (Louisiana Revised Statutes, sec. 13:3881.)

Maine.—$40 per week of wages due; minimum $10. (Maine Revised Statutes, T. 14, sec. 2602.)

Maryland.—$100 earnings due, except in Caroline, Cecil, Kent, Queen Anne's, and Worcester Counties, where the exemption is 75% of all earnings due. Not applicable to claims for State income taxes. (Maryland Anno., Code, Art. 9, secs. 31,31A, 31B.)

Massachusetts—$50 per week of wages due. (Massachusetts General Laws, Ch. 246, sec. 28.)

Michigan.—For a householder having a family:

	Percent	Minimum	Maximum	Wages due
First garnishment	60	$30	$50	Up to 1 week.
		60	90	More than 1 week.
All other cases	60	12	30	Up to 1 week.
		24	60	1 week to 16 days.
		30	60	Over 16 days.
For other persons:				
1st garnishment	40	20	50	
All other cases	30	10	20	

Source: Michigan Statutes Annotated, 27A.7511.

Minnesota.—50% of resident's current unpaid net wages (less amounts required by law to be deducted or withheld). All earnings for the preceding 30 days if necessary for the use of a family supported wholly or partly by his labor. (Minnesota Statutes Anno. secs. 550.37(13); 575.05.)

Mississippi.—75% of resident's earnings due or to become due. The garnishment is a continuing levy until the amount due is accumulated. Does not apply to orders or judgments for alimony, separate maintenance, or child support. (Mississippi Code Anno. sec. 307.)

Missouri.—90% of the previous 30 days' wages due a resident head of a family. (Missouri Revised Statutes, sec. 525.030.)

Montana.—50% in cases of debts for gasoline or necessaries, otherwise 100% of earnings of a married person or family head for the preceding 45 days if necessary for the use of the debtor's family supported in whole or in part by his labor. All earnings for the preceding 30 days are exempt in actions for $10 or less. (Montana Revised Codes, sec. 93–5816.)

Nebraska.—90% of wages of the head of a family. (Nebraska Revised Statutes, sec. 25–1558.)

Nevada.—50% in cases of debts for necessaries, otherwise 100% of earnings for the preceding 30 days if necessary for the use of the debtor's resident family supported in whole or in part by his labor. 50% of such earnings for debtors without a family residing in the State. (Nevada Revised Statutes, sec. 21.090.)

New Hampshire.—$20 per week of wages due, and all wages earned after service of the writ. (New Hampshire Revised Statutes Anno., sec. 512:21.)

New Jersey.—90% of earnings due or to become due; 100% of less than $18 per week. Court may decrease if debtor's income exceeds $2500 per year. The execution is a lien and continuing levy until paid. (New Jersey Revised Statutes, secs. 2A:17–50, 2A:17–56.)

New Mexico.—75% of the previous days' earnings of the head of a resident family; 80% of his earnings are $100 or less for the period. (New Mexico Statutes Anno., sec. 26–2–27.)

New York.—90% of earnings; 100% if earnings are $30 per week or less. The execution affects earnings due or to become due. (New York Civil Practice Laws and Rules, sec. 5231.)

North Carolina.—100% of earnings for the preceding 60 days if necessary for the use of the debtor's family supported in whole or in part by his labor. (North Carolina General Statutes, sec. 1–362.)

North Dakota.—$50 per week plus $5 per week for each dependent (up to $25) of the wages or salary of a resident debtor who is the head of a family. $35 per

week for residents not the head of a family. (North Dakota Century Code Anno., sec. 32–09–02.)

Ohio.—80% of the first $300 and 60% of the balance of the preceding 30 days' earnings of a family head or a widow; minimum $150. $100 of the previous 30 days' earnings of other residents. (Ohio Revised Code Anno., secs. 2329.66, 2329.62.)

Oklahoma.—75% of the previous 90 days' earnings. 100% if necessary for the maintenance of a family supported wholly or partly by the labor of the resident debtor, except for child support orders. (Oklahoma Statutes Anno., T. 31, secs. 1, 1.1, 4.)

Oregon.—50% of earnings due after deductions for taxes; minimum $25 and maximum $250 in any 30 day period. (Not applicable to process to collect State income taxes owed by the debtor or to enforce judgments for damages for fraud.) (Oregon Revised States, sec. 23.180.)

Pennsylvania.—100% of earnings. (Pennsylvania Statutes, T. 42, sec. 886.)

Puerto Rico.—75% of a resident's earnings for the preceding 30 days if necessary for the use of his resident family, supported wholly or in part by his labor. (Laws of Puerto Rico Anno., T. 32, sec. 1130.)

Rhode Island.—$50 of earnings due. (Rhode Island General Laws Anno., sec. 9–26–4.)

South Carolina.—100% of the preceding 60 days' earnings if necessary for the use of a family supported wholly or in part by his labor. However, up to 15% of earnings due may be ordered when the judgment is on food, fuel, or medicine accounts, up to a maximum of $100. (South Carolina Code, sec. 10–1731.) For debts contracted in South Carolina prohibits garnishment of resident employee under an out-of-State garnishment unless based on a South Carolina judgment.

South Dakota.—100% of the preceding 60 days' earnings if necessary for the use of the debtor's family supported wholly or partly by his labor. (South Dakota Code, sec. 33.2404.)

Tennessee.—$17 earnings per week plus $2.50 per week for each dependent child under 16 years, for a resident head of a family. $12 per week for other residents. Exemption does not apply to debts for alimony or support, taxes or fines. (Tennessee Code Anno., secs. 26–207—209.)

Texas.—100% of current wages. (Texas Constitution, Art. 16, sec. 28; Civil Statutes, Arts. 3832, 3935, 4099.)

Utah.—50% of the preceding 30 days' earnings of a married man or head of a resident family, if necessary for the use of his family supported wholly or in part by his labor. Minimum $50. (Utah Code Anno., sec. 78–23–1.)

Vermont.—$30 per week plus 50% of compensation due in excess of $60 per week. (Vermont Statutes Anno., T. 12, sec. 3020.)

Virginia.—$100 per month plus 75% of the balance, but not more than $150 of the monthly earnings of the head of a family. 50% of the exemption above for other persons. (Exemption is also enumerated for weekly, bi-weekly, or semi-monthly pay periods.) (Virginia Code Anno., sec. 34–29.)

Washington.—$35 per week plus $5 per dependent (maximum $50 per week) for a debtor with dependents. $25 per week for persons without dependents. (Washington Revised Code, sec. 7.32.280.)

West Virginia.—80% of earnings due or to become due. Minimum $20 per week. The execution is a lien and continuing levy on wages due or to become due within 1 year. (West Virginia Code, sec. 3834.)

Wisconsin.—$120 income of a debtor with dependents (after deductions for State and Federal taxes) plus $20 per dependent, for each 30 day period prior to service of process, but not more than 75% of net income. 60% of such income of a debtor without dependents, but not less than $75 nor more than $100. (May also be computed on a 90-day basis.) (Wisconsin Statutes Anno., sec. 272.18.)

Wyoming.—50% of the previous 60 days' earnings when necessary for the use of the debtor's resident family, supported wholly or in part by his labor. (Wyoming Statutes Anno., sec. 1–422.)

(Rev. Robert J. McEwen, chairman, Department of Economics, Boston College, Chestnut Hill, Mass., submitted the following publication for inclusion in the record:)

Economic Issues in State Regulation of Consumer Credit

By

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ECONOMIC ISSUES IN STATE REGULATION OF CONSUMER CREDIT

ROBERT J. MCEWEN, S.J.*

I. INTRODUCTION

Forty years ago, Professor E. R. A. Seligman opened a session of the annual meeting of the Academy of Political Sciences with a very thoughtful and farsighted paper on "Economic Problems Involved in Installment Selling." With remarkable insight, he concluded his paper with the following warning:

> [I]t must not be forgotten that installment selling, like every institution, is subject to the perils of novelty. If this were the time to deal with the subject fully, it could be pointed out that in the course of history credit has assumed manifold forms; and each new form of credit has had to fight its way to recognition after going through three stages: that of initial growth, that of the sloughing off of abuses, and that of the final emergence of the soundness of the principle.
>
> While [installment selling] . . . has undoubtedly come to stay, all manner of abuses and of perils which it would be shortsighted to deny have crept in. What is needed is a sober and impartial analysis of its true significance. As the years roll by, outworn methods will be discarded; new corruptions will appear. Is it not the part of wisdom to separate the chaff from the grain; to be on our guard against the more obvious dangers; and to eliminate . . . improper practices . . . ?[1]

Today, state regulation has become an important, but much misunderstood phase of the community's attempt through government action

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[1] Seligman, Economic Problems Involved in Installment Selling, 12 Acad. Pol. Sci. Proc. 583, 594 (1927).

to insure that the economic processes of borrowing and lending promote the general public welfare.

If they are to be sound, arguments for enacting legal control of consumer credit must rely on the best economic and social research and analysis available. Unfortunately for the public interest, in this as in many other areas of policymaking through legislation, pressures from pecuniary self-interest are so great that they lead to enormous concealment of fact and distortion of analysis. To uncover the real economic issues underlying state consumer-credit laws is the primary purpose of this article.[2] Three issues are selected for extended discussion, mainly because of their appearance in credit-industry arguments presented in the course of debate on consumer-credit legislation.

1. What is the precise definition of consumer credit? Are legal regulations commensurate with the appropriate economic definitions?

2. What must the state do to establish framework conditions on both the demand and the supply side of the consumer-credit market in order to make it function more effectively and more in the public interest? On the demand side of the market this refers particularly to state action requiring disclosure of information useful to the customer. On the supply side this refers to state control of operating methods of the companies, with particular reference to selling and collection practices, credit-rating bureaus, and the relationship of financing agencies to sellers of merchandise.

3. Can competition be relied upon to produce fair rates after the state has established the framework conditions surrounding the market? If competition in the market cannot be relied upon, then should the state set rates, or should the state set ceilings far above the prevailing rates and designed merely to ward off instances of gross extortion?

II. Definition of Consumer Credit

A definition of consumer credit is necessary in order to identify and classify the realities of that to which regulation might be directed.

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2 It should be emphasized that this article is by no means a complete treatment of the importance or significance of consumer credit in the functioning of the national economy. The questions raised by this issue include the following: (1) Does consumer credit constitute a destabilizing force in the economy? Does it really stimulate consumer saving? (2) In enabling him to enjoy goods and services before accumulating the income to pay cash for them, does consumer credit benefit or harm the consumer? (3) Does consumer credit benefit producers by expanding product markets and allowing the production economies that go with an increased volume? (4) If the objective and subjective gains from the use of credit, whether they be monetary or nonmonetary, are greater than the costs, is not consumer welfare really increased? These questions have been raised by economic writers since the earliest days of installment credit. See Neufeld, The Economic Significance of Consumer Credit, in Consumer Credit in Canada 5 (Ziegel & Olley ed. 1966).

In a sense, definitions are names we agree to give to things, and the most important element is precision of expression and consistency of use both by the definer and by all others dealing with the same reality. It is quite true that a definition, to be meaningful, must be related to the purpose of the discussion in which it is used. For this reason, legal and economic definitions do not have to withstand the same tests. In economic analysis, for instance, trends in the magnitude of consumer credit are important items of information. For legal purposes, however, the precise nature and essence of the business transactions are more important than their volume or fluctuation.

One way to define consumer credit is to say that it is purchasing power advanced to individual consumers, usually in relatively small amounts, for the purchase of consumer goods and services.[3] This definition advances the present discussion only insofar as it includes all those transactions to which consumer-credit legislation can reasonably be directed. Because of the difficulties in classifying types of credit, the definition, to be helpful, must be construed broadly. If legislation cannot precisely include those activities which are capable of producing the evil sought to be prevented, it seems more appropriate, in view of the desired objectives, that such legislation be overinclusive rather than underinclusive.

The difficulties inherent in defining and classifying the various types of consumer credit were well stated by Albert Hart:

> The loan classification of the Federal Reserve . . . shows a mixture of at least three classification principles: (A) the line of business in which the borrower is engaged . . .; (B) the type of collateral . . .; (C) the purpose of the loan . . . . Since the "purpose" of a loan can often be described in several alternative ways, many economists are skeptical of principle C. If either A or B—preferably both—could be carried consistently across the whole mass of loans, bank statistics would be more illuminating.[4]

In viewing broadly the nature of consumer credit, therefore, one must consider an important principle more properly applied to all credit and not just to consumer credit:

> The purpose of consumer credit is to enable the borrower to enjoy income before he has earned it or received it. Consumer credit comes into existence whenever an individual acquires

[3] As normally used in banking statistics, the figures for consumer credit exclude borrowing for investment in securities, real estate, or home construction.

[4] Hart, Money, Debt, Economic Activity 55 (2d ed. 1953).

> funds or goods for personal use in return for a promise to pay for the same in the future.[5]

An important economic truth which is embodied in this quotation has, unhappily, been freely ignored and distorted by legislators and courts for too many years. It should be emphasized that credit or a loan is involved in every exchange in which there is *delay* in completing the transaction. In any case in which the buyer does not render payment to the seller upon acquisition of the seller's goods or services, the economic reality of the situation requires us to acknowledge that the seller is making a loan to the buyer of the value of those goods or services for as long a period as it takes the buyer to complete his payment.[6] This concept is often obscured and disfigured by legislated subterfuge, either to avoid the honest statement of actual interest and finance charges or to evade legally prescribed maximum rates of interest. Its importance, however, requires that it be embodied in the definition of consumer credit.

A difficulty in a definition as a basis for regulation can arise because of the nature of the goods for which consumer credit is used. The general distinction between a consumer good and a producer good is frequently obvious; there are not too many overlapping or indistinguishable cases that present much difficulty. However, it does make sense to conceive of consumer credit as any method by which an individual consumer has access to immediate purchasing power, in return for which he obligates himself to make specified future payments out of his income. Thus, a definition should include the transactions which permit the consumer to acquire certain goods that might also be considered producer goods. Furthermore, in those cases where an item that is ordinarily a consumer good can also be used as a producer good (*e.g.*, an automobile), it would seem that legal regulations on the matter should tend to include all loans made for that particular good, on the theory that no great harm will be done by overinclusion, but that great complexity and harm may result from opening loopholes that might be exploited. Because of the nature of personal cash loans, it seems appropriate to include all such loans under the heading of consumer credit without attempting to find out whether the money will be spent to buy a consumer good, to pay off previous debts incurred for the purchase of consumer goods, to lend the proceeds to an uncle for the purchase of securities, or to put the funds to any of the hundreds of uses consumers can find for the proceeds of personal loans.

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[5] Stokes & Arlt, Money, Banking and the Financial System 593 (1955).

[6] Writers of books on credit frequently admit this point in early chapters and then proceed to ignore it in subtle attempts to justify the "time-price differential." See Bartels, Credit Management 4 (1967); Neufeld, Manual on Consumer Credit 4, 88-92 (1961).

