# UNIFORM CONSUMER CREDIT CODE (1974)*

*drafted by the*

NATIONAL CONFERENCE OF COMMISSIONERS
ON UNIFORM STATE LAWS

*and by it*

APPROVED AND RECOMMENDED FOR ENACTMENT
IN ALL THE STATES

*at its*

ANNUAL CONFERENCE
MEETING IN ITS EIGHTY-THIRD YEAR
ON MAUAI, HAWAII
AUGUST 1-9, 1974

*WITH PREFATORY NOTE AND COMMENTS*

Approved by the American Bar Association
Chicago, Illinois, February 24, 1975

*The Conference changed the designation of the Consumer Credit Code (1974) from Uniform to Model as approved by the Executive Committee on July 16, 1996.

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# UNIFORM CONSUMER CREDIT CODE (1974)

## PREFATORY NOTE

In promulgating the Uniform Consumer Credit Code (the "U3C") in 1968 (the "1968 Text"), the National Conference of Commissioners on Uniform State Laws proposed a completely new approach to the law governing consumer credit.

Enactment of the Code would abolish the crazy-quilt, patchwork welter of prior laws on consumer credit and replace them by a single new comprehensive law providing a modern, theoretically and pragmatically consistent structure of legal regulation designed to provide an adequate volume of credit at reasonable cost under conditions fair to both consumers and creditors. Upon its enactment, no longer would credit regulation within a State consist of a number of separate uncoordinated statutes governing the activities of different types of creditors in disparate ways.

All creditors dealing with consumers would be covered by the same statute. Under this Act, the total consumer credit process -from advertising through collection-would be within the scope of regulation, with variations in the law based on functional differences in the kinds of transactions rather than on the kinds of creditors involved. Whether a consumer is financing an automobile with a sales finance company or borrowing money from a consumer finance or small loan company, certain basic protections would apply across-the-board to safeguard the consumer.

Thus the Conference has chosen to approach consumer credit in much the same way it did so successfully with respect to secured transactions under Article 9 of the Uniform Commercial Code: function should prevail over form.

Nine States have now adopted the U3C: Oklahoma and Utah in 1969, and Colorado, Idaho, Indiana, and Wyoming in 1971, all in substantially the form of the 1968 Text; Kansas in 1973 in substantially that of the U3C Committee's Working Redraft No. 4; and Iowa and Maine in 1974 in substantially that of the Committee's Working Redraft NO.4 or 5. The Code has had an impact on the development of consumer credit law far beyond those States in which it has been adopted. Many provisions of the Federal Truth in Lending Act and Federal Reserve Board Regulation Z are traceable to the U3C. The National Consumer Act and, later, the Model Consumer Credit Act, although taking extreme consumer positions, follow the structure of the U3C. In 1971 Congress enacted for the District of Columbia comprehensive consumer credit legislation drawn in large part from the U3C. In 1972 Wisconsin enacted similar legislation based on the U3C and the National Consumer Act. Adaptations of U3C provisions have been enacted widely in the credit laws of many States; the home solicitation sale provisions are perhaps the best illustration.

### Revision of the 1968 Text

Events occurring after promulgation of the 1968 Text have made it desirable to revise it. Experience in the States which enacted the Code has proved that the Code works and that both

consumers and creditors are pleased with it, but this experience has also turned up a few unforeseen problems of the kind that come to light only after a law has been in effect. The revision has dealt with these matters as well as with some of the variations from the 1968 Text that were enacted in several of the States.[1]

The late 1960's and early 1970's have seen a number of important legislative and judicial developments in consumer credit. Information gained from legal services attorneys has thrown new light on the needs of poverty-level consumers, but has also revealed that those needs cannot be met solely by consumer credit legislation of general application. The National Consumer Law Center has produced a number of legislative proposals. The United States Supreme Court revolutionized debtor-creditor law in its *Sniadach*[2] decision in 1969. Developments at both the federal level (Consumer Credit Protection Act, Regulation Z, Fair Credit Reporting Act) and the state level (Wisconsin Consumer Act) have invited a review of the U3C. Then, too, new ways of granting consumer credit appeared on the scene during this period. The concept of a nation-wide credit card was in its infancy when the 1968 Text was being prepared in the 1960's; today it is a reality.

A major factor calling for a review of the U3C is the Report of the National Commission on Consumer Finance ("NCCF"). This landmark study, the product of three years of work by a federally sponsored Commission, is the first comprehensive examination in the United States of the whole field of consumer finance. The recommendations of the Commission reflect both objectivity and understanding of the complex consumer credit process.

The National Commission on Consumer Finance was authorized under Title IV, Section 404 (a) of the Consumer Creait Protection Act to " . study and appraise the functioning and structure of the consumer finance industry, as well as consumer credit transactions generally." It issued its Report on December 31, 1972, four weeks after the U3C Committee's Working Redraft NO.4 was published. The Report contains some 100 recommendations intended to improve the consumer credit marketplace, over 40 of which were intended exclusively for implementation by federal statute, *e. g.*, amendments to the Truth in Lending Act and to the Bankruptcy Act. Of the 60 or so recommendations requiring State action, at least 15 related to matters entirely outside the scope of the U3C, *e. g.*, bank branching and enforcement of antitrust laws. Thus only about 45 recommendations required consideration by the U3C Committee.

Of these 45 recommendations, the U3C Committee's Working Redraft NO.4 anticipated over half. The Committee's Working Redraft NO.5 and this Act substantially implement the National Commission's recommendations regarding co-signer agreements, door-to-door sales, buyer's claims and defenses in credit card and other consumer credit transactions, deficiency judgments, "sewer service," limitations on garnishment, debt collection practices, and State enforcement of the Federal Truth in Lending Act. Thus, this Act reflects a conscious and, it is believed, successful effort to incorporate into a single comprehensive code the majority of the recommendations of the National Commission on Consumer Finance that were intended for implementation by state action.

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[1] See Report NO.1 of the U3C Committee which contains comments of the Committee on the desirability of the variations in State enactments of the 1968 Text.

[2] Sniadach v. Family Finance Corp. (1969) 89 S.Ct. 1820, 395 U.S. 337, 23 L.Ed.2d 349.

## Price of Credit

A basic issue in any regulation in this area is the price of credit. In simplest terms, consumers want credit at the lowest possible prices, and creditors want to supply credit but can and will do so only if they may reasonably expect repayment of principal plus an adequate return on credit extended. In a free economy the prices of goods, services and land traditionally have been controlled by free operation of the market place. To some extent this principle has also extended to the price of credit but for a variety of historical reasons since before the time of Christ, societies have attempted to control the price of credit by executive or legislative fiat. Invariably these attempts have either dried up "legal" or legitimate credit or significantly reduced the amount of credit which would have been available in a free economy. Invariably, too, consumers have been losers by this process.

For hundreds of years in England[3] and in the American colonies and in most of the States, general usury statutes prescribed such low maximum ceilings that they materially interfered with the extension and free flow of credit. In many areas general usury statutes have prevented entirely or reduced substantially the extension of credit with the result that either the courts or legislatures found it necessary to provide a proliferation of exceptions to these statutes. The basic premises of the 1968 Text were that (1) in the business area general usury statutes should be terminated completely and control of the price of credit left solely to the free operation of the market place; (2) although in the consumer credit area the operation of the same free enterprise principles is equally warranted, many consumers do not have equal bargaining power with creditors and traditionally have been protected by governmental controls, including maximum rates, and the U3C should provide recommended maximum rates in a standard form more simple and understandable than a hodgepodge of exceptions to general usury statutes; and (3) any rate structure provided should be of the maximum ceiling variety and not a specification of actual rates to be charged as in the regulation of public utilities.

The U3C Committee's Working Redrafts Nos. 1 through 5[4] and this Act reflect the belief, strongly buttressed by the NCCF Report, that these basic premises are sound and reaffirm them. The proposed specific ceiling rates are socially and economically sound and fit with the other provisions of the U3C and the approach used in drafting it.

This Act makes no change in the specific maximum rates included in the 1968 Text. Empirical evidence developed since 1968 and cited in the U3C Committee's Report NO.1 strongly supports the wisdom of the basic principles adopted and the specific rates suggested. Although the 1968 Text's maximum rates were lowered in some enacting States, in all these States consumer credit has been extended in most cases at rates below the ceilings permitted by the U3C. Five of the six enacting States studied in the Committee's Report NO.1 lowered the maximum ceiling on revolving sale credit from 24% per annum to 18%; however, tr.is change is rejected because the cost studies referred to in the Committee's comment in its Report No. 1

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[3] England repealed its usury laws in 1854.
[4] The U3C Committee's Working Redrafts Nos. 1 and 2 were internal; its Working Redrafts Nos. 3, 4, and 5 were distributed widely.

consistently establish that in the case of substantially all sellers, the cost of extending revolving consumer sales credit exceeds 18% per year. For the reasons stated in Report No.1, reduction in this ceiling rate is believed to be economically unsound.

The extensive studies and findings reported in Chapters 6, 7 and 8 of the NCCF Report clearly support the reasonableness of the U3C maximum ceilings. If anything, the NCCF Report indicates that if the U3C ceilings are open to criticism, the ground should be that they are too low at least for small, short term extensions of credit.

The United States is now experiencing serious inflation. In attempting to combat this inflation the federal government has imposed price controls and ceilings on some goods and services. Opinions may differ as to whether these controls or ceilings were or were not desirable, but there can be little doubt that they not only have not controlled prices significantly but also have caused severe dislocations in the supplies of some goods and services. The difficulties coming to light in these attempts to control prices of goods and services extend equally to attempts to control the price of credit by legislation. General usury statutes and other state laws limiting rates on home mortgages below free market rates have drastically reduced the availability of mortgage funds, the volume of home construction, and employment in the building trades.

## Competition and Freedom of Entry

In advocating primary reliance on the market place to control the price of credit, the National Conference has recognized the fundamental importance of competition to permit market forces to operate most effectively, a recognition consistent with the conclusions of the National Commission on Consumer Finance. In moving away from the segmented controls of particular types of credit grantors in consumer credit laws prior to the U3C to a single comprehensive statute dealing with consumer credit generally, it is believed that competition has been and will be enhanced. In the U3C Committee's Working Redrafts Nos. 3 through 5 and in this Act, this comprehensive approach has been continued and strengthened by eliminating the separation and duplication in the treatment of sales credit and loans provided in the 1968 Text.