What has been said so far about the difficulty of defining and isolating consumer credit emphasizes the problem of data-gathering in this field.[7] From an economic point of view, the main objective of gathering such information is the ascertainment of significant trends in the use of credit—trends that may have important bearing on the national economy as a whole or on the behavior of consumers specifically. From the particular point of view of protecting individual consumers, all credit transactions should be included in which research has uncovered some element of deception or abuse. On this principle, we must recognize the unreality of the legal distinction between cash credit and vendor credit. No useful analytical purpose is served by the attempt to separate transactions of this sort. They are each in essence one and the same thing—a postponement of one half of the exchange transaction. Thus, both must be included in the definition of consumer credit.

Care should be taken to exclude from coverage those transactions which are not forms of consumer credit, even though they may include consumer-credit elements. Some authors, for example, attempt to identify lease arrangements as a form of consumer credit.[8] Such a classification, however, appears to be a mistake, because there really is no granting of credit in a lease. With the possible exception of lease arrangements that include an option to purchase at the end of the term, straight leases are nothing more than the purchase, for a fixed amount, of a specified service for a specified time. For instance, if one leases an automobile for a week or a month, he purchases for a price expressed simply in dollars the use of this machine for that period of time. Since everything is "pay as you go," such economic transactions do not belong under the heading of consumer credit.[9] To call these arrangements merely other means of financing simply confuses the picture. It is true that, in a long-term lease, the lessee obligates himself to definite payments for definite future time periods. But these payments are tied to the enjoyment of definite future services which the lessor obligates himself to provide. In effect, the lessee is as much granting the lessor credit as the lessor is granting it to the lessee. Moreover, if the leased item should be destroyed, the lease ceases to operate. The continued existence of a consumer good purchased on time, however, in no way affects the validity of the installment contract; money which has been advanced must be repaid.

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[7] See generally Jones, Measurement of Consumer Credit, 48 U. Ill. Bull. 83-99 (1951).

[8] See, e.g., The Mortgaged Society, Forbes, Dec. 1, 1965, p. 51.

[9] It should be noted, however, that credit can be extended in conjunction with a lease arrangement. To the extent that use of the leased item precedes payment for such use, the lessor has extended credit to the lessee, in the same manner that a vendor grants credit to a vendee by permitting use before payment.

A recent article in *Forbes* discussed a "new look" at personal debt, and by implication suggested that adoption of this view would make discussion of consumer credit more meaningful.

> Some economists—notably economists in the Federal Government and in the nation's major corporations—argue that a whole new look should be taken at exactly what is personal debt. If renting an apartment is not considered a debt but a cost, is it fair to assess mortgage payments as "credit" payments? If a man signs a three-year lease at $150 a month, isn't he as much "in debt" (for $5,400) as a man who borrows money to buy a house? Similarly, no one regards the cost of going to work by commuter train as "going into debt." Should payments on a car used for the same purpose be regarded as evidence of debt? Isn't much of what is now called consumer debt merely a replacement for services that people used to buy?[10]

Unfortunately, this supposed insight is not an improvement but a further confusion. Credit laws should be aimed at protection of owner as borrower, not as user, and thus consumer credit must be defined accordingly—in terms of borrower.

It is important to distinguish carefully between the product or the service obtained by a purchaser and the time and the source of the funds or other thing of value by which the transaction is consummated. If there is any delay between the obtaining of the good or service and the handing over of its equivalent price in goods, or more commonly money, then we have an instance of consumer credit. Someone—the purchaser—has come into possession of useful assets whose employment could otherwise produce a return to the person in control or possession of them. Whether the repayment interval be small or great, the possession of assets or the enjoyment of services prior to the fulfillment of the other side of the exchange is properly called credit. The law can reasonably decide which varieties of credit phenomena present problems of public welfare that deserve control, but the law should never speak or act as if certain transactions do not involve credit when essentially they do, nor as if certain transactions do involve credit when essentially they do not.

III. Legal Control of Market Framework Conditions

Most economists would agree on the fundamental requirements for the proper functioning of a mixed capitalistic economy such as exists in the United States today. Given the proper institutional framework,

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10 The Mortgaged Society, supra note 8, at 51.

free producer and consumer decisions—to buy and sell, to save and invest, to produce this product or that product—lead to the best possible allocation of resources. Such choices must be made through a market operating within a social framework which is at least partially the result of legal requirements. Strictly speaking, these legal requirements are not interferences with market operation, but instead are needed guidelines or boundaries which preserve the possibility of a truly free and informed expression of buyers' and sellers' preferences in the market.

From the buyer's point of view, the two chief requirements are *adequacy of information* on which to base a rational choice and *freedom from any coercion* that could force his choice along certain lines. From the point of view of the selling side of the market, fairness requires that there must be no collusion or constraints on the offerings of competing sellers. Because the system is fueled by self-interest, legal proscriptions to prevent forms of monopolistic control, deceit, and misrepresentation are absolutely essential to the proper operation of a market economy. Only then is there a possibility of achieving maximum consumer welfare. For this reason, even the most libertarian economists and political scientists should and do logically accept the principle of some legal control of consumer credit. What matters is that the controls promise to accomplish the objectives italicized above.

The justification for governmental control of consumer credit, as well as of credit in general, is closely intertwined with the economic nature of money and credit.[11] Indeed, in most modern economies, many transactions between buyer and seller, or borrower and lender, are based ultimately upon the lender having access to the money-creating powers of the commercial-banking system.[12] As R. I. Robinson put it:

> The collective demands of consumers for credit are channeled back to the money and capital markets through a variety of financial institutions. The most important and also the most complex of these institutions in the market are commercial banks. Commercial banks have at least three different channels of extending credit to consumers: they do it directly in the form of cash loans, they purchase installment paper from the auto and other dealers who originate it, and

[11] Bartels, op. cit. supra note 6, at 474, states: "Still another criterion of the stature of credit in our economy is the extent and manner in which it has been subjected to social regulation. This is an indication of the esteem in which it is held and of the disrepute which it has attained."

[12] The commercial-banking system creates new checkbook money in the form of demand deposits when it makes loans to borrowers. Its money-creating power arises from the fractional reserve requirements against demand deposits permitted by the Federal Reserve System under authority from Congress. Almost 80% of the U.S. money stock in the hands of the public consists of deposit money. See Whittlesey, Freedman & Herman, Money and Banking 20 (1963).

they lend to sales or consumer finance companies that make loans or buy paper.[13]

In the last analysis, these money-creating powers are delegated by the federal government itself. This provides an additional reason then, for governments at all levels to be sensitive to the need for legal controls over practices associated with lending and borrowing. State regulation of consumer-credit practices generally includes the following provisions: (1) licensing of firms engaged in this activity; (2) detailed requirements pertaining to contract terms and to practical methods of operating by such firms; (3) some stipulations about rates or maximum charges; and (4) supervision, examination, and code enforcement by a state agency, usually the bank commissioner.

A. *The Capital Market*

The consumer-credit market is only a tiny segment of the much larger and economically crucial capital market. On the demand side of the capital market are grouped the entrepreneurs or producers who have plans for expansion of production and need to borrow capital. They expect to sell their goods at a margin great enough to yield a profit over and above the sum necessary to pay the interest cost of the borrowed capital. Many agencies catering to the demands for consumer credit are in fact on both sides of the market. They are on the demand side of the capital market because they anticipate putting borrowed funds to work by lending them to consumers, thereby earning sufficient income to pay the interest cost of the borrowed capital and to create profits for themselves.

On the supply side of the general capital market are all those financial agencies that specialize in attracting and collecting income from "savers." "Savers" are those people willing to forego temporarily the use of newly earned income in return for interest. In addition to this source of supply of capital funds, the commercial-banking system, operating under federal-reserve requirements, can provide a further source of funds that have never been income and are newly created demand-deposit money. Thus, the supply side of the capital market is made up of two rather different segments.

Consumers of goods and services (including the services of money-lenders) appear in the capital market only indirectly through the agencies (*e.g.*, banks and finance agencies), whose credit is much stronger. Consumer-credit demand, therefore, as anticipated by these financial intermediaries, is translated into the demand side of the

[13] Robinson, Money and Capital Markets 261-62 (1964). For a comparison of the roles played by commercial banks and financial intermediaries in this process, see Smith, Financial Intermediaries and Monetary Controls, 73 Q.J. Econ. 535 (1959).

capital market, and the bidding prices create the interest rate when they interact with the supply prices of lenders.[14]

It is entirely possible that defects in the demand side of the consumer-credit market can affect the prices paid in the other parts of the capital market. Imperfections in both the demand side and the supply side of the consumer-credit market itself are of concern not merely to consumers, but to everyone interested in the proper functioning of interest rates in capital markets. If the imperfections of the consumer-credit market are such as to attract into consumer lending (through artificially high rates) an excessive amount of the total supply of loanable funds, this inevitably has a disruptive effect upon the productive side of the economy. Some entrepreneurs would be denied funds completely, while others would be made to pay a higher rate of interest than if consumer-credit rates were lower. Therefore, an understanding of the real demand from the consumer-credit side would contribute to a general improvement in the functioning of the whole economic system.

B. *Demand Side of the Consumer-Credit Market*

On the demand side of the consumer-credit market, the most important question is whether or not borrowers are in a position to understand the charges they are paying for consumer credit, because, without this understanding, a rational decision as to whether or not to borrow cannot be made. In most consumer-credit transactions, terms are stated as "add-on" or discount charges or as monthly dollar payments. Often borrowers, or purchasers, have no idea of the price they are paying for credit, as compared to the knowledge they have of the interest rates they receive on savings deposits or government bonds, for example.

One of the most important legal regulations suggested by consumer associations is the requirement that lenders state charges in terms of simple annual interest rates. The basic notion of a rate is nothing more than a measure of flow—of water, income, or what have you. Every rate is a ratio involving a time period, a base amount, and an increment related to that base over the time period. An annual interest rate is derived from the number of dollars which must be paid to borrow one hundred dollars for a year. It is what the market establishes as the price that borrowers pay for command over present purchasing power and that lenders receive for relinquishing command over

[14] Here again, it is useful to put to rest once and for all the artificial attempt to inject a distinction between "pure" interest rate (the *actual* interest cost) and other service costs or charges associated with the demand for funds. As many others have pointed out, there is practically no interest rate anywhere in the economy that is not a mixture of elements of pure interest, service charges, and risk elements.

present purchasing power for one year.[15] This form of disclosure has been resisted by most lending agencies. In doing so, however, the opponents of annual-rate disclosure completely ignore the fact that consumers are always beset with annual-rate quotations when banks and lending institutions attempt to attract savings and deposits from the public. The necessity for a consumer to compare what he is able to earn when he puts his money in a bank with what it will cost him when he takes money out of a bank—the necessity of having these comparisons available in identical percentage terms—is a chief and most compelling consumer argument for disclosure of annual-rate information.

The opponents of such disclosure generally attempt to draw fine distinctions among the actual cost elements in the charges on loans. For instance, Professor Robert Johnson has said:

> Examination of the operating costs of credit institutions reveals that the dominant component of this "credit package" is the service element, that only a relatively small portion of the finance charge paid by the consumer can be attributed to pure interest.
>
> . . . Because the major component of a consumer finance charge is for service and risk, it is more properly viewed as a service charge.
>
> If it is treated as a service charge, the consumer finance charge need not be converted into an annual rate. Indeed most service charges are presented in much the same manner as finance charges are now stated to the consumer.[16]

Two comments are in order. First, what Johnson says about the components of cost included in the credit package is correct, but it is likewise applicable to any and every interest rate charged either to consumers or to businesses.[17] Second, the fact that service charges have long been presented in a certain way does not at all mean that their conversion into an annual rate could not be done and would not be an improvement. As far as the borrower is concerned, all types of charges are the same: they are part of the total cost of credit to him. What the consumer needs to know is whether 5 per cent interest from a savings bank provides a better use of his funds than paying off what is called a "4 ½ per cent" auto loan. It usually does not, and it is highly un-

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15 The function of interest rates is so critical to the operation of the economy that sophisticated commercial dealers convert practically every financial instrument and financial transaction into percentage terms. This is done to make as fine a profit calculation as possible, to guide the businessman in the selection of the most profitable investment of his assets.

16 Johnson, Methods of Stating Consumer Finance Charges 14 (1961).

17 Messner, Social Ethics, Natural Law in the Western World 814-15 (rev. ed. 1965).

fortunate that communications media are bombarded with such misleading advertisements.[18]

According to the opponents of annual-rate statement, "the most appealing of the arguments for use of the interest-rate form of statement is that it will enable consumers to shop more effectively for credit."[19] They concede that this argument implies also that this more effective shopping for credit will generally reduce its cost. In addition, some of these opponents, notably Professor Johnson, allege the "impossibility" of expressing finance charges as annual rates. There are two main objections proposed by Professor Johnson: (1) "The finance charge can be buried in the prices of items sold on credit"; and (2) "The charge cannot be computed at the time credit is granted on a wide variety of credit transactions."[20]

Let us examine these two arguments and their implications. It is perhaps true that a retailer could raise the price of a product and either totally eliminate any mention of installment financing or quote a ridiculously low rate. The total elimination of explicit finance charges occurs even now in some types of credit-card and department-store credit, for instance, when one gets thirty-day "free" credit. However, the consumer, as long as he has a single price to deal with, is perfectly able to compare the price on the goods or services he is getting with prices for that same benefit in competing stores. This goes on all the time, and the consumer is well accustomed to handling these situations. The popularity of discount stores, which have eliminated such

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[18] The attempt to distinguish lender profit from borrower interest is a determined, if misguided, one. Ray McAllister, speaking of revolving credit and installment credit, noted that

> these . . . seem to be *interest rates*, which in fact they are not since in both types of credit interest "on the use of money" represents only a part of the total credit costs.
>
> It is argued that because regular installment credit charges are *not* usually expressed as a "true" annual rate it is improper to express revolving credit charges as a *true annual rate*. Again, it is pointed out, this would equate the charge for revolving credit in the mind of the buyer with an interest rate, which it is not.

McAllister, An Analysis of Proposed Federal Legislation Covering Consumer Instalment Credit, in Business Studies 31, 38 (No. Tex. State Univ. Fall 1966).

[19] Johnson, op. cit. supra note 16, at 15. Professor Johnson does indeed reach some strange conclusions by his arguments. He decides that consumers will not only be no better off, but will actually be more confused if annual-rate expressions are imposed. It is interesting to examine the reason for his conclusion. He argues that unless each and every type of credit offered to consumers is able to be stated in the annual-rate formula, the consumer will still be confused. To achieve comparability of rate statements for 90% of the types of credit offered to consumers would not, in Johnson's eyes, be an improvement. This argument is totally unacceptable. This is a field in which one is grateful for even a small improvement in the information available to consumers—for even the slightest correction of deceitful and confusing methods of telling the consumer what he is paying.

[20] Id. at 16.