Licensing is a means of providing governmental control of particular kinds of activity, but it restricts freedom of entry into markets and inhibits competition. The 1968 Text avoided the extension of licensing requirements and also sought to diminish existing licensing requirements.

However, the small loan industry, accustomed to licensing under pre-Code law, in no way objected to licensing and entirely approved of its continuance under the U3C. Moreover, banks and thrift institutions contended that since they could not open offices without the approval of supervisory authorities and since all their activities were regulated and subject to close supervision and examination, small loan lenders should be subject to similar requirements. Consumer comment received on this issue favored increasing rather than decreasing licensing requirements. In response to these various views, the U3C Committee's Working Redrafts Nos. 3 through 5 and this Act have added in Section 2.302 the requirement that licensees obtain a separate license for each place of business where loans are made.

As in the 1968 Text, any lender making loans at a rate in excess of 18% per annum either must be a bank, thrift institution or other supervised financial organization (subsection (41) of Section 1.301) or obtain a license under Section 2.302. On the other hand, this Act avoids imposing on sellers or other types of organizations not engaged in lending any requirement to obtain a license, whether the business carried on is direct or through the use of credit cards. (See subsections (12), (15), (25), and (39) of Section 1.301 and Sections 2.301 and 2.302.)

## Consumer Oriented Changes and Additions

Another basic issue in the regulation of consumer credit is adequate protection of consumers from creditor practices and agreements that are abusive or have a potential for abuse. Drawing upon the sources referred to in this Prefatory Note, a substantial number of consumer oriented changes from the 1968 Text have been included in this Act. It is believed that each change or addition has merit and will provide additional protection to consumers but will not interfere with the extension of consumer credit or with legitimate practices of the great majority of creditors.

In making these consumer oriented changes, the necessary relationship between these changes and the U3C rate structure has not been forgotten. In the language of the National Commission on Consumer Finance :

> Recommendations regarding remedies are inextricably inter(-Woven with Commission recommendations on rates and availability……It is imperative that the relationship be realistically assessed--the higher the rate the fewer the remedies needed and vice versa. States may decide to narrow or broaden Commission recommendations on remedies and contract provisions. But they should recognize that modifications are likely to affect the cost and availability of consumer credit.[5]

A summary of many of these changes and additions follows.

### (1) Holder in Due Course; Sales Related Loans; Credit Cards

A major controversial area in consumer credit has been that related to the holder in due course doctrine as applied to outright transfers of retail paper, to sales related loans and to credit card transactions. Traditionally banks and others made credit judgments on purchases of consumer paper solely on the basis of the credit of the buyer and without regard to any aspects of the sale transaction being financed. Insulation of creditors from claims and defenses arising out of sale transactions was obtained in different ways: by use of negotiable notes generating the rights of a holder in due course, or by provisions in contracts freeing assignees of rights under contracts from claims or defenses of buyers against sellers. Banks and others have attempted to preserve these longstanding principles. They have argued that they are lenders of money, not sellers of goods or services, that buyers have the right and responsibility of picking sellers, and that buyers should look solely to sellers for cure of violations of sales contracts, breaches of warranty, and the like.

[5] NCCF Report, p. 24.

On the other hand, consumer advocates contend that financing institutions often have close relations with sellers from whom notes and rights under sales contracts are acquired, that these institutions are better able than consumers to police sellers and to require of them reasonable standards of performance. Consequently, consumer advocates contend that creditors acquiring sale paper should *not* be free from claims and defenses of buyers against sellers. Consumer advocates have no difficulty in providing examples of hardships suffered by aggrieved buyers when faced with contentions by assignees of their contracts that the assignees know nothing about the details of the sales and should not be affected by claims or defenses buyers might have against sellers, and that buyers are still obligated to make their instalment payments.

For upward of 20 years, this underlying dispute has existed and waxed more intense. The issue has been tested in courts, with a number of courts deciding in consumer cases that waiver of defense clauses included in instalment contracts signed by buyers were not effective as contrary to public policy. Legislatures took up the issue and in a number of States enacted statutes prohibiting the use of negotiable notes in consumer sale transactions or limiting or prohibiting waiver of defense clauses in retail instalment sale contracts, and sometimes both. These statutes varied in terms of dollar amounts involved and types of transactions to which they applied.

Recognizing the existence of the controversy and that the underlying issue had not been finally resolved, the 1968 Text by Section 2.403 prohibited the taking of negotiable notes in consumer sale and lease transactions and by Section 2.404 provided alternative provisions relating to the effectiveness of waiver of defense clauses. Of the six enacting States covered by Report No.1, all enacted the prohibition of negotiable notes in Section 2.403 of the 1968 Text, two States prohibited the waiver of defense clauses, one State took no action on the subject, and three States elected to permit these clauses with restrictions.

In Section 3.307 of this Act, the prohibition of the use of negotiable instruments in consumer sales and leases is continued and strengthened. In Section 3.404, the consumer position is substantially adopted by deleting entirely Alternative B of the 1968 Text and by strengthening the 1968 Alternative A provisions prohibiting waiver of defense clauses. It is believed that on this issue consumers have the stronger case. However, this decision reinforces the need to retain the proposed rate ceilings, since the findings of the National Commission on Consumer Finance show that restrictions on holders' rights tend to increase finance charges and reduce the availability of credit.

In more recent years, another issue has developed which is different from but closely related to transfers of sale paper. That issue is the further contention by consumers that even if the transaction is· exclusively in the form of a loan but if proceeds of the loan are used to purchase goods or services, at least under certain circumstances, lenders should be subject to defenses of buyers against sellers. Banks, consumer finance companies and other lenders have objected to this type of provision even more strenuously than to provisions prohibiting waiver of defense clauses in assigned instalment sale contracts.

Notwithstanding objections of this kind by lenders, a number of legislatures have enacted provisions of this type. Section 3.405 of this Act includes such a provision, but is limited to certain prescribed situations where the relationship between the lender and the seller is close and the lender either acts in a manner or receives benefits of a kind that ties the lender closely not only to the seller but to the particular sale transaction.

Inevitably, the argument and debate with respect to these two issues led to argument and debate of the same underlying issues when goods or services are purchased with the aid of a three party credit card issued by a bank or other financing agency. Again banks have argued strenuously that in issuing credit cards and making payments to sellers upon use of the cards by the cardholders, the bank knows nothing about the sellers or the sale transactions and should be completely insulated in its rights against its cardholders from any claims or defenses the cardholder buyers might have against the sellers. Banks have further argued that making them in any way subject to claims or defenses cardholders might have against sellers could seriously interfere with the acceptability and convenience of credit cards (and, by extension, the development of the electronic funds transfer system), because not only would banks be more hesitant to issue cards but sellers would also be more reluctant to make sales in reliance on credit cards.

On the other hand, consumer advocates have contended that banks issuing credit cards are better equipped to police sellers than are consumers, banks may in agreements with sellers obtain charge back agreements from them if merchandise risks or claims arise, and in any event, as between cardholders and card issuing banks, merchandise risks of this kind should be borne by the banks.

On this third and latest issue, argument and debate again have been intense. However, in California and in the Fair Credit Billing Act passed by the Senate as S.2101 in the summer of 1973, a compromise solution was worked out which bids fair to provide a resolution of this third issue. The compromise solution is that the card issuing bank is subject to any claims or defenses the cardholder may have against the seller only if (1) the customer makes a good faith attempt to resolve a disagreement with the seller, (2) the credit card transaction involves more than $50, and (3) both the residence of the cardholder and the place where the sale or lease occurred are [in the same State or) within 100 miles of each other.

If the card-issuing bank is subject to claims or defenses under this solution, it may have to rely upon rights of charge-back against the seller.

The rationale of this compromise as to amount is that in smaller transactions of $50 or less, the credit card should be looked upon as basically the equivalent of cash and the transaction should have all the finality of a cash transaction.

The rationale for the geographic distinction is that the normal area for use of a credit card as a credit instrument is reasonably proximate to the residence of the cardholder and consequently card-issuing banks should be subject to claims and defenses of the cardholder against the seller only if a transaction and the seller are in this not too large area. A further reason is that any policing of merchants by banks could not reasonably be expected for unlimited geographic distances. Consequently, if and to the extent a cardholder uses his credit card in

another State or at a location some distance from his residence, sellers, card-issuing banks and others in the credit card mechanism should not have to worry about credit cards giving to cardholders undue advantages in merchandise disputes by being able to withhold payments from the banks and in turn forcing banks to charge back items to sellers requiring sellers to seek collection from cardholders in distant places.

Section 3.403 of this Act adopts this basic compromise solution. Further, in each of Sections 3.403, 3.404, and 3.405 the extent to· which card-issuing banks, lenders and finance companies may be subject to claims and defenses of buyers against sellers is limited to the amount outstanding for the particular transaction at the time the bank or other lender first receives notice of the dispute. Suggestions that card-issuing banks and other lenders should be responsible for the original amount of the transaction and even for product liability that might arise out of the transaction are rejected as neither feasible nor reasonable.

**(2) Territorial Reach of Protection**

Additional protection is afforded to residents of the enacting State with respect to mail order loans by applying the limitations on finance charges and related provisions to these transactions and giving the Administrator power over them as though the loans were entered into in the enacting State. Also prohibitions of other types of agreements limiting the jurisdiction of the enacting state have been added. See Section 1.201.

**(3) Vendor's Single Interest Insurance**

The conditions under which a creditor may make an additional charge for vendor's single interest insurance have been more clearly specified and tightened. See Section 2.501.

**(4) Notice to Consumers of Precautions and Rights**

In certain types of closed-end credit transactions, the creditor is required to furnish the consumer with a copy of the basic contract documents and to advise the consumer of this right, of the wisdom of not signing without reading, and of the right to prepay and possible right to receive a refund. See Section 3.203.