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ancillary services as free delivery or charge accounts, proves that the customer can make the distinction between the goods and services he gets for different product prices in different stores. To think otherwise is seriously to demean the natural intelligence of our countrymen. We must, therefore, totally reject the argument that consumers cannot uncover finance charges buried in the price of items sold on credit.[21]

Let us now turn to Professor Johnson's second objection, namely the fact that on many types of credit the precise rate cannot be calculated in advance, because the conduct of the customer during the life of the loan or the payment period is unknown. By this is meant that no one can precisely foretell, on a revolving-credit plan, how much and on what precise day the customer will buy on this plan and how much he will pay back. Professor Johnson also argues that "on many types of consumer credit it is difficult to identify the finance charge accurately because of various fees or insurance premiums accompanying the payment of the finance charge."[22]

The substance of Professor Johnson's argument completely falls, however, when the proponents of the annual rate minimize the need for an expression of the precise annual interest rate equivalent that a revolving-credit customer actually *has paid*. It is quite satisfactory, for purposes of consumer information, if sellers reveal that, in the initial computation of charges on these revolving plans, they are using a broad formula which is roughly equivalent to a particular annual rate under estimated typical payment conditions. So long as some such formula is worked out by the authorities charged with enforcement, and all sellers are required to use a similar formula and manner of expression, then the information available to the public is actually uniform and sufficient. The public would be forewarned that deviations from the assumed conditions will alter the precise rate paid by each individual. This arrangement is perfectly feasible and will give the customer information of exactly the type he needs. What matters is not whether each consumer gets the mathematically precise rate paid on every single contract. Instead, it is important that he get an honest estimate with a margin of error that is relatively small.[23]

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21 This rejection is based, of course, upon the assumption that the retail market is free from collusive pricing. To further strengthen consumer awareness of the problem, consumer groups have in the past mounted campaigns encouraging customers to demand discounts for cash, on the principle that if "free" services of credit or delivery are furnished to a credit customer for exactly the same product price that a cash customer pays, cash customers are made to subsidize credit customers. Consumer education about this practice could eventually force retailers into the practice of cash discounts.

22 Johnson, op. cit. supra note 16, at 17. This quotation appears to confirm the contention that confusion already exists on a vast scale, and that the only way to avoid multiplication of these deceitful fees and premiums is to force the whole package of fees to be converted into a single percentage rate.

23 There is no need to fear that there will be a weakening of the competitive position

Finally, it should be pointed out that some arguments employed against consumer-credit controls and contract terms miss the point entirely. For instance, it has often been alleged that consumers do not want and will not use information such as annual-rate percentages. It may be freely conceded that there are some pieces of information that the buyer does not now realize are important for him to know. If, however, it is objectively true that a certain piece of information is essential to a rational decision, then it is perfectly reasonable for the law to require it to be given. It then becomes a matter for consumer education to bring the people to the point where they appreciate the necessity of making a decision only after considering this information. It is inconceivable that anyone can sincerely argue that pertinent information should *not* be made available just because present-day consumers either do not know enough to ask for it or do not use it where it is now available. If the consumer-credit industry really thought this information would have no effect, there would never have been any controversy at all.[24]

Fortunately for the consumer, several federal agencies supervising financial institutions have recently stepped into this matter with a simultaneous release to all agencies under their control. In it they set out guidelines to be followed by financial institutions in advertising to attract deposits from the public. Chief among these directives is the following:

> Interest or dividend rates should be stated in terms of annual rates of simple interest, and the advertisement should state whether such earnings are compounded and, if so, the basis of compounding. Neither the total percentage return if held to final maturity nor the average annual rate achieved by compounding should be stated unless the annual rate of simple interest is presented with equal prominence.[25]

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of individual sellers, since all firms will be required to follow the same formula for the specific type of credit.

[24] Some of the arguments or positions advanced by credit-industry spokesmen are obviously well calculated to inject confusion and bewilderment into the debate and should hardly be seriously advanced. For instance, all the talk about how difficult or impossible it would be for companies to train their people to tell customers the true annual interest rate sounds hollow when faced with assurances from the publishers of financial tables that they can add a true annual-rate column to their charts with no difficulty or delay, and at minimal expense. See generally Mors, Consumer Credit Finance Charges 108 (1965).

[25] See Letter From Board of Governors of the Federal Reserve System to State Member Banks, Dec. 16, 1966, in 52 Fed. Reserve Bull. 1774 (1966). The agencies involved were the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Federal Home Loan Bank Board, and the Board of Governors of the Federal Reserve System. See also Business Week, Dec. 24, 1966, p. 81. It is also a source of considerable gratification that the 1967 consumer message from President Johnson contained a request for a percentage rate disclosure per year.

Interestingly enough, this joint action was stimulated by a veiled threat from the Securities and Exchange Commission to apply the anti-fraud provisions of the securities acts to advertising by financial institutions.

C. *Supply Side of the Consumer-Credit Market*

To appraise the adequacy of a legislative program which controls market practices of sellers and lenders, several factors must be considered. An effective program must be of sufficient scope to encompass within its provisions all types of credit transactions and institutions, covering all consumer goods and services. The effective program must provide for the licensing and supervision of lenders, and must include appropriate sanctions for abusive activity. Further, the legislation, if it is going to accomplish its objectives, must indicate what contract provisions are to be required, permitted, or prohibited; it must also specify the requirements for inclusion of provisions covering insurance, extensions, and refinancing, as well as the procedures as to collections, defaults, and repossessions. Lastly, the legislation must establish the rate-determination process.

Many of the above factors exist, in varying degrees, in legislation which often takes the shape of small loan laws. The included types of transactions and institutions, the licensing and related items, and rates are reasonably well covered. In addition, state requirements relative to contract terms generally present no great economic issue beyond the elimination of coercion, fraud, or deceit. Several practices, however, still remain in the category of unfinished consumer-protection business.

Credit-Rating Bureaus. For their own protection, lenders have set up a system of credit-rating bureaus. While this system is now mainly local, it is in the process of being developed into a national network. In an age in which access to credit can be a very important aspect of a consumer's economic welfare, a close examination of the operation of such credit-rating bureaus is necessary, and public control of them may be required. In too many instances, consumers have been forced into paying debts by a form of blackmail which insinuates that the credit-rating-bureau files will forever bar that delinquent customer from access to credit anywhere in the world. In some of these cases, payments were made on demands that never should have been honored. In other cases, reputations of debtors and consumers have been blackened and credit denied on the basis of completely unjustified allegations conveyed to the credit-rating bureau. In a recent newspaper article, Vance Packard wrote:

> An acquaintance discovered quite by accident that his local credit bureau, in a litigation report on him, said he had been the target of three law suits for failure to meet commit-

ments; on the record he obviously was a bad credit risk. In fact, the first case was a $5 scare suit back in the nineteen-thirties over a magazine subscription he had never ordered; the second involved a disagreement over a $200 lawyer's fee and was later compromised amicably; the third concerned a disputed fee he had charged a client, and this suit he won in court. It took my friend two days of digging to clear his record with the credit bureau.[26]

It will be necessary for legal experts to consider ways and means of protecting the public from potential injury caused by such mistaken reports in the files of private credit-rating bureaus.

Relationship of Seller, Lender, and Customer. Another aspect of the supply side of the credit market that calls for regulation and improvement pertains to the relationship between the seller of goods, the customer, and the lender of the money used to purchase the goods. Frequently there is a sharp legal separation between financing agency and retailer. The lending agency buys the customer's promissory note from the retailer and becomes a detached "third party" to the transaction. The customer is then in a borrower-lender relationship with the finance company or bank. The latter is a "holder in due course" of the customer's promise to pay certain sums of money independent of the underlying transaction. This principle is sacrosanct in the law in order to protect the negotiability of commercial paper.

This protected status was abused, however, by some financing institutions who allowed their credit, their forms, and their good names to be used by unscrupulous businessmen in soliciting business. Abuses multiplied, particularly in the home-improvement field. Fly-by-night operators absconded with down-payments and never completed the jobs they had contracted for, while the bank or finance agency had the legal power to compel the customer to keep paying installments on loans used to pay for goods or work he had never received.

Massachusetts has pioneered in the move to eliminate the divorce between the sellers of goods and the grantors of credit. Several years ago the legislature passed and the Governor signed a bill abridging the holder-in-due-course privilege for any financing agent who takes a promissory note originating from the purchase of a consumer good. Such a note must explicitly state that it is a "consumer note."[27] In such cases, the financing agent is also liable for any defenses that the buyer might have against the original seller. The principle on which this law is based is very simple. Were a bank or finance company to know

[26] Packard, Don't Tell It to the Computer, N.Y. Times, Jan. 8, 1967, § 6 (Magazine), p. 44, at 90.

[27] Mass. Gen. Laws Ann. ch. 255, § 12C (Supp. 1966).

that it could be liable to the ultimate customer, it would be very concerned about the reliability and honesty of the businessman or contractor whose installment sales it was financing. This author can testify, from personal experience with businessmen who were affected by this law, that it actually had the intended effect—banks became much more careful about the integrity of the businessmen whose installment paper they purchased.

The interconnected nature of this tripartite transaction is clearer from the way the British system of hire-purchase works.

> Instead of the trader giving credit to the customer he sells the goods to the finance company and thus obtains his price in cash. The finance house then hires the goods to the customer and derives the profits and expenses from the difference between the cash price, less the deposit, paid to the trader and the total of the installments received from the customer.[28]

The English have thus been wrestling with essentially the same problem from a different angle, created by the different historical development taken by English law. As seen above, the dealer is not considered the owner of the goods purchased on installment plans by a customer, because the dealer has executed a contract of sale to a finance company. However, the finance company has not been considered liable for any defects in the goods. These were serious gaps in the protection of English purchasers on the installment plan. Some have suggested a law making the dealer the agent of the finance company, but even this may not be enough.[29]

IV. Rates and Ceilings

The two previous sections have treated the nature of consumer credit and some required conditions that the government must establish as the framework within which the consumer-credit market must function. Essentially these conditions encompass full disclosure of information to buyers, freedom of buyers from fraud, deceit, or coercion, and the prevention of monopolistic or restrictive trade practices by the credit industry. This latter goal, of course, can only be achieved by vigorous enforcement of all the antitrust laws.

It is hard to imagine how the consumer-credit market might have developed in the absence of government regulation. Historical and economic factors made it necessary to have state regulation of the small loan business. Restrictions on charges for extensions of credit

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28 Final Report of the Committee on Consumer Protection, Stat. Instr., 1962, No. 505, at 166.

29 See generally Borrie & Diamond, The Consumer, Society and the Law (1964).

began in ancient times and continued through the Middle Ages.[30] In the United States, there have been many usury laws which set maximum ceilings on interest rates somewhere in the range of 6 to 10 per cent. With such ceilings, however, it was totally impossible to make small loans profitably. Lending to the consumer in small amounts was much costlier and more risky than business lending. Investigation, service, collection and other handling costs, plus the market rate of interest, drove the total cost of a loan to a consumer well above the ceilings set in traditional usury laws. If the state did not wish to leave the whole field of small loans to illegal "loan sharks," with interest-rate charges sometimes as high as 50 or 100 per cent a year, it had to make it possible for legitimate capital and legitimate lenders to function within the law. This conflict between law and economic reality led to the practice of special small loans licensing and to controlled exemption from ordinary maximum rates. As one author on consumer credit has written, "The lending of money to consumers is an economic activity which apparently thrives with or without legal sanction. The only choice is whether such lending is to be done in large part by loan sharks or by legitimate lenders."[31]

Most states now have laws establishing ceilings on the interest rates and finance charges that may be applied to consumer credit. This is particularly true of most categories of what are commonly called "small loans." Presuming, therefore, that the government has done all it can to establish the proper framework conditions for the credit market to operate in the public interest, is this enough, or must the state go further? Should it attempt to fix any rates at all, or should it leave the whole matter to the forces of competition at the market? Assuming it is decided that the state should fix some maximum rates, at what level should these be set? Should they be set deliberately high in order to make it possible for all, even the most inefficient suppliers of credit, to function in the market, or should they be set very low so that only the most efficient suppliers can stay in the market, and if so will this accentuate whatever trend to monopoly already exists? Should ceilings be set close to prevailing market prices, or should they be set rather high in order to prohibit only the most exorbitant charges? The issue raised by this problem—freedom of pricing—is one on which hot debate and lively dissent take place among economists.

On the one hand is a school of thought which believes that, apart

[30] Those governmental and church restrictions on interest stemmed largely from several aspects of the borrower-lender relationship in early times; loans were frequently made to a person in distress, while capital and money were not considered productive goods as they are today. In fact, in some periods a negative interest rate was paid by the owner to someone who guaranteed to keep his principal safe for him.

[31] Edwards, Consumer Credit Institutions Other Than Banks, in American Financial Institutions 716 (1951).

from assuring truthful and accurate information to the customer, the state should keep out of the credit-pricing process and leave it to the forces of the market. Some of their objections to state-set rates are quite persuasive. By what criteria will rates be set? Frequently, they are set on a cost-plus basis, thus encouraging continuing support even to inefficient and costly suppliers of this service. In addition, it is claimed, with a fair amount of evidence, that whatever ceiling is set automatically becomes a floor, if not the actual price, that the majority of lenders charge. Is the credit industry to be treated like a public utility? What theory of a fair price will govern the action of the state in setting rates? Interminable delays and problems are also involved when a legislature or an administrative board attempts to set rates.

On the other side of the argument, those who maintain that the state must set rates point to several considerations: (1) The borrowers in the market for consumer credit are often not in a financial position to shop around among competing sellers; (2) they frequently are not intellectually able to judge or digest the meaning of the information currently furnished them about rates and terms of credit;[32] and, (3) the supply side of the credit market is not sufficiently competitive to trust it to force rates down to a reasonable level.[33]

The evidence on this third point is voluminous but frequently contradictory. One writer, however, has summarized his study of banking concentration by saying:

> Examining bank performance in 36 major metropolitan areas, we found that structural differences among these markets exert an important influence on bank performance. Market concentration, especially, was found to be significantly associated with the pricing, output, and profits of banks—high

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32 Note the significant conclusion on this point from the Juster & Shay study. "Since the majority of consumers probably fall into the rationed category, there will be little rate response observable in the population as a whole under existing conditions . . . . [R]ationed consumers showed virtually no knowledge of rates." Juster & Shay, Consumer Sensitivity to Finance Rates: An Empirical and Analytical Investigation 2-3 (1964). "Rationed consumers are defined as those who, given the finance rate, desire more credit than the major or "primary" credit sources . . . are willing to grant; unrationed consumers are those whose demand for credit is satisfied by their actual borrowing from primary credit sources." Id. at 1. See also the types and levels of ignorance discussed by the Malony Committee Report in the section on hire-purchase and the English consumer. Final Report of the Committee on Consumer Protection, supra note 28, at 168-71.

33 Past efforts of lenders and vendors seem to have been directed to avoiding competition on price alone. Bartels, op. cit. supra note 6, at 36. "Clear distinction has not been made between the total charge and the charge for credit service; therefore the purchaser has not always been critical of price or aware of competitive practices." Id. at 471. To increase competition it is necessary to require suppliers of credit to state their charges in ways that facilitate price comparision. Ibid.

> concentration being associated with high loan rates, low rates on time and savings deposits, and high profits.[34]

Professor Donald Jacobs, too, has reached the conclusion that changes in the regulations governing bank operations and changes in entry restrictions on new banks are necessary if banks are really going to be able to compete with other financial intermediaries.[35]

In a recent credit conference in Canada, Professor Wallace P. Mors stated the case for ceilings as follows:

> There are some grounds . . . for believing that interest or finance rate ceilings might be necessary even with rate and dollar disclosure. Like most markets, the consumer credit market is imperfectly competitive. Imperfections are many and include differentiation of loan services among financing agencies, limitation of buyer-seller contracts, and borrower inability to determine price. Rate and dollar disclosure of finance charges would reduce only one of the many factors which contribute to market imperfections.[36]

Professor Neufeld, upon whose paper Professor Mors was commenting, had suggested the desirability of making entry into the credit industry easier, and of thus avoiding monopoly profits by encouraging competition. Mors answered this by saying:

> Proliferation of installment lenders might increase competition and reduce monopoly profits without reducing prices to consumers. Judging from small-loan experience, the greater the number of loan offices, the smaller is the size of the average office and the greater is the cost of operations. Any intensification of competition takes the form of increased advertising and other forms of sales promotion, rates of charge remaining at the ceiling level allowed by law.[37]

Several conclusions should be drawn from this discussion. First, the essence of a credit transaction—delay of payment by the buyer—should be acknowledged and laws revised to agree with economic reality. Second, the imperfectly competitive nature of the market should be faced. On the buyer's side of the market there are imperfections because of the lack of knowledge of alternatives in rates,

[34] Edwards, The Banking Competition Controversy, in Studies in Banking Competition and The Banking Structure 327 (1966).

[35] Jacobs, The Framework of Commercial Bank Regulation: An Appraisal, in id. at 350.

[36] Mors, The Economic Significance of Consumer Credit: Commentary, in Consumer Credit in Canada 21-22 (Ziegel & Olley ed. 1966).

[37] Id. at 22.

terms, and sources, and differences in creditworthiness between buyers. On the seller's side there is a naturally differentiated product because of the nature or availability of the goods offered, and an artificially differentiated product created by brand-name advertising; no two sellers are really selling identical, homogeneous commodities or services. Other elements of differentiation between one lender and another may be: collection methods and policies, ease of obtaining loans, down-payment and/or security needed. Third, state governments should still do all in their power to introduce more competitive features into the market. On the demand side this means (a) encouraging full disclosure of all pertinent facts, rates, and terms to enable comparisons, and (b) consumer education to make consumers aware of their choices and their rights. On the supply side, the state should encourage (a) entry of new credit grantors, and (b) expansion of the types and fields into which old and new lenders may enter.

Even after all these improvements in market conditions and practices have been achieved with the aid of state law, there remains the nagging question: Will banks and finance agencies engage in sufficient price competition to keep interest and finance rates at levels reasonably fair to the consumer? The answer to that question is probably "no." Even with vigorous regulation by banking authorities and diligent application of antitrust law to bank structure and conduct, it seems likely that state control of interest rates on consumer credit will still be necessary in the public interest. If so, the proper course of action should be to set rates and not ceilings.

V. Conclusion

In the larger context, it is clear that glaring abuses in the consumer-credit field have led to popular demands for state regulation. This raises an economic issue that far transcends the credit field: How do we reconcile and relate the interests of business and the public within the broad context of a free capitalistic economy? It is commonly accepted that the general public makes very little distinction between abuses associated with the financing of a sale and problems caused by the seller or his product. In the eyes of a buyer, it is all one. He usually attributes all problems directly and immediately to the original seller and focuses his complaints accordingly. How much popular conflict and disenchantment with business is really due to finance industry abuses is anyone's guess, but in no event is it small. Otherwise, consumer associations and consumer groups throughout the fifty states would hardly have made consumer-credit abuses the focal point of their attack.

Popular disenchantment with business is emphasized by those economists and social psychologists who are devoting their attention

to the study of conflict in society and the requirements of social harmony. One European author recently wrote:

> [I]n the majority of cases hire purchase could better have been avoided. . . . *First save, then spend, is as a rule better than the other way around.* This is quite clear in the cases in which the original harmony between seller and buyer changes into an open conflict: the buyer has become overburdened by debts which exceed his means . . . .
>
> . . . [Most consumers] believe that they are often overcharged. This brings us to the clash of interests which, next to that on wages, is perhaps the strongest in contemporary folklore: the businessman is frequently regarded as the consumers' natural enemy, if not as a *swindler*.[38]

This is a very disturbing state of affairs, mainly because it is so unnecessary. If the businessman ceased looking on consumer credit as an additional source of profit for him, and concentrated his attention on making a profit from his real business—selling good quality products to satisfied customers—this suspicion and hostility toward businessmen in general might diminish or even disappear. It was a sorry commentary on business when a consumer magazine could headline its credit article "Bait the Hook with Merchandise."[39] Hopefully, businessmen will see that it is in their own interest to work for an equitable system of regulation of the consumer-credit field.[40] This will then restore credit to what it was intended to be—a valuable and convenient tool to facilitate the production and exchange of goods and services to the mutual benefit of business and the consumer.

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[38] Pen, Harmony & Conflict in Modern Society 135-36 (1966).

[39] 31 Consumer Reports 457-61 (1966).

[40] Some actual business "deeds" along this line would be much more effective than the pious declarations adopted by The Better Business Bureau Managers and widely published in November 1966. The following is an example of such language:

> The Better Business Bureaus decry and regret actions or publicity by whomsoever, which create the false impression that American Business generally is opposed to consumer interests—or which unfairly disparage or degrade the general dependability and integrity of American Business.
>
> . . . .
>
> [They] . . . deplore any attempts to set up business and their customers as antagonists when, in fact, they are dependent on each other for the mutual benefit of both.

The Bulletin, Better Business Bureau, Nov. 1966, p. 1.

(Mr. Clive W. Bare, referee in bankruptcy for the Eastern District of Tennessee, submitted the following material pertaining to bankruptcy proceedings in the State of Tennessee:)

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF TENNESSEE, NORTHERN DIVISION

IN THE MATTER OF WILLIAM SYLVESTER BRANCH, DEBTOR

In Proceedings Under Chapter XIII, No. 23,372

MEMORANDUM OPINION

Section 656(b) of Chapter XIII of the Bankruptcy Act (wage earner plans) provides that before confirming any plan the court shall require proof from each creditor filing a claim that such claim is free from usury. General Order 55(4) which applies to proceedings under Chapter XIII provides that each proof of claim based upon the loan of money shall contain proof that the claim is free from usury as defined by the laws of the place where the debt was contracted.

William Sylvester Branch, the above debtor, filed an original petition under Chapter XIII on February 21, 1966. The debtor is 46 years old, married, and employed as a porter at the East Tennessee Tuberculosis Hospital, earning $200.00 per month. With his petition, he submitted his wage earner plan providing for payment out of his future earnings and wages the sum of $20.00 each week. The plan further provided that Merit Finance Company (Merit), a secured creditor, receive fixed monthly payments of $60.00. Merit, on March 9, 1966, filed its proof of claim in the amount of $2,870.00, accepting the debtor's plan.

Merit is an industrial loan and thrift company operating under the provisions of Tennessee Code Annotated. Secs. 45–2001–45–2017. Merit asserts that it holds a note secured by a second mortgage on the debtor's home, and a security interest in the debtor's household goods and an automobile, all executed November 19, 1965, at Knoxville, Tennessee. Merit's claim is based upon the following transactions.

(1) On December 22, 1964, the debtor negotiated a loan with Merit. He executed a note in the sum of $72.00 payable in 12 monthly installments of $6.00 each. Merit's ledger card (Account No. 63–235) indicates the $72.00 note was made up of the following items and charges:

Cash received by debtor	$59.04
Interest	4.32
Investigation charge	2.88
Life insurance premium	1.44
Accident and health premium	4.32
Total of note	72.00

(2) On January 23, 1965, the first loan was renewed or "flipped." [1] The debtor executed a new note in the amount of $378.00 payable in 18 monthly payments of $21.00 each. Merit's ledger card (Account No. 63–337) indicates the following items and charges:

Payment to Merit on unpaid balance old loan (credit given for insurance premium rebate, $4.94)	$68.06
Paid Franklin Finance Company for borrower	108.00
Cash to borrower	95.11
Property insurance	15.00
Interest	34.02
Investigation charge	15.12
Life insurance premium	11.34
Accident and health premium	28.35
Recording fee (security agreement, household furniture)	3.00
Total of note	378.00

[1] "Industrial loan and thrift companies . . . freely engage in the practice of 'flipping,' whereby a borrower who has repaid a portion of a loan is allowed to make or is enticed to make another loan whereupon the new loan is set up combining the new amount with the old balance on which all allowable charges have already been made, and the full amount of allowable charges is gain imposed on the new balance." *Final Report of the Legislative Council of the 80th General Assembly, State of Tennessee* (1968).

Repayments by debtor: $21.00—February 22, 1965; $84.00—March 6, 1965.

(3) On March 6, 1965, the second loan was renewed or "flipped." Merit's ledger card (Account No. 63–483) indicates a new note in the amount of $552.00 was executed, payable in 24 monthly installments of $23.00 each. The ledger card indicates the following items and charges:

Payment to Merit on unpaid balance old loan (rebate insurance premium, $45.58)	$227.42
Cash to borrower	149.70
Interest	66.24
Investigation charge	22.08
Life insurance premium	22.08
Accident and health premium	41.40
Property insurance premium	22.08
Recording fee	1.00
Total of note	552.00

Repayment by debtor: $21.85—April 24, 1965 (late fee charged $1.15); $23.00—July 1, 1965.

(4) On August 10, 1965, the third loan was renewed or "flipped" and a new note executed in the amount of $672.00, repayable in 24 monthly installments of $28.00 each. Merit's ledger card (Account No. 63–1074) indicates the following items and charges:

Payment to Merit on unpaid balance old loan (rebate insurance premium, $56.72)	$450.43
Cash to debtor	9.89
Interest	80.64
Investigation fee	26.88
Life insurance premium	26.88
Accident and health premium	50.40
Property insurance premium	26.88
Total of note	672.00

Repayments on the above loan appears as follows: $28.00—September 9, 1965; $28.00—October 9, 1965.

(5) On November 19, 1965, the fourth loan was renewed or "flipped" and this time a note executed in the sum of $2952.00, payable in 36 monthly payments of $82.00 each. Merit's ledger (Account No. 63–1396) indicates the following items and charges:

Payment to Merit on unpaid balance old loan (rebate insurance premium, $79.90)	$536.10
Paid City Finance Company	1,044.00
Paid Consolidated Credit Company	72.00
Cash received by debtor	10.28
Interest	531.36
Investigation charge	118.08
Life insurance premium	177.12
Accident and health premium	280.44
Property insurance premium	177.12
Recording fee	5.50
Total of note	2,952.00

Repayment by debtor on this loan: $82.00—_____, 1966.

A resume of the debtor's five loans with Merit, from December 22, 1964 to November 19, 1965, indicates the following:

Received by debtor or paid to others for his benefit	$1,548.02
Interest charges	716.58
Investigation charges	185.04
Insurance premiums (net after rebate)	678.41
Recording charges	9.50

Repayments by the debtor total $287.85. As indicated heretofore Merit says the debtor owes it $2870.00 at this time.

The question before the court is whether Merit's claim is free from usury. In Chapter XIII proceedings, where a loan of money is involved, General Order

55(4) places the burden of proof upon the claimant to show that its claim is free from usury. In my opinion Merit's claim is not free from usury and such usurious charges must be disallowed.

To creditors and leaders in the business community who are constantly asking why there is such a large number of bankruptcy petitions filed in Tennessee each year,[2] an analysis of the financing charges in the loans under consideration in this opinion furnishes one of the principal answers.

USURY

In the United States the meaning of usury is the taking or reserving of illegal interest. The test of usury in a contract is whether it would, if performed, result in securing a greater rate of profit than is allowed by law. The form of the agreement is immaterial, since any shift or device by which illegal interest is arranged to be received or paid is usurious.

"A profit made or loss imposed on the necessities of the borrower, whatever form, shape or disguise it may assume where the treaty is for a loan and the capital is to be returned at all events, has always been adjudged to be so much profit taken upon a loan, and to be a violation of these laws which limit the lender to a specified rate of interest." *Bank of United States* v. *Owens*, 27 U.S. 527.

Lenders often seek to augment the interest which they charge for a loan by requiring borrowers to pay for pretended services rendered or for fictitious expenses incurred by the lender.

"The cupidity of lenders and the willingness of borrowers to concede whatever may be demanded or to promise whatever may be exacted in order to obtain temporary relief from financial embarrassment have resulted in a great variety of devices to evade the usury laws. To frustrate such evasions the courts look beyond the form of transactions to their substance. The general rule is that a court in determining whether or not a contract or transaction is usurious will disregard its form and look to the substance, condemning it when it finds the requisites of usury present, regardless of the disguises they may wear. No case is to be judged by what the parties appear to be or represent themselves to be doing, but by the transaction as disclosed by the whole evidence, and if from that it is in substance a receiving or contracting for the receiving of usurious interest for a loan or forbearance of money, the parties are subject to the statutory consequences, no matter what device they may have employed to conceal the true character of their dealings." 55 Am. Jur., Usury, at p. 332.

It is often contended that the parole evidence rule bars evidence of intent, but the rule is otherwise. Parole evidence always is admissible to show that the party intended an illegal contract even though the evidence contradicts the recitals or varies the promises of written instruments.

Such an exception to the parole evidence rule is obviously sound, for to bar oral evidence of intent would make it possible for anyone to avoid the penalties of the law by the simple expedient of casting an unlawful transaction in the form of a written contract having the appearance of legality on its face, in which form it would be unassailable.

By their nature, devices to conceal usury have the appearance of legality: the disguised transaction is usurious for the very reason that the true intent of the parties to the transaction differs from the apparent or professed intent. It is, therfore, necessary to discover every fact that shows the true character of the transaction and to apply the fundamental principles of interest and usury, regardless of the disarming form in which the transaction may have been cast.

INTEREST

Interest is the compensation which may be demanded by the lender from the borrower, or the creditor from the debtor, for the use of money. Tennessee Code Annotated 47–14–103. The legal rate of interest in this state is fixed by Tennessee Code Annotated 47–14–104 at the rate of six dollars ($6.00) for the use of one hundred dollars ($100) for one (1) year. ". . . and every excess over that rate is usury."

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[2] 9,281 petitions filed in Tennessee during the fiscal year ending June 30, 1965. This number was exceeded only in three states—Alabama, California, and Ohio. *Report of the Administrative Office of the U.S. Courts.*

Tennessee Code Annotated 45–2007(f) authorizes industrial loan and thrift companies ". . . to deduct interest in advance on the face amount of the loan for the full term thereof."

Merit's records filed in this proceeding indicate the following charges for interest:

Loan No.	Amount of note	Term of loan (months)	Interest
63–235	$72	12	$4.32
63–337	378	18	34.02
63–483	552	24	66.24
63–1074	672	24	80.64
63–1396	2,952	36	531.36
Total interest charges			716.58

As pointed out heretofore the first loan was "flipped" four times within a period of eleven months; total benefits received by the debtor amounted to some $1548.02; interest totaling $716.58 was charged.[3] In no instance was interest rebated when the loan was "flipped."