**(5) Receipts, Statements and Evidence of Payment**

Provisions that consumers are entitled to receipts, statements as to dates and amounts of payments, and evidence of payment in various situations have been added. See Section 3.206.

**(6) Notice to Co-Signers**

Provisions requiring notice to co-signers and other sureties as to the nature of their obligations have been inserted in accordance with NCCF recommendations. See Section 3.208.

**(7) Restrictions on Security and its Enforcement**

A potential loophole in the restrictions on security interests that might allow a creditor to take security in a wife's goods for the husband's debt has been eliminated by extending the

restriction to property generally rather than only to property of the consumer. See Section 3.301. In addition, enforcement of security interests in property, exempt from execution under a judgment, to secure loans has been restricted. See Section 5.116.

### (8) Revocable Deductions from Earnings

Better to assure that an authorized deduction from earnings is revocable both in law and in fact, provisions have been added to give the consumer notice of the revocable nature of any authorization of deductions. See Section 3.305.

### (9) Referral Sales and Leases

Restrictions on referral sales and leases have been tightened so as to cover both referral arrangements that are not specifically bargained for in a contract sense and arrangements financed by other than the seller or lessor. In addition to the sanction provided in the section dealing with referrals, a private right of action by the consumer for violation of the prohibition is created better to deter this conduct. See Sections 3.309 and 5.201.

### (10) Home Solicitation Sales

The provisions with respect to home solicitation sales have been widened to cover transactions at any residence, not just the residence of the buyer, and have been tightened to prevent evasion by the seller or lessor arranging to have someone else do the financing or by too free use of the emergency exception, and by assuring the buyer a copy of the "buyer's right to cancel" at the time he signs the agreement. Further protection to the consumer is also afforded by prohibition of any cancellation fee and clarification of the right to cancel even though goods sold have received the ordinary use or consumption contemplated by the transaction. Provisions are added that compliance with Federal Trade Commission notice requirements meets U3C requirements in this regard. See Article 3, Part 5.

### (11) Refunds of Separate Charges for Insurance

To restrict the creditor's right to withhold a refund until the maturity of a contract, provisions have been added entitling a consumer to a refund at his option rather than a credit in the event of a required rebate of any separate charge for insurance. See Section 4.108.

### (12) Deficiency Judgments

Following the NCCF recommendation, restrictions on deficiency judgments have been increased to apply to transactions up to $1,750 rather than $1,000 and have been widened to apply to loans in which the lender is subject to claims and defenses arising from sales as well as to consumer credit sales. See Section 5.103.

### (13) Garnishment

Also following a~ NCCF recommendation, provisions for special court relief from

garnishments after judgment on normally non-exempt earnings have been lidded. See Section 5.105.

### (14) Unconscionability

Provisions for court determination of unconscionability in an action by the consumer have been widened to cover, in addition to a consumer credit transaction, (a) a transaction that a consumer is led to believe will give rise to a consumer credit transaction so that, for example, a seller cannot bind the consumer to a short term sale contract payable in a lump sum on the assurance he will secure financing, and then inform the consumer that financing is unavailable and keep the down payment or goods traded upon the consumer's default, (b) inducing a transaction by unconscionable conduct; and (c) unconscionable collection practices. In addition, factors that may be considered in determining unconscionability are spelled out and a provision allowing recovery of attorney's fees is included. See Section 5.108.

### (15) Default

Provisions have been added that restrict the unfettered right of the creditor to determine what constitutes a default; that require as a condition to acceleration of debt or enforcement of security interest that the consumer be given notice of his right within a reasonable time to cure a default consisting of the failure to make a required payment; that further clarify the conditions under which self-help repossession is permissible; that control venue in suits against a consumer to collect; that specify what a creditor's petition or complaint must contain to establish his claim; and that provide for relief from default judgments for cause, including sewer service. See Sections 5.109 through 5.115.

### (16) Consumers' Remedies

The consumer is given a right of action to recover actual damages and a penalty for the violation of all provisions of the Act which do not have an express or implicit sanction, and even for some provisions that do, better to guard against *in terrorem* uses of prohibited agreements and practices and better to assure compliance with the law. Although the question of the availability of a class action in general is left to other law, the right to recover a penalty is expressly made not enforceable in a class action. In addition, recovery of a penalty is authorized in cases of excess charges or failure to refund within a reasonable time after demand (and a presumption as to reasonable time is created), and the amount of the penalty is not tied to the excess charge, which might permit only a low recovery and therefore establish an inadequate incentive when the excess charge is small. Finally, the voidness penalty for making supervised loans without a necessary license has been deleted as unworkable, and the allowance of attorney's fees has been liberalized and clarified. See Section 5.201.

### (17) Administrator's Powers

The rule making power of the Administrator has been expanded; his investigatory powers are increased; his ability to use the device of an assurance of discontinuance has been clarified; his ability to obtain injunctions or other appropriate relief has been clarified; and his powers to

sue on behalf of consumers have been clarified. See Sections 6.104, 6.106, 6.109, 6.110, 6.111, 6.112, and 6.113.