It will also be observed from the notes filed in this proceeding that in every instance interest has been charged on interest, e.g., consider the fifth loan made by the debtor. The debtor executed a note in the amount of $2952.00 which includes interest amounting to $531.36. The interest figure was arrived at by charging interest on the face amount of the note, to which the interest had already been added, thus interest is charged on interest.

Did the "flipping" of the loans by Merit in the transactions under consideration enable it to obtain an excess over the legal rate of interest? T.C.A. 47–14–103, 104.

When the first loan was made, the debtor executed a note in the amount of $72.00. This amount includes $4.32 interest for twelve months. One month later the loan was "flipped." The face amount of the new note includes $68.06 payment to Merit on the first loan (rebate given for insurance premiums). Although the debtor had already been charged with interest on $72.00 for twelve months, the $68.06 balance is added into the face amount of the second note ($378.00) and interest is again charged—this time for eighteen months. In the third loan interest is again charged on $227.42 remaining unpaid on the second loan, again for eighteen months. In the fourth loan interest is again charged on $450.43 balance on the third loan, this time for a thirty-six month period. In the fifth loan interest is again charged on $536.10 balance on the fourth loan, again for a thirty-six month period. These transactions indicate interest on interest on interest on interest on interest. Yet the statute says the legal rate of interest in this State is $6.00 for the use of $100.00 for one year "and every excess over that rate is usury." T.C.A. 47–14–103, 104.

When the first loan was made the debtor was entitled to the use of $72.00 for one year. He was charged $4.32 interest. When the loan was "flipped" at the end of one month, however, he was again charged interest on $68.06 of the original $72.00. Six per cent interest on $72.00 for one month (deducted in advance) is $0.36.[4] Yet the debtor was given no rebate for interest when the loan was "flipped."

A period of one and one-half months intervened between the "flipping" of the second and third loans. The second note is for $378.00, interest charged is $34.02 for an eighteen-month period. Interest on $378.00 for one and one-half months is $2.84. Again the debtor was given no rebate when the loan was "flipped."

The third note is for $552.00, interest charged is $66.24. A period of approximately five months intervened between the third and fourth loan. Interest on $552.00 for five months is $13.80. Again the debtor was given no rebate for interest when the loan was flipped.

The fourth note is for $672.00, interest charged is $80.64. A period of approximately three and one-half months intervened between the fourth and fifth loans.

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[3] The belief held by many that loan companies in Tennessee charge only six percent interest is a mistaken one. What is overlooked is that they are permitted to deduct interest in advance on the face amount of the loan for the full term thereof.

[4] As heretofore pointed out, T.C.A. 45–2007(f) authorizes industrial loan and thrift companies to deduct interest in advance on the face amount of the loan for the full term thereof. T.C.A. 45–2007(f).

Interest on $672.00 for three and one-half months is $11.76. Again the debtor was given no rebate when the loan was "flipped."

The fifth note is for $2952.00, interest charged is $531.36. Although the fourth loan had some 21 months yet to run and interest had been charged for that period, the debtor was given no rebate for interest.

Had new loans been made instead of "flipping" the prior loans Merit could not have charged interest on the old loan, e.g., the second loan would have been for $203.11 plus legal charges, which total considerably less than the $378.00 note executed by the debtor. The same is true of the other loans. When the third loan was "flipped" the debtor received only $9.89; the face amount of the note was increased however from $552.00 to $672.00 even though the debtor had repaid $44.85 on the third loan. The reason for "flipping" the loans is obvious.

It is my conclusion that Merit "flipped" the loans so that it could again collect interest (and investigation charges) on the old balances even though interest (and investigation charges) had already been imposed. Does such practice constitute usury under the Tennessee statute and decisions?

If the transaction is intended as a device to evade the statute, it constitutes usury. *Nashville Bank v. Hays*, 9 Tenn. 243; *Lawrence v. Morrison*, 9 Tenn. 444; *Weatherhead v. Boyers*, 15 Tenn. 545; *Turney v. State Bank*, 24 Tenn. 407; *Doak v. Snapp*, 41 Tenn. 180.

When the facts are made to appear, no scheme or device to avoid application of usury statutes, regardless of how ingenious or intricate scheme or device may be, will permit anyone guilty of participating in a usurious transaction to escape its consequences, and consent or cooperation of one paying the usurious interest is immaterial. *Providence A.M.E. Church v. Sauer*, 45 Tenn. App. 287.

In determining whether or not a given transaction is usurious, the court will disregard form and look to substance.

". . . it is not to be tolerated for men to do indirectly what they are forbidden to do directly, the courts of justice have always stripped the transaction of its guise, and pronounced upon it according as the intention may be spelled out." *Weatherford v. Boyers*, 15 Tenn. 545, 563.

Any method through which usurious rate may be obtained is violation of law. *Dowler v. Georgia Enterprises*, 162 Tenn. 59.

In *Cobb v. Puckett*, ——— Tenn. App. ———, Judge Parrott labeled the practice by loan companies of charging investigation fees where no investigations are made and charging for insurance premiums without the knowledge of the borrower as "one step removed from pickpocketing and larcency."

An intention to violate the law, as a necessary element of usury, may be implied if other elements are present. *Jenkins v. Dugger*, 96 F. 2d 727.

It is my conclusion that the "flipping" of loans in the transactions under consideration was a plan or scheme to enable Merit to obtain an excess over the legal rate of interest. The consent or cooperation of the debtor is immaterial. The transaction is a continued one; although new advances were made and new instruments were executed, each note refers to the previous one.

INVESTIGATION CHARGES

Tennessee Code Annotated 45–2007(i) authorizes industrial loan and thrift companies—

"To charge for services rendered and expenses incurred in connection with investigating the moral and financial standing of the applicant, security for the loan, investigation of titles and other expenses incurred in connection with the closing of any loan an amount not to exceed four dollars ($4.00) per each one hundred dollars ($100) of the principal amount loaned, and a proportionate amount for any greater or lesser amount loaned, provided no charge shall be collected unless a loan shall have been made."

Merit's records filed in this proceeding indicate the following charges for investigation:

Loan No.	Amount of note	Investigation charge
63–235	$72	$2.88
63–337	378	15.12
63–483	552	22.08
63–1074	672	26.88
63–1396	2,952	118.08

It will be noted that Merit in each instance deducted a flat 4% investigation charge. Is Merit entitled to these charges?

In *Cobb* v. *Puckett* supra, the loan company deducted a 4% investigation charge for 19 loans within a period of some four years. The loan company manager testified he could not say what expenses, if any, had been incurred in checking the credit of the complainant. The court allowed the first investigation charge of $1.92 but disallowed all others.

At the hearing on Merit's claim in this proceeding the loan company introduced no proof in support of its charges for investigation. Under the statute it would be entitled to reimbursement for actual expenses incurred in connection with its investigation, assuming, of course, that some expense was incurred. In my opinion the statute does not authorize a flat 4% fee to be deducted from every loan made, regardless of whether any investigation expense is incurred. The purpose of the statute is to reimburse the lender for actual expenses incurred, not to authorize collection of addition interest.

It will also be noted from an examination of Merit's note that the 4% investigation fee has been been charged on the face amount of the note which includes the amount of the loan, insurance premiums, interest and the investigation fee itself. The statute authorizes a charge "not to exceed four dollars ($4.00) per each one hundred dollars ($100) of the *principal amount loaned.*" (Underscoring added.) This raises the question of whether Merit's instrument is usurious on its face and therefore unenforceable. *White* v. *Kaminsky*, 196 Tenn. 180, 185.[5] It does not appear necessary at this time to determine this question, however. Merit's claim will be allowed in an amount equitable to the parties involved.

Although Merit failed to show that it incurred any expense in investigating the debtor's moral and financial standing, security for the loan, etc., when given a opportunity to do so, its first investigation charge will be allowed in accordance with *Cobb* v. *Puckett*, supra. All other investigation charges will be disallowed.

It must be remembered that the burden of proof is upon Merit to show to the satisfaction of the court that its claim is free from usury and all unauthorized charges. General Order 55(4). Merit failed to carry this burden of proof and in fact introduced no proof whatsoever in support of any investigation charge.

INSURANCE PREMIUMS

Tennessee Code Annotated 45–2007(k) authorizes industrial loan and thrift companies to require at the expense of the borrower, insurance against the hazards to which the collateral used to secure the loan is subject, *and upon failure of the borrower to supply such insurance*, to procure the same. It further authorizes them to accept, *but not require*, as collateral, insurance against the hazards of death or disability of a borrower.

Merit's records indicate the following charges for insurance premiums:

Loan No.	Premiums charged	Rebates when loan "flipped"	Net premiums[1] charged
63-235	$5.76	$4.94	$0.82
63-337	54.69	45.58	9.11
63-483	85.56	56.72	28.84
63-1074	104.16	79.90	24.26
63-1396	634.68	----------	634.68

[1] This does not include interest and investigation fee charged on insurance premiums. No part of such charges was rebated when the loans were flipped.

Mr. John N. Culvahouse issued the life and accident and health and property insurance policies as agent for American Bankers Insurance Company of Florida. Mr. Culvahouse is manager of Merit Finance Company. Apparently the debtor was given one or more certificates along with various other documents when the loans were negotiated. The certificates refer to a "master policy" but the debtor

[5] When the provisions of the note and trust deed are construed as a single instrument ($531.36 interest added into the face amount of the note, 6% additional interest provided for in the deed of trust) the transaction is not only usurious but the usury appears on the face of the instrument. See *Braniff Invest. Co.* v. *Robertson*, 124 Texas 524, 81 SW (2d) 45.

was not given a copy of the master policy nor was one filed with the court. When questioned by the court concerning the insurance, the debtor testified:

"To tell you the truth I didn't know anything about it."

The debtor signed a so-called "Insurance Authorization" in which he purportedly made application to the insurance company, declaring that "the purchase (of insurance) is entirely voluntary and has not been made compulsory by the creditor." It is my conclusion however that the debtor signed the insurance applications without knowledge of their contents, just as he signed all documents placed in front of him. His testimony that the signing "was right fast and right quick" aptly describes the transactions in which the debtor signed financing statements, security agreements, deed of trusts, insurance applications, and possibly other forms, many in triplicate.

This conclusion is fully supported by an examination of one of the documents signed by the debtor. I refer to the so-called deed of trust on his home. This incredible instrument (Ex. 1) provides that a vendor (not otherwise identified in the instrument) for the consideration of $200.00 contracts and agrees to sell to a purchaser (also not identified) certain real estate which in fact is the debtor's home. This instrument further recites a sale price of $7750.00 payable in monthly installments of $90.22 each. Mr. Culvahouse testified that certain language was copied inadvertently from another instrument when this so-called trust deed was prepared. This instrument as well as all other instruments was prepared in the loan company office. The trust deed further provides that the debtor is indebted to Merit in the sum of $2952.00 payable in 36 monthly installments of $82.00 each, "*with interest thereon from date at 6 per cent per annum.*" As heretofore stated, interest amounting to $531.36 had already been added into the $2952.00 note. Again, Mr. Culvahouse testified that the inclusion of interest in the trust deed was a mistake. Yet this is one of the instruments the loan company would have the court believe was signed by the debtor with full knowledge of its contents. These may have been mistakes but clearly it shows that the debtor was signing all instruments placed in front of him by the loan company officials, including an instrument with provisions that even the loan company officials now say are erroneous, without having the slightest knowledge of what he was signing.

Merit's officials testified that the loan in this instance was handled exactly in the same manner as all other loans. I am sure this is true. A review of some nine claims filed by Merit in Chapter XIII proceedings now pending in this court indicates that in every instance life and accident and health insurance premiums have been included, as well as a flat 4 per cent investigation charge, plus interest thereon.

In my opinion, the "tie-in" sale of credit insurance in connection with small loan transactions is being used to evade the statutory limitations on the costs of the loan.[6] The practice followed by Merit is the same practice followed by most, if not all, loan companies in this area. In most instances, if not all, the lenders are profiting by the transactions in that there are "adjustments" between the lender and the insurance company of the premiums charged, if not an actual retention by the company of a part of the premium.

In the case before the court, Mr. Culvahouse, manager of Merit, testified that at the end of the year "so much per cent" of the insurance premiums was returned to Merit's home office by the insurance company. Thus it is clear that Merit is profiting from the insurance transactions.

It is my conclusion that all insurance charges must be stricken from Merit's claim, as well as all interest and investigation fees charged thereon. The life and accident and health insurance policies were issued by Merit without the debtor's consent. This is in violation of the Tennessee statute. T.C.A. 47–2007(k). There is no proof in this record that the debtor was given an opportunity to obtain property insurance which a loan company can require, providing the coverage bears a reasonable relation to the existing hazard or risk of loss. Instead Merit's manager, as agent for the insurance company, issued all policies in question.

In *Hagler* v. *American Road Insurance Company and Ford Motor Credit Company*, ——— Tenn. App. ———, the same individual represented both the credit company and the insurance company. In that case Chancellor Phillips (Sullivan County Chancery Court at Bristol) found that the plaintiff had been required to pay $367.00 for an automobile insurance policy "but in addition thereto was

[6] For an excellent discussion and history of tie-in sales of credit insurance in connection with small loan transactions, see *In the Matter of Richards,* Bk. No. 63–1324, Dist. of Maine, opinion of Referee Poulos.

gouged for another $43.50 for a life insurance policy which he did not have any knowledge of or know anything about." The Chancellor found that the credit company official played a dual role of conflicting interest when he represented with one hand the credit company and with the other the insurance company. The Chancellor's findings leave no doubt as to his conclusion in the matter:

"The Court has tried many cases that would shock the conscience of the Court. This Court is brought to realize that a situation exists where an overreaching, usurious, unlawful, scheme and plan and design by a right hand and a left hand working in collusion and scheming for the purpose of defrauding and deceiving and taking money away from unsuspecting persons in an unlawful, inequitable and unconscionable manner, so as to be a public outrage ot decent principles of banking and financing in the business world.

'The Court, therefore, brands the entire transaction one that smells with fraud, deceit, overreaching, deception and unlawful financing. *The very fact that the same man undertakes to represent two masters constitutes a badge of fraud on its face.*" [Italic added.]

Upon appeal, the Court of Appeals affirmed. Judge Parrott, expressing the unanimous opinion of the Court, quoted the findings of the Chancellor in this regard and stated that he could see how his conscience was shocked. Judge Parrott pointed out that the finance charges and insurance policies were arranged for by the same person who turned out to be the manager of the finance company as well as the agent for the insurance company.

"In our opinion, to permit such a dual agency on the part of these defendants creates a bad situation. If such is not a violation of the law it is a practice which could only lead to trouble and misunderstanding and presents a breeding ground for fraud."

Thus in Tennessee a court of equity has held that when the same man undertakes to represent two masters, a loan company on one hand and an insurance company on the other, the transaction is fraudulent on its face.