### Alternative Methods of Computing Finance Charges-Open-End Credit

Another issue that has caused concern in recent years is the appropriate method for computing finance charges on open-end credit. This issue is a product of evolutionary development of practices during ~the last 25 or more years and of the failure of protagonists for different views to recognize or openly discuss the basic questions involved. This Act deals with this problem in realistic terms.

Four general approaches in imposing finance charges have been used although there have been many variants particularly with regard to the average daily balance method.
The method used by a number of large retailers when they first established revolving accounts was the "ending balance method." The finance charge was computed on the balance in the account at the close of the monthly billing cycle (the "ending balance"). This balance reflected all amounts owed through the date the balance was determined and took into account all purchases and payments through that date.

The previous balance method is the one used by most retailers and until the advent of the modern computer was by far the prevailing method. The finance charge is computed on the same balance as under the ending balance method but the billing of the charge is deferred until the close of the next billing cycle for that customer. At the close of the cycle when the charge is billed, the balance is the "previous balance," that is the previous month's ending balance brought forward as the beginning balance of the current cycle. The billing of the finance charge is deferred to give the customer the opportunity to avoid a finance charge by paying the full amount before the next cycle's billing date. If he makes only a partial payment the finance charge is computed on the full amount of the previous balance. It is this feature which has chagrined consumer advocates who have felt that the finance charge should reflect payments made during the cycle for which the bill was received. The deferral feature of the previous balance method was designed to accommodate customers who wanted the option of using their revolving accounts like the formerly common 30-day charge accounts. Merchants found that the lack of opportunity to avoid finance charges made the ending balance system unattractive both to themselves and to consumers and led many merchants to change from the ending balance method to the previous balance method.

The adjusted balance method provides for the calculation of the finance charge on an amount equal to the previous balance minus all payments and credits during the current cycle but excludes any purchases made during the current cycle. The primary user of this method is a major retailer who did not offer revolving credit until many years after these accounts had become popular.

The average daily balance method requires computer technology and could not be utilized until recent years. The cost of this technology makes this method unavailable to many credit grantors. Under this method the finance charge is computed on the sum of the balances outstanding each day during the billing cycle, divided by the number of days in the cycle.

Purchases mayor may not be included in the daily balance from the day they are made and there mayor may not be an optional feature permitting the customer to avoid finance charges by full payment.

Against this evolutionary background in the retail area, another important factor-the bank credit card-has become involved in the controversy. A cardinal principle has been that if and when a bank lends money, it is entitled to a return or interest on the money loaned from the date of the loan until the loan is paid. In various ways this principle has been followed in both closed-end and open-end credit, but one major exception has developed. When banks moved into the credit card field in the 1960's, they recognized that if credit cards were to be used in the purchase of goods and services, banks would be competing with retailers already extending credit for these same purposes. Consequently, to develop a credit card program that would be competitive with retailers, banks modeled their operations closely on revolving credit techniques of retailers and contrary to the usual principle of banking, provided for free periods to cardholders either under the previous balance or adjusted balance methods. Hence, in bank credit card operations under which banks pay to retailers the dollar amount, less a "merchant discount," of credit card purchases within a few days from the date of purchase and hence at that time advance actual funds for the account of cardholders, but make no charge to cardholders for the credit advanced for the same 30-60 day free period allowed by retailers, the basic principle of charging interest for the full period on which funds are outstanding has been abandoned, the loss of interest being compensated for by the merchant discount charged the retailer.

Against this background, both retailers and banks have vehemently contended that the previous balance method of computing finance charges is justified, legitimate, and proper and should not be outlawed. On the other hand, consumer advocates have urged the mandatory imposition of the adjusted balance method. In support of this position, they contend that it is unfair to them if they have to pay finance charges computed on balances existing at the beginning of a cycle, if these balances have been reduced by payment::; made during the cycle. Based upon varying possible fact situations, consumer advocates cite "horror stories" of very high percentage rates in finance charges (computed by the actuarial method) that may result if the previous balance method is utilized. In advancing these arguments, however, these advocates never suggest that if the previous balance is reduced by payments made during the cycle, it should also be increased by additional purchases made and charged to the account during the cycle. In other words, these advocates are happy to have, in both retail and bank credit card operations, the continuance of a 30-60 day free period but make the essentially one~sided argument that if the previous balance method is used, it should be reduced by payments made during the cycle.

Computation of finance charges on the average daily balances outstanding in the account of a customer during the cycle for which a bill is rendered is a legitimate, proper method. This Act authorizes the use of this method in Section 2,202(2) (a). However, since the previous balance vs. the adjusted balance argument continues, both in the Congress in its consideration of S.2101 and throughout the country in state legislatures, Section 2.202(2) (b) of this Act provides alternative language for each of the previous balance and adjusted balance methods to permit legislatures to adopt whichever form they approve. Although a strenuous effort was made in the consideration the use of the previous balance method in the Senate and, as S.2101 now stands,

the pre method will continue to be permissible.

### Changes in Provisions for Deferrals and Rebates Sections 2.503 and 2.510

A widespread if not the prevailing practice in the credit industry is to compute both deferrals and rebates by the sum of the balances method. This practice permits single computations in precomputed transactions involving both one or more deferrals and a subsequent rebate. Subsection (6) of Section 3.210 of the 1968 Text in requiring separate calculations of deferrals and rebates casts doubt on this industry practice.