In *Cobb* v. *Puckett*, supra, the complainant sued the defendants to recover alleged usury paid to them under a series of notes. Defendants were operating under the Industrial Loan and Thrift Act and had collected some $176.30 insurance premiums when a loan in the original amount of $48.00 had been "flipped" some eighteen times. Chancellor Brock (Chancery Court of Hamilton County) found that the premiums charged for life insurance and accident and health insurance constituted usury since the defendant required complainant to purchase such insurance, contrary to T.C.A., Sec. 45–2007(k). The Chancellor pointed out that while the law permits such insurance to be purchased at the *request* of the borrower, it expressly prohibits the lender from requiring such insurance. Chancellor Brock found that Cobb did not request such insurance and held that the insurance premiums deducted constituted usury. Chancellor Brock not only entered a judgment in favor of complainant for the usurious insurance premiums deducted but awarded him punitive damages in the sum of $500.00.

Upon appeal the Court of Appeals affirmed, stating:

"We are in accord with the Chancellor that the repeated charges of an investigation fee and the charges for the insurance premiums which the plaintiff had not requested were designed to conceal and secure excessive charges for the use of the money."

The court quoted the Supreme Court of Tennessee, *Mallory* v. *Columbia Mortgage and Trust Company*, 150 Tenn. 219, as follows:

"In determining whether or not a given transaction is tainted with usury it is generally held that the court will disregard the form and look to the substance. *Good faith is the decisive factor when compensation is exacted and received by an intermediary (lender) in addition to the legal rate.*"

Although all insurance charges deducted by Merit will be stricken, the debtor will be required to furnish Merit, within ten days, insurance against the hazards to which its collateral is subject. This coverage will be obtained from an insurance carrier of the debtor's own choosing.

JURISDICTION OF BANKRUPTCY COURT

Courts of bankruptcy are essentially courts of equity and their proceedings inherently proceedings in equity. *Local Loan Co.* v. *Hunt* 292 U.S. 234. In the exercise of equitable jurisdiction the bankruptcy court has the power to sift the circumstances surrounding any claim to see that injustice or unfairness is not

done in the administration of the bankrupt estate. *Pepper* v. *Litton*, 308 U.S. 295. As pointed out by Mr. Justice Douglas in that case—

"Courts of bankruptcy are constituted by sections 1 and 2 of the Bankruptcy Act (30 Stat. 544) and by the latter section are invested "with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in bankruptcy proceedings." Consequently this Court has held that for many purposes "courts of bankruptcy are essentially courts of equity, and their proceedings inherently proceedings in equity." *Local Loan Co.* v. *Hunt*, 292 U.S. 234, 240. By virtue of section 2 a bankruptcy court is a court of equity at least in the sense that in the exercise of the jurisdiction conferred upon it by the Act, it applies the principles and rules of equity jurisprudence. *Larson* v. *First State Bank*, 21 F. 2d 936, 938. Among the granted powers are the allowance and disallowance of claims; the collection and distribution of the estates of bankrupts and the determination of controversies in relation thereto; the rejection in whole or in part "according to the equities of the case" of claims previously allowed; and the entering of such judgments "as may be necessary for the enforcement of the provisions" of the Act. In such respects the jurisdiction of the bankruptcy court is exclusive of all other courts. *United States Fidelity & Guaranty Co.* v. *Bray*, 225 U.S. 205, 217.

"The bankruptcy courts have exercised these equitable powers in passing on a wide range of problems arising out of the administration of bankrupt estates. They have been invoked to the end that fraud will not prevail, that substance will not give way to form, that technical considerations will not prevent substantial justice from being done. By reason of the express provisions of section 2 these equitable powers are to be exercised on the allowance of claims, a conclusion which is fortified by section 57 (k)."

General Order 55(4) requiring claimants when the claim is based upon the loan of money to establish that the claim is free from usury has already been referred to. Also, Sec. 656(b) of Chapter XIII (11 USC 1056(b)) places the unmistakable duty upon the court to require proof from each creditor filing a claim that such claim is free from usury.

The purpose of Chapter XIII proceedings is to aid those wage earners of limited means who wish to avoid straight bankruptcy and who desire to liquidate their debts out of future earnings through the medium of Federal Courts. If rehabilitation of the wage earner under Chapter XIII is to be effective, he must be relieved of obligations which he has been induced to undertake through fraud or other unlawful means, or which by their terms are illegal. To aid in attaining this objective, Congress has provided that every creditor asserting a claim against a wage earner must prove that his claim is not usurious. Sec. 656(b); General Order 55(4).

CONCLUSIONS

(1) *Burden of Proof.* In a Chapter XIII proceeding, when a claim is based upon the loan of money, the creditor must show to the satisfaction of the court that the claim is free from usury and all illegal charges. Sec. 656(b) Bankruptcy Act (11 U.S.C. 1056(b)); General Order 55(4).

(2) *Interest—"Flipping of Loans."* Merit "flipped" the loans under consideration for the purpose of obtaining an excess over the legal rate of interest. T.C.A. 47–14–104. *Providence A.M.E. Church* v. *Sauer*, supra; *Weatherhead* v. *Boyers*, supra.

(3) *Insurance Premiums.*

(a) The debtor did not request life or accident or health insurance. The issuance of such policies by Merit is contrary to the provisions of the statute. T.C.A. 45–2007(k); *Cobb* v. *Puckett*, supra.

(b) All insurance policies (life and accident and health and property) were issued by Merit's manager acting in a dual role of a conflicting interest. *Hagler* v. *American Road Insurance Company and Ford Motor Credit Co.*, supra.

(c) The debtor was not given an opportunity to supply Merit with property insurance. Merit can require insurance against the hazards to which its collateral is subject only upon failure of the borrower to supply such insurance. T.C.A. 45–2007(k). The debtor will be given an opportunity to supply such insurance from an insurance carrier of his own selection.

(4) *Investigation Charges.* Merit submitted no proof that it incurred any expense in investigating the moral and financial standing of the applicant, security

for the loan, etc. T.C.A. 45–2007(i). These charges, other than the charge for the first loan, must be disallowed. *Cobb* v. *Puckett*, supra.

(5) Merit's claim will be allowed as follows:

Loan No.	Principal allowed	Investigation fee	Interest	Total
63–235	[1] $59.04	$2.88	$3.54 (12 months)	$65.46
63–337	[2] 206.11	----------	18.54 (18 months)	224.65
63–483	[3] 150.70	----------	18.08 (24 months)	168.78
63–1074	[4] 9.89	----------	1.18 (24 months)	11.07
63–1396	[5] 1,126.28	----------	202.68 (36 months)	1,328.96
Total	----------	----------	----------	1,798.92
Less payments made by debtor	----------	----------	----------	287.85
Claim allowed	----------	----------	----------	1,511.07

[1] Cash received by debtor.
[2] $95.11 cash; $108 payment to Franklin Loan; $3 recording fees.
[3] $149.70 cash; $1 recording fees.
[4] Cash received by debtor.
[5] $10.28 cash; $1,044 payment to City Finance; $72 payment to Consolidated Credit.

(6) From this computation it will be noted that interest has been allowed on the principal amount loaned. Merit contends that it is entitled to deduct interest on the face amount of the note which includes interest. No brief has been submitted on this point, however. If Merit is mistaken in this position, its instrument is usurious on its face and therefore unenforceable. *White v. Kaminsky*, supra. Also, Merit charged interest on investigation fees and such fact appears on the face of the instrument. T.C.A. 45–2007(i) authorizes an investigation fee not to exceed 4 per cent on the "principal amount loaned." This also raises the question of the instrument being usurious on its face and therefore unenforceable. No determination of this question appears necessary at this time. Merit's claim is allowed in an amount deemed equitable to the parties involved; the money advanced by Merit will be repaid in full with interest.

ORDER

At Knoxville, Tennessee, in said district, on the 8 day of June, 1966.

In accordance with the foregoing findings of fact and conclusions of law, it is

ORDERED, that claim No. 5, filed by Merit Finance Company on the 9 day of March, 1966, be, and the same hereby is, allowed as a secured claim in the amount of $1,511.07.

CLIVE W. BARE,
Referee in Bankruptcy.

IN THE COURT OF APPEALS OF TENNESSEE, EASTERN SECTION

JULIUS C. COBB, COMPLAINANT-APPELLEE, VS. PAUL E. PUCKETT, ET AL., DEFENDANT-APPELLANT

From the Chancery Court for Hamilton County—Honorable Ray L. Brock, Jr., Chancellor

AFFIRMED

Wood & Wood of Chattanooga for Julius C. Cobb.
Eugene N. Collins of Chattanooga for Paul E. Puckett, et al.

OPINION

Parrott, (J.)

Julius C. Cobb filed the bill in this case against the individually named defendants and their partnership company which is engaged in the small loan busi-

ness in Chattanooga, operating under the Industrial Loan & Thrift Act, to recover alleged usury and overcharges.

The Chancellor, in a well-written and comprehensive opinion, awarded and the defendant a judgment in the amount of $114.36 for usury and overcharges and $500.00 punitive damages.

The original loan in question was made on April 23, 1960, with the complainant receiving $38.98 and signing a note in the amount of $48.00 and giving a chattel mortgage on a General Electric television set. On this transaction he was charged $1.00 for life insurance, $2.50 for fire insurance, $2.88 for accident and health insurance, $1.92 for investigation fee, and 72 cents interest. From the date of the original note until February 1, 1964, this note was renewed or "flipped" eighteen different times [see attached chart]. On each occasion complainant was charged similar fees as on the first note. On various of these transactions, as shown by the chart, he was given refunds on insurance and interest. A computation of all the transactions shows the complainant has received $442.98 from the loans and has paid a total of $653.00 which includes $19.00 life insurance, $61.78 fire insurance, $95.22 accident and health insurance, $63.68 investigation fees, $31.36 interest and has received a total in refunds of $21.82.

Of the above mentioned charges, the Chancellor found the defendant was justified in charging the first investigation fee of $1.92 but the remaining investigation fees of $61.76 bore no reasonable relation to the expenses and services of the lender. He further found the borrower had made no request for life insurance, accident and health insurance and such insurance was purchased by the defendant without complainant's knowledge.

After giving credit for the refunds on the life and accident and health insurance, the Chancellor found there was an overcharging of $108.80 of insurance premiums. This amount plus the $61.76 overcharge on investigation fees totals $170.56. After deducting $56.20, the amount owed by complainant on the last note, a judgment of $114.36 for usury and overcharges was entered plus $500.00 for punitive damages.

Defendants in this appeal insist the Industrial Loan & Thrift Act does not vest a right of action in a borrower but is regulatory in nature and only vests police powers in the Department of Insurance and Banking.

This question is not raised by any of the pleadings and it appears it was not called to the attention or decided by the Chancellor. Hence, this Court could ignore the issue.

Since this appears to be the first time this question has been raised in the appellate courts, in an effort to avoid future controversy, we deem it proper for us to respond.

In other cases involving this same act, this Court has assumed the borrower had a cause of action for charges in excess of those provided by the act. We are of the opinion this position is sound and now do so hold.

The legal intent and purpose of the Industrial Loan & Thrift Act and the Small Loan Act are the same. It is true both acts are regulatory in nature but neither precludes a borrower from bringing a suit for charges of fees, interest and insurance premium which are in excess of those provided for in the act.

Our Supreme Court, in discussing the purpose and intent of the Small Loan Act in the case of Family Loan Co. v. Hickerson, 73 S.W. 2d 694, at page 697, said:

"As held in Personal Finance Co. v. Hammack, 163 Tenn. 645, 45 S.W. 2d 528, the act is regulatory. The purpose was to impose restraint on those engaged in dealing with impecunious borrowers, by regulating the maximum that could be charged and by providing penalties and forfeitures for exceeding the maximum. By the adoption of this regulatory statute the Legislature conferred no right upon lenders operating under it to exact more as compensation for the use of money than others are permitted to receive and collect. Whether the contract between the borrower and lender was designed to evade laws that forbid usury is always a question of fact determinable by inquiry into the particular transaction. Extraneous charges and expenses cannot be added. It is the rule repeatedly expressed in the actions involving claims for usury that the courts disregard form and look to the substance. McWhite v. State, 143 Tenn. 222, 226 S.W. 542."

We think the court's reasoning in the Hickerson case is applicable to the Industrial Loan & Thrift Act. If the Legislature had intended to preclude actions by the borrower for overcharges, it would have said so in the act.

Defendant also insists the Chancellor erred in holding the complainant was overcharged or did not know he was being charged with life, accident and health insurance.

We reject this insistence and concur with the Chancellor. The complainant testified he had no knowledge of being charged with insurance premiums except the fire insurance and he was never given any policies. From the proof as a whole, it appears that as a matter of course the defendant included these insurance premiums on all loans.

Defendant also challenges the Chancellor's holding on the investigation fees. As pointed out by the Chancellor, the defendant's manager testified he could not say what expenses, if any, had been incurred in checking the credit of the complainant. With the frequency and regularity with which these loans were "flipped," we doubt if the defendant had sufficient time to make an investigation on each loan.

We are in accord with the Chancellor that the repeated charges of an investigation fee and the charges for the insurance premiums which the plaintiff had not requested were designed to conceal and to secure excessive charges for the use of the money.

Our Supreme Court, in the case of Mallory v. Columbia Mortgage & Trust Co., 150 Tenn. 219, said:

"In determining whether or not a given transaction is tainted with usury it is generally held that the court will disregard the form and look to the substance. *Good faith is the decisive factor when compensation is exacted and received by an intermediary [lender] in addition to the legal rate.*"

In our opinion these charges are in no way expenses incident to the making of the loan or do they bear a reasonable relation to the service extended by the lender. On the contrary, they are evidence that the lender did not deal with the borrower in good faith.

Under Tennessee law where usury appears upon the face of an instrument, the obligation is unenforceable. White v. Kaminsky, 196 Tenn. 180, 264 S.W. 2d 813.

If, however, usury does not appear upon the face of the contract, it is valid to the extent of the money loaned and lawful interest and voidable only as to the usurious excess and to this extent the court will enforce the contract. Bank v. Walter, 104 Tenn. 11, 55 S.W. 301.

There being no usury on the face of these instruments, the Chancellor correctly applied the latter rule by enforcing the contract and giving the respective parties credit due for all amounts within the contract.

This brings us to the Chancellor's holding the defendants were liable for punitive damages.

Our Supreme Court, in the case of Bryson v. Bramlett, 321 S.W. 2d 555, reversed this court and held that a borrower may recover punitive damages from a money lender in acts involving fraud, malice, gross negligence, oppression or harassment. The reason given for the allowance was to serve as an example or warning to the parties and to deter similar transactions. So, there seems no question that the Chancellor had the authority to award punitive damages.

As to the amount of punitive damages, the case of Lichter v. Fulcher, 28 Tenn. App. 670, 125 S.W. 2d 501 at page 508 gives a clear and succinct statement:

"Where the case is tried before the Chancellor it is obvious that it is peculiarly within the discretion of the Chancellor as to how much, if any, punitive damages should be allowed. It is a matter of discretion which will not be interfered with by this court. We know of no fixed rule which could guide this or any other court in fixing the amount of exemplary damages to be awarded. And we know of no reason why we should substitute our judgment for the judgment of the Chancellor in this respect. The fact that we have the latter say in the matter offers no reason for altering the decree entered, and we are not inclined to do so."