The revisions of Sections 2.503 and 2.510 of this Act are designed to provide affirmatively for this industry practice which simplifies computations and not only does not prejudice consumers but also reduces their costs. A further revision of Section 2.510 requires the use of the actuarial method of calculating refunds upon prepayment of transactions involving a large number of payments when the sum of the balances method produces higher costs to consumers.

### Federal Preemption of Disclosure

Increasingly in the last decade the Congress has interested itself in various aspects of consumer credit. Particularly in the case of the Consumer Credit Protection Act (of which the Truth in Lending Act is a part) enacted in 1968 and in amendments of that Act enacted since 1968, Congress has moved into a major area of consumer credit: disclosures to be made to consumers. In that Act the Congress took pains to recognize that other areas of consumer credit continued to be subject to state law and, even in the case of disclosure, made provision for determinations by the Board of Governors of the Federal Reserve System that state law was sufficiently identical with the federal Act to warrant States applying for and obtaining exemptions from the application of the federal Act. Under these provisions, four or more States have applied for and obtained exemptions.

However, States seeking exemption found that state laws with respect to disclosure must be identical not only to the Truth in Lending Act but also to Regulation Z issued under that Act.

Entirely aside from these efforts on the part of the Congress and certain States to preserve States' rights and some measure of state control over consumer credit, actual experience from 1968 to the present time has demonstrated that in substantially all cases, creditors engaging in consumer credit look to the federal law and Regulation Z as the controlling law in the area of disclosure. Creditors have found that any additional provisions of state law on the subject constitute a nuisance in attempts to comply with federal law and frequently add confusion in these efforts to comply. Further, in those States obtaining exemptions from the Federal Reserve Board, state officials charged with the duty of enforcing state statutes and regulations designed to parallel the federal Act and Regulation Z find the task of keeping state law parallel onerous and troublesome.

Against this background, this Act evidences the conclusion that the Congress has

preempted the field of disclosure and any attempt of States to remain in the field by enacting statutes and regulations of their own cause substantially more harm than good. Consequently, this Act contains few substantive disclosure provisions and in Section 3.201 provides simply that a person upon whom the federal Act imposes duties or obligations shall make or give to the consumer the. disclosures required of him by the federal Act and in all respects comply with that Act. Section 3.201 allows the Administrator to enforce the disclosure provisions of the Truth in Lending Act and Regulation Z as state law. Other tracking sections of this Act include Sections 1.102 (2); 1.202(5); 1.301(1); 1.301(33); 1.302; 2.201(4); 2.401 (4); 2.501(1); 2.501(2); 3.209; 3.501; 5.107; 5.203; 5.302; and 6.102(3).

In adopting this basic approach the National Conference recognizes that in some States problems of delegation of legislative power may arise. However, in the ever increasing complexity of areas in which both the federal government and individual States have enacted legislation, solutions of this type are increasingly common and have been sustained. See, *e. g.,* incorporation of definition of "taxable income": by reference to Federal Internal Revenue Code, approved in City National Bank of Clinton v. Iowa State Tax Commission, 251 Iowa 603, 102 N.W.2d 381 (1960); incorporation by state legislatures of Federal Insurance Contributions Act for coverage of state and local governmental employees under Social Security; enactment of state War Emergency Acts as enforcement measures in aid of federal legislation creating the Office of Price Administration and providing for the regulation of prices during war time, approved in People v. Mailman, 182 Misc. 870 (1944); affirmed on appeal 293 N.Y. 887 (1944); incorporation of state law in Federal Assimilative Crimes Act of 1948, 17 U.S.C. § 13, approved in United States v. Sharpnack (1958) 78 S.Ct. 291, 355 U.S. 286, 2 L.Ed.2d 282. In any event, whatever difficulties may be involved, the course adopted in this Act and the abandonment of any effort to duplicate disclosure requirements by substantive provisions seem preferable to the alternative of attempting to establish and maintain parallel federal and state legislation on the subject.

**Changes Resulting from Special Problems of Particular Types of Creditors**

In a few instances particular types of creditors presented special problems which they considered deserved clarification of or changes from the 1968 Text. In the instances set forth below some adaptations to solve these special problems appear to be justified.

At the request of credit unions, subsection (6) of Section 1.202 has been added so that in any State enacting the U3C it will be optional with the enacting State whether ceilings on rates or limits on loan maturities provided in the U3C will be applicable to credit unions or whether these rates and maturities will be governed by other laws of the State or the United States enacted specifically for credit unions.

A widespread practice of some oil companies operating directly or through franchised filling stations is to avoid the usual revolving credit feature in their credit card agreements which gives the customer the option of paying in full or in instalments. Instead, these companies customarily require full payment of the amount of each billing statement but provide for and assess charges if payments are delinquent. Section 2.601 makes clear that transactions of this kind are not consumer credit transactions governed by the U3C; however, to make equally clear

that consumer credit transactions are involved if charges for delinquency are imposed but delinquencies are ignored in practice; the definitions of "finance charge" in Section 1.301(20) and "open-end credit" in Section 1.301 (28) have been revised or added.