We are of the opinion it is wrong for a lender of money to charge investigation fees when no investigations are made and to charge for insurance premiums without the knowledge of the borrower. To do such on eighteen successive loans compounds these wrongs and is unconscionable—one step removed from pickpocketing and larceny. Such action is a gross display of bad faith on the part of the lender and justifies an award of punitive damages.

After considering the entire record, we find the evidence preponderates in favor of the Chancellor's decree and there was no abuse of discretion on the part of the Chancellor in awarding punitive damages.

Thus, all assignments of error are overruled, the decree of the Chancellor is affirmed with the costs taxed to the appellant.

Judge.

Concur:

---- P.J.

---- J.

Date	Amount of note	Cash received	Amount paid	Insurance			Investment fee	Interest	Refunds
				Life	Fire	A. & H.			
Apr. 23, 1960	$48	$38.98	$32.00	$1	$2.50	$2.88	$1.92	$0.72	
June 21, 1960	48	22.98	16.00	1	2.50	2.88	1.92	.72	
July 20, 1960	88	41.10	22.00	1	3.34	5.28	3.52	1.76	$0.84
Sept. 20, 1960	88	7.94	44.00	1	3.34	5.28	3.52	1.76	.84
Nov. 23, 1960	88	29.94	22.00	1	3.34	5.28	3.52	1.76	.84
Jan. 27, 1961	88	7.94	44.00	1	3.34	5.28	3.52	1.76	4.28
Mar. 21, 1961	88	33.38	22.00	1	3.34	5.28	3.52	1.76	1.02
May 24, 1961	88	8.12	46.20	1	3.34	5.28	3.52	1.76	1.02
Aug. 22, 1961	88	30.12	45.10	1	3.34	5.28	3.52	1.76	
Nov. 25, 1961	88	29.10	45.10	1	3.34	5.28	3.52	1.76	1.02
Feb. 24, 1962	88	29.02	91.30	1	3.34	5.28	3.52	1.76	
Oct. 6, 1962	88	73.10	44.00	1	3.34	5.28	3.52	1.76	1.02
Dec. 8, 1962	88	30.12	22.00	1	3.34	5.28	3.52	1.76	1.02
Feb. 9, 1963	88	8.12	22.00	1	3.34	5.28	3.52	1.76	4.28
Apr. 6, 1963	88	11.38	23.10	1	3.34	5.28	3.52	1.76	1.02
June 15, 1963	88	7.02	22.00	1	3.34	5.28	3.52	1.76	1.02
Sept. 7, 1963	88	5.92	22.00	1	3.34	5.28	3.52	1.76	1.80
Nov. 16, 1963	88	7.80	46.20	1	3.34	5.28	3.52	1.76	1.80
Feb. 1, 1964	88	30.90	22.00	1	3.34	5.28	3.52	1.76	
Total		452.98	653.00	19	61.78	95.52	63.68	31.36	21.82

[From the Chattanooga Times, Oct. 2, 1960]

CREDIT MEN HERE ALARMED BY HIGH BANKRUPTCY RATE—ASSOCIATION ANALYZES SYSTEM—DOCTOR BILLS LEAD IN UNCOLLECTED DEBTS, COURT SUITS WITH LOAN COMPANIES SECOND

HOW 3,368 ACCOUNTS WERE LISTED IN REPORT

Type of creditors	Number of creditors listed	Percent of total	Total amount	Average size of account
Medical	770	22.3	$62,124.81	$80.68
Loan and finance	657	19.6	239,048.90	363.85
Clothing	397	11.7	27,119.76	68.31
Furniture and appliance	373	11.4	63,568.01	170.42
Automotive	323	9.5	75,622.00	234.12
Food	210	6.2	18,110.96	86.23
Jewelry	107	3.4	7,468.09	69.75
All other	531	15.9	92,203.80	173.64
Total	3,368	100	585,270.33	

Of the listed debt $260,402.95 was secured. Only $30,581.62 of the liability was for "accommodation papers" and $25,600 of this was listed by four persons, thus indicating that practically no petitions were filed to escape from debts created by endorsing notes for someone else.

In considering the tabulations it is well to take into account the fact that certain of the creditors listed do not in the end lose in the same proportion as their debts may appear. Loan and finance companies are usually protected by chattel mortgage or by endoresment of a person other than the bankrupt. Furniture and appliance dealers in most instances are protected by sales liens. The medical, clothing and food groups, on the other hand, rarely, if ever can count on salvaging anything from an account bankrupted on.

There were assets of $116,321.38. However, most of this amount was shown in a very few of the cases examined, and usually where there were any assets of consequence the petition showed a large amount of secured debt. It can be stated that practically all of the cases could be termed "no asset" cases.

While the average amount of liability was approximately $2,900 each, it is interesting to examine 20 of the cases (10 per cent), where a very small amount of debt was shown in the bankruptcy schedule:

Liabilities	Amount	Secured	Unsecured	Annual income
1	$533.00	$533.00	0	$1,000
2	299.13	0	299.13	1,000
3	572.50	0	572.00	2,800
4	525.20	0	525.00	[1]
5	369.05	0	369.05	2,000
6	364.00	0	364.00	2,250
7	365.00	264.00	101.00	5,800
8	607.86	299.25	208.61	700
9	728.00	0	728.00	1,200
10	561.00	561.00	0	2,288
11	340.13	120.65	219.48	2,458
12	296.15	289.00	47.15	3,200
13	446.00	413.00	33.00	720
14	352.00	218.00	89.00	730
15	659.00	523.00	136.00	2,750
16	576.00	152.00	424.00	3,000
17	370.00	110.00	260.00	500
18	674.00	10.00	664.00	2,100
19	495.00	280.00	215.00	2,300
20	668.75	120.00	548.75	2,100
Total	9,801.77	3,992.90	5,803.17	38,896

[1] Unknown.

When court costs and fees are considered, it would appear that in some cases the creditors could have been paid about as easily as the costs. It should be pointed out that in some cases a pauper's oath is filed in payment of costs in these cases.

The following study was made to determine if perhaps some of those filing petitions might have avoided doing so if they had had the proper guidance from their creditors; their employers; their attorneys, or from the court.

Amount of liability	Number of petitions	Percent
Less than $1,000	39	19.5
$1,000 to $2,000 [1]	73	36.5
$2,000 to $3,000	36	18.0
$3,000 to $4,000	19	9.5
$4,000 to $5,000	7	3.5
Over $5,000	26	13.0

[1] 56 percent.

For the purpose of trying to determine if there is any relation between the type of creditors being listed in bankruptcy petitions and the type of creditors filing suits in the sessions court, a study of 16,209 suits filed during the 12-month period ending in April 1960 was made and the following facts charted:

Type of creditor suing	Number of suits filed	Percent of total	Total amount of suits	Average size of suit
Medical	3,632	22.5	$217,794.88	$59.96
Loan and finace	2,624	16.2	371,108.89	142.60
Clothing	2,609	16.1	163,051.24	62.49
Furniture and appliance	1,917	11.8	279,238.09	145.66
Automotive	1,556	9.6	143,957.76	92.51
Food	854	5.2	41,506.89	48.60
Jewelry	694	4.3	49,137.00	70.80
All other	2,323	14.3	373,270.00	160.69
Total	16,209	100%	1,642,064.75	

A comparison of the two charts showing the percentage of those listed in bankruptcy schedules and those filing suits in sessions court is as follows:

Type of creditor	Percent of suits filed	Percent of listings in bankruptcy
Medical	22.5	22.3
Loan and finance	16.2	19.6
Clothing	16.1	11.7
Furniture and appliance	11.8	11.4
Automotive	9.6	9.5
Food	5.2	6.2
Jewelry	4.3	3.4
All others	14.3	15.9
Total	100.0	100.0

The bankruptcy law is being badly abused in Chattanooga and many persons are recklessly filing petitions with little or no regard to the serious moral and financial consequences of their future.

This is reported in a study made by the Retail Credit Men's Association a summary of which was released for publication.

George W. Lundy, manager of the credit bureau, explained that because of the upward trend in bankruptcies being filed in this federal district and the wide publicity being given to this "unfortunate" situation the president of the association appointed a committee to make a study of the matter for the benefit of its members.

The committee is composed of C. R. Belcher, president, Citizens Savings & Loan Corp.; R. B. Brotbeck, credit manager, Miller Bros. Co.; Walter P. Coppedge, senior vice president of the American National Bank and Trust Co.; Leslie L. Hudson, vice president, Johnson Tire Co. and president of the association, Lundy, secretary of the association and credit bureau manager, and John Parry, vice president of Fowler Bros. Co.

These persons represent a cross-section of the credit grantors in the community, Lundy pointed out. The purpose of the study was to determine the causes of the increase in the number of cases being filed and to learn why, in a period of relatively low unemployment and high prosperity, bankruptcies were not decreasing, as it would normally appear they should, he continued.

A table given in the report analyzes a total of 200 bankruptcy petitions involving total liabilities of $585,270.33 and 3,368 creditors.

In first place were medical creditors numbering 770, or 22.3 per cent of the total. The average account was $80.68 and the total amount $62,124.81. Second in number but first in dollars and cents involved were 657 finance companies listing a total of $239,048.90, or an average of $363.85.

Another table shows that of 20 petitions the average amount of liability per petitioner was $2,900, but that 10 percent of the cases showed only a small amount of debt ranging from $299.13 to $728.

Another table shows that 56 per cent of the 200 petitions were for more than $2,000 each. Thirty-nine had liabilities of less than $1,000 and 73 owed from $1,000 to $2,000 each.

MEDICAL CREDITORS SUE

A fourth table showed that of creditors in sessions court, the largest number—3,632—or 22.5 per cent of a total of 16,209, involved medical creditors. The total amount of suits was $217,794.88 of an average medical suit of $59.96. Second in number of suits and first in amount involved were those of loan and finance companies with 2,624 suits for $374,108.89 or an average of $142.60.

A fifth table compares suits filed in sessions court with listings in bankruptcy. Medical suits represented 22.5 of the total and medical listings in bankruptcy were 22.3 per cent, while 16.2 per cent of the suits listings finance companies accounted for 19.6 per cent of the bankruptcy listings.

"It is difficult to understand why more people are seeking relief from debts during times when personal savings are at an all-time high figure, when savings and loan associations report the highest amount of share accounts, in the history of such institutions, when wages and salaries are at a high level,

when fewer people are unemployed than average, when more people have more life insurance savings and when more people own or are buying their homes," Lundy said.

MANY PHASES CONSIDERED

"Many phases of the dilemma were considered by the committee. First, they asked themselves: Has the system and the machinery of consumer credit broken down? Are credit grantors too lax in the manner they extend credit or is it the fault of the people who do the buying? Is John Q. Public, after all, as honest as we have been assuming he is?

"Is the manner of exchanging credit information through the credit bureau adequate or does the fault lie in the fact that enough credit information is available to avoid getting these defaulters on the books but no heed is paid to the information that is available? Do credit grantors rely too strongly on the fact that if a person does not pay you can sue him? Are too many suits being filed? Is our Tennessee garnishment law too severe?

"Should the garnishment law be repealed and credit be extended on the basis of the debtor's established willingness to pay, rather than as now on the creditor's ability to sue and force payment?

"If it is the fault of those extending credit, then which group of credit grantors is most guilty of leading or influencing people to go into bankruptcy? Is it the butcher, the baker, or the candle stick maker; the clothing merchant; the jeweler; the grocer; the automobile dealer; the doctor; the loan and finance company; the furniture store; the banker, etc.

"Second, the question was asked as to whether any fault could be laid in the mechanics of obtaining a discharge in bankruptcy. Do attorneys simply file petitions because a client or prospective client asks them to do so, or do they counsel with the client and seek always to advise him of the entire consequences of bankruptcy, and offer some alternate plan of relief?

COMPREHENSIVE STUDY

"Third, many questions were raised about the person bankrupting. He is the person who was the beneficiary of the goods or services purchased. He is the person, after all, who made the debt and it is he the creditors were looking to for payment. He is the person who the rest of his life will be called upon to 'explain' each time he asks someone else to trust him in a financial transaction.

"Here are some of the questions the committee asked about him: How old is he? Is he married, divorced or single? Does he have a large or a small family? Has he ever bankrupted before? Is he employed? If so, how long has he been on the job? What was his general credit rating before he bankrupted? Do women bankrupt too?

"Why did he elect to 'throw in the towel' rather than to suffer the inconveniences and discomforts of meeting his obligations when the going got rough? Are there sometimes moral 'implications' involved in personal bankruptcy? Does modern advertising create such a strong desire in him for the finer things of life and modern sales and credit plans make it so easy for him to get these finer things, that he is unable to resist biting off more than he can chew?

"It was the hope of the committee that the answers to many of these questions might lead to the answer of the one big question—why an increasing number of Chattanoogans—more so than in other adjoining communities—are bankrupting during a period of prosperity."

"In an attempt to find these answers 200 bankruptcy petitions filed here between January 1959 and June 1960 were picked at random and examined in detail. He explained some of the facts revealed by these court records have been rather startling and have, the committee thinks, led to some conclusions it will be well to examine.

Among these are the fact that 10½ per cent of them had bankrupted before. Sixty-one per cent of them had poor credit ratings during the period proceeding their bankruptcy, and 31 per cent had only fair credit ratings, while 8 per cent had good ratings. On the basis of this it would appear that either the petitioners were very adept at getting credit or that credit managers and shop keepers were lax in letting their wares out on the cuff," it was stated.

MOST HAD JOBS

"Normally, when you think of some poor fellow being 'forced' to go into bankruptcy you would assume the fellow was out of work, owed a lot of money, and had a big family to feed." Lundy said. "The court records show practically all were working, and that on an average their earnings were greater during the year they bankrupted than they had been during the preceding year.

"Of the names on the petitions, the credit bureau had recently made reports on 108 of them. From these reports it was learned that the average bankrupt had been on his job five years and nine months. These same reports show that persons with large families rarely ever bankrupt, and that the average petitioner had 1.48 dependents. Eighty-one per cent are married, 15 per cent are divorced, and 4 per cent are single.

"An interesting statistic is the fact that 76.5 per cent of those filing are men and 23.5 per cent are women. Because the researching committee was surprised that approximately one person out of four bankrupting was a woman, it was decided that a search of the records 20 years ago would be made for comparison. In 1940 the ratio average was 83.3 per cent men and 11.7 per cent women, thus indicating that the percentage of women bankrupting, as compared to men, has about doubled in 20 years."

The 200 petitions were filed by 63 of the approximately 350 attorneys practicing locally, with 102 of them, or about 50 per cent being filed by nine attorneys, the committee found. There were total liabilities, in the cases checked, amounting to $585,270.33. A detailed tabulation of all creditors listed in the schedules was made and distributed as to type of creditor owed.

CALLED SERIOUS

After consideration of the disclosures of the survey and conferences with leaders in the consumer credit field, the committee said it came to the conclusion that the situation with regard to bankruptcy in the community has reached serious proportions.

The seriousness of the situation lies not so much in the economic loss to creditors as it does in the breakdown or moral considerations of some of those bankrupting.

"The committee takes no issue with the bankruptcy law," the report continues. "It is a good law, and serves a good purpose in our American economic system, and a vast majority of the bankruptcies are justifiable cases. On the other hand, there appears to be evidences of abuse of the intent of the law. It might even be said that in some cases the court is being used as a dumping ground—a place to discard debts the petitioner no longer has the moral stamina to pay, even though he might possess the physical means to do so.

"Such conclusions as these raise the question as to who is responsible for the situation. It was concluded that the primary blame must rest on the abuser—he who comes into court with his problems. It was also concluded that there may be others who have unwittingly contributed to his delinquency. There are evidences of retailers making their wares too easy to obtain on credit. Some credit managers are often reluctant to say no when that word would be a kindness to the applicant who has demonstrated he is a poor manager of his financial affairs.

"Those engaged in the lending of money, while being 'a friend in need' when they bail a person out by consolidating his many debts into one, are sometimes inclined to allow a person to overload because they are secured on the transaction. Some tradesmen appear inclined to extend credit more on the strength of the fact they can sue and garnishee than they would be were it not possible to enforce payment in this manner.

"It appears to the committee that perhaps too many suits are being filed in our community and a close parallel is noted in that the groups filing the greatest number of suits are also the groups being listed the greatest number of times in the bankruptcy schedules. It is unfortunate indeed that in spite of the large number of our citizens who carry health insurance that the medical group is forced to resort to the courts to collect their fees in so many instances. It was noted in the survey that a majority of those bankrupting did so after having been sued.

"The committee feels that further study of our garnishment law should be made, for there appears to be some relation between the number of suits filed and the number of bankruptcies filed. The fact that many persons bankrupt soon after being sued is also a matter deserving further study.

"It is the hope of the committee that the attorneys who file the petitions are now and that they will continue to counsel their clients with reference to the stigma attached to bankruptcy. It is hoped that attorneys are taking full advantage of their opportunities to advise methods of setting debts in ways other than through bankruptcy, particularly so in those cases where the amount of debt appears to be so small.

"The committee admits it has no knowledge of the technical responsibility, functions and discretionary powers of the bankruptcy court, nor has it employed counsel to advise it in such matters. It relies solely in Webster's dictionary, the elementary edition, which defines a court as a place where justice is administered and on the old concept that he who comes into court must come with clean hands. At least one case came to the attention of the committee where the petitioner, in its opinion, did not go into court with clean hands. It is regrettable that this should have happened.

"Now as to those who obtain goods and services on their promise to pay at a later date and, because of their inability or inconvenience to discharge the debt seek relief in bankruptcy court, the committee feels that in too many cases petitions are filed because of poor advice or because they are mad at someone for suing them.

"It appears from the records that many petitions have been filed when much less drastic solutions could have been found. It also would appear that some petitions have been filed simply because it was an easy way out and these are the cases which appear to indicate moral degradation.

"In former years bankruptcy was considered, except in unusual cases, a badge of dishonor and disgrace. Although today it has lost some of its stigma, it is still nonetheless, considered as strictly derogatory in appraising one's fitness for trust in financial matters. As has been stated, a vast majority of the cases of bankruptcy are legitimate, but even so, many firms refuse credit solely on the basis of the fact that the person has in some previous year bankrupted. Most mortgage companies will refuse to take applications for the financing of homes from persons who have bankrupted unless the failure was a long number of years ago and the person is able to give a satisfactory explanation of the failure. Also, he must show evidence of complete recovery, and even then it is difficult for a former bankrupt to get a home financed.

"The better class retailers' requirements are about the same. Even those who do extend credit to a former bankrupt do so with a wary eye to the future, and the account is usually marked 'watch' until sufficient experience is had to assure them the person is stable. They fear that 10 per cent who will bankrupt again.

"Many persons have visited the credit bureau to see what can be done about getting that bankruptcy off my record. Their trip is in filed it becomes a part of their permanent record and remains with them 'until death do us part.' Many persons claim they were 'forced' to bankrupt, but that they have since paid off their debts, and some—very few—do.

"What does happen is that they pay the company holding the mortgage on the car, otherwise they would have to give it up. They pay the note for borrowed money on which Uncle Joe is endorser, otherwise there would be a family 'incident.' They pay the mortgage on the furniture unless it is so worn out they think the loan and finance company would not have it. They pay the installment on the TV, otherwise it goes back to the dealer. Very very few ever pay the doctor, the grocer, and the other unsecured creditors.

"The committee concludes with the advice that bankruptcy is in many cases the only solution to a serious financial disaster, but that it is a most serious step for the person filing the petition. It is something that, whether justifiable or not, will live to haunt the bankrupt the rest of his life."

(Mr. James E. Moriarty, referee in bankruptcy, U.S. District Court, Central District of California, submitted the following material on the various codes in California and the bill introduced by Assembly-

woman Yvonne Brathwaite in the California Legislature pertaining to garnishment and other material relation to her bill:)

CALIFORNIA FINANCIAL CODE

Small Loans—Section 24000 et seq.

Sections 24005
24410
24411
24412
24451 as amended
24452 as amended
24453 as amended
24454
24468

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In general 3
Purpose 2
Validity 1

Library references

Pawnbrokers and Money Lenders ⟹3.
C.J.S. Pawnbrokers § 4.

1. Validity

The Small Loan Act exempting from its operation banks, trust companies, building and loan associations, industrial loan companies, credit unions, licensed pawnbrokers, nonprofit agricultural cooperatives, corporations loaning money pursuant to Agricultural Credit Act, bona fide conditional contracts of sale involving disposition of personal property when not used for purpose of evading the Act, licensed personal property brokers, and licensed real estate brokers does not deny "due process" and "equal protection" of law because it does not uniformly apply to all classes of lenders. Ex parte Fuller (1940) 102 P.2d 321, 15 C.2d 425.

The Small Loan Act does not deny "due process" and "equal protection" of law because of fact that it applies only to loans of $300 or less. Id.

2. Purpose

The purpose of this division was to forbid use of credit as a substitute for money in what would be usurious transactions if money were loaned directly. Master Charge v. Daugherty (1954) 267 P.2d 821, 123 C.A.2d 700.

The purpose of legislation regulating the operations of persons procuring or making small loans is to protect the public from lenders who would otherwise take advantage of the needy. People v. Vanderpool (1942) 128 P.2d 513, 20 C.2d 746.

3. In general

In action by notary against employer, a personal property broker and small loan agency, to recover notary fees, evidence that notary, under threat of discharge from employment, indorsed check for fees to which she was entitled under Personal Property Brokers Act and Small Loan Act to employees' association organized by employer, supported finding that employer exercised duress upon notary. Millsap v. National Funding Corp. (1944) 152 P.2d 634, 66 C.A.2d 658.

§ 24001. *Definitions.* Unless the context otherwise requires, the definitions given in this article govern the construction of this division. (Stats. 1951, c. 364, p. 1146, § 24001.)

Derivation: Stats. 1939, c. 1045, p. 2886, § 2.

§ 24002. *Broker.* "Broker" includes all who are engaged in the business of negotiating or performing any act as broker in connection with a loan to be made by a lender. (Stats. 1951, c. 364, p. 1146, § 24002.)

Derivation: Stats. 1939, c. 1045, p. 2886, § 2.

§ 24003. *Charges; costs.* "Charges" includes the aggregate fees, bonuses, commissions, brokerage, discounts, expenses, and other forms of costs, except interest charged, contracted for or received by a lender or a broker, or any other person in connection with the investigating, arranging, negotiating, brokering, guaranteeing, making, servicing, collecting, and enforcing of a loan or a forbearance

of money, credit, goods, or things in action, or any other service rendered. (Stats. 1951, c. 364, p. 1146, § 24003.)

Derivation: Stats. 1939, c. 1045, p. 2886, § 2.

§ 24004. *Charges; profit or advantage.* "Charges" include any profit or advantage of any kind that any licensee may contract for, collect, receive, or obtain by a collateral sale, purchase, or agreement, in connection with the negotiating, arranging, making, or otherwise in connection with any loan of three hundred dollars ($300) or less. (Stats. 1951, c. 364, p. 1146, § 24004.)

Derivation: Stats. 1939, c. 1045, p. 2895, § 19; Stats. 1943, c. 251, p. 1165, § 2.

§ 24005. *Charges; exclusion of certain commissions.* "Charges" do not include commissions received as a licensed insurance agent or broker in connection with insurance written as provided in Section 24466. (Stats. 1951, c. 364, p. 1146, § 24005.)

Derivation: Stats. 1939, c. 1045, p. 2895, § 19; Stats. 1943, c. 251, p. 1165, §.2.

§ 24006. *Commissioner.* "Commissioner" means the Commissioner of Corporations of the State of California. (Stats. 1951, c. 364, p. 1146, § 24006.)

Derivation: Stats. 1939, c. 1045, p. 2886, § 2.

§ 24007. *Lender.* "Lender" includes all persons who are engaged in the business of lending their own money, credit, goods, or things in action. (Stats. 1951, c. 364, p. 1146, § 24007.)

Derivation: Stats. 1939, c. 1045, p. 2886, § 2.

NOTES OF DECISIONS

In general 1
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1. In general

Whether a finance company purchasing conditional sales contracts for automobiles and trade acceptances on accounts receivable, is doing business within the Personnel Property Brokers Act or Small Loan Act depends on whether a sale or a loan of money is involved, and all circumstances of a particular transaction must be considered, but if there is a bona fide sale of a conditional sales contract, the mere fact that there is a guarantee of payment by the seller is not in itself enough to constitute the transaction a loan rather than a sale, nor would an agreement to repurchase a defaulted contract itself be sufficient to make the transaction a loan rather than a sale. 8 Ops. Atty. Gen. 157.

2. Loan of credit

Where corporation proposed to issue cards which would enable holders to purchase, on credit, merchandise or service at specified business places and card holder would sign an invoice which corporation would purchase at a discount from 6 to 10% and corporation would bill card holder for face amount of invoice and collect from him, transaction would be "loan of credit" to its card holders and corporation must procure a license as a lender before engaging in such a business. Master Charge v. Daugherty (1954) 267 P. 2d 821, 123 C.A. 2d 700.

§ 24008. *Lender; broker.* "Lender" and "broker," do not include employees of the lender or broker regularly employed at the particular location specified in the license of the lender or broker. (Stats. 1951, c. 364, p. 1146, § 24008.)

Derivation: Stats. 1939, c. 1045, p. 2886, § 2.

§ 24009. *Licensee.* "Licensee" means any lender or broker licensed under this division. (Stats. 1951, c. 364, p. 1146, § 24009.)

Derivation: Stats. 1939, c. 1045, p. 2886, § 2.

CROSS REFERENCES

Cooperative corporations, generally, see Corporations Code § 12200 et seq.
Nonprofit corporations, generally, see Corporations Code § 9000 et seq.

NOTES OF DECISIONS

1. Validity

The Small Loan Act exempting from its operation, nonprofit agricultural cooperatives, corporations loaning money pursuant to Agricultural Credits Act, 12 U.S.C.A. § 1151 et seq., does not deny "due process" and "equal protection" of law because it does not uniformly apply to all classes of lenders. Ex parte Fuller (1940) 102 P.2d 321, 15 C.2d 425.

§ 24052. *Conditional contracts of sale.* This division does not apply to bona fide conditional contracts of sale involving the disposition of personal property, when

such forms of sales agreements are not used for the purpose of evading this division. (Stats. 1951, c. 364, p. 1147, § 24052.)

Derivation: Stats. 1939, c. 1045, p. 2887, § 3.

NOTES OF DECISIONS

1. Validity

The Small Loan Act exempting from its operation, bona fide conditional contracts of sale involving disposition of personal property when not used for purpose of evading the Act, does not deny "due process" and "equal protection" of law because it does not uniformly apply to all classes of lenders. Ex parte Fuller (1940) 102 P.2d 321, 15 C.2d 425.

§ 24053. *Personal property brokers.* This division does not apply to any personal property broker or broker licensed under the Personal Property Brokers Law,[1] when transacting business as authorized by that law. (Stats. 1951, c. 364, p. 1147, § 24053.)

Derivation: Stats. 1939, c. 1045, p. 2887, § 3.

NOTES OF DECISIONS

1. Validity

The Small Loan Act exempting from its operation licensed personal property brokers does not deny "due process" and "equal protection" of law because it does not uniformly apply to all classes of lenders. Ex parte Fuller (1940) 102 P.2d 321, 15 C. 2d 425.

§ 24054. *Real estate brokers.* This division does not apply to any broker licensed under the Real Estate Law, Part 1, Division 4, of the Business and Professions Code,[1] when transacting business as authorized by that law. (Stats. 1951, c. 364, p. 1147, § 24054.)

Derivation: Stats. 1939, c. 1045, p. 2887, § 3.

NOTES OF DECISIONS

1. Validity

The Small Loan Act exempting from its operation real estate brokers does not deny "due process" and "equal protection" of law because it does not uniformly apply to all classes of lenders. Ex parte Fuller (1940) 102 P.2d 321, 15 C.2d 425.

§ 24407. *Preservation of records.* Licensees shall preserve their books, accounts, and records, including cards used in the card system, if any, for at least two years after making the final entry on any loan recorded therein. (Stats. 1951, c. 364, p. 1150, § 24407.)

Derivation: Stats. 1939, c. 1045, p. 2891, § 14.

§ 24408. *Annual report.* Each licensee shall file a report with the commissioner annually on or before the fifteenth day of March, giving such relevant information as the commissioner reasonably requires concerning the business and operations during the preceding calendar year of each licensed place of business within the State conducted by the licensee. The report shall be made under oath and in the form prescribed by the commissioner. (Stats. 1951, c. 364, p. 1150, § 24408.)

Derivation: Stats. 1939, c. 1045, p. 2891, § 14.

CROSS REFERENCES

Annual examination by commissioner, see § 24603.

§ 24409. *Composite of annual reports.* The commissioner shall make and file annually with the Division of Corporations as a public record a composite of the annual reports and any comments on the reports that he deems in the public interest. (Stats. 1951, c. 364, p. 1150, § 24409.)

Derivation: Stats. 1939, c. 1045, p. 2891, § 14.

§ 24410. *False or misleading advertising.* No person shall advertise, print, display, publish, distribute, or broadcast or cause to permit to be advertised, printed, displayed, published, distributed, or broadcast, in any manner any statement or representation with regard to the rates, terms, or conditions for making or negotiating loans, which is false, misleading, or deceptive, or, in the case of a licensee, which refers to the supervision of such business by the State or any department or official of the State. (Stats. 1951, c. 364, p. 1150, § 24410.)

Derivation: Stats. 1939, c. 1045, p. 2891, § 15.

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[1] § 22000 et seq.

[1] Business and Professions Code § 10000 et seq.