In many States special statutes have been passed providing for insurance premium financing. To provide for the particular needs of this type of financing a definition of an "insurance premium loan" and some substantive provisions have been added and appear in this Act. See Sections 1.301(22), 2.302(2), 2.401 (6), 3.207, 5.110(3) and 5.111(4). These provisions together with other general provisions of the U3C make these special statutes unnecessary and permit their repeal.

In the States that have enacted the U3C and in other States that have considered it, supervised financial organizations, *e. g.*, banks, thrift institutions and the like, have argued that they are currently supervised by agencies to whom various types of fees and charges must be paid and that they should not be required to pay the same fees as other creditors to finance the administration of the U3C. This Act reflects the belief that all creditors extending consumer credit in a State enacting the U3C are governed by the U3C and should share in financing the cost of its administration, but, responding to these arguments of supervised financial organizations, a new subsection (4) of Section 6.203 reduces by 50% the standard volume fees payable by these organizations.

**Refinements and Clarifications**

In addition to the above changes and additions, this Act includes many clarifications and refinements and much simplification and improvement of language. Not the least of these has been the reorganization of Articles 2 and 3 to eliminate much of the duplication in these two Articles in the 1968 Text. Although these two Articles have been substantially shortened by the changes, no important distinctions between sales credit and loans have been ignored; rather, they have been clarified, particularly in the case of credit cards. Sections referring specifically to credit cards include: Sections 1.301(12), (15), (17), (24), (25), (28), and (39) and 3.403.

# UNIFORM CONSUMER CREDIT CODE

## 1974 ACT

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

## COMMENT

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

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

## Article 1

## GENERAL PROVISIONS AND DEFINITIONS

Part 1

## SHORT TITLE, CONSTRUCTION, GENERAL PROVISIONS

Section


Part 2

## SCOPE AND JURISDICTION



Part 3

## DEFINITIONS

Part 3

**LIMITATIONS ON AGREEMENTS AND PRACTICES**



Part 4

**LIMITATIONS ON CONSUMERS' LIABILITIES**



Part 5

**HOME SOLICITATION SALES**



**Article 4**

**INSURANCE**

Part 1

**INSURANCE IN GENERAL**



Part 2

**CONSUMER CREDIT INSURANCE**



Part 3

**PROPERTY AND LIABILITY INSURANCE**



**Article 5**

**REMEDIES AND PENALTIES**

Part 1

**LIMITATIONS ON CREDITORS' REMEDIES**

Part 2

## NOTIFICATION AND FEES



Part 3

## COUNCIL OF ADVISORS ON CONSUMER CREDIT



Part 4

## ADMINISTRATIVE PROCEDURE AND JUDICIAL REVIEW

**Article 7**

**[Reserved for Future Use]**

**Article 8**

**[Reserved for Future Use]**

**Article 9**

**EFFECTIVE DATE AND REPEALER**



ARTICLE 1

**GENERAL PROVISIONS AND DEFINITIONS**

Part 1

**SHORT TITLE, CONSTRUCTION, GENERAL PROVISIONS**

Section

Part 2

## SCOPE AND JURISDICTION

1.201. Territorial Application.
1.202. Exclusions.
1.203. Jurisdiction [and Service of Process].

Part 3

## DEFINITIONS

1.301. General Definitions.

(1) "Actuarial method".
(2) "Administrator".
(3) "Agreement".
(4) "Agricultural purpose".
(5) "Amount financed".
(6) "Billing cycle".
(7) "Card issuer".
(8) "Cardholder".
(9) "Cash price".
(10) "Conspicuous".
(11) "Consumer".
(12) "Consumer credit sale".
(13) "Consumer credit transaction".
(14) "Consumer lease".
(15) "Consumer loan".
(16) "Credit".
(17) "Credit card".
(18) "Creditor".
(19) "Earnings".
(20) "Finance charge".
(21) "Goods".
(22) "Insurance premium loan".
(23) "Lender".
(24) "Lender credit card".
(25) "Loan".
(26) "Merchandise certificate".
(27) "Official fees".
(28) "Open-end credit".
(29) "Organization".
(30) "Payable in instalments".
(31) "Person".

(32) "Person related to".
(33) "Precomputed consumer credit transaction".
(34) "Presumed".
(35) "Sale of goods".
(36) "Sale of an interest in land".
(37) "Sale of services".
(38) "Seller".
(39) "Seller credit card".
(40) "Services".
(41) "Supervised financial organization".
(42) "Supervised lender".
(43) "Supervised loan".

1.302. Definition: "Federal Truth in Lending Act".
1.303. Other Defined Terms in Act.

# ARTICLE 1

PART 1

## SHORT TITLE, CONSTRUCTION, GENERAL PROVISIONS

### § 1.101. [Short Title]

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

### § 1.102. [Purposes; Rules of Construction]

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

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

(a) to simplify, clarify, and modernize the law governing consumer credit and usury;

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

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

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

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

(f) to conform the regulation of disclosure in consumer credit transactions to the Federal Truth in Lending Act; and

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

jurisdictions.

(3) A reference to a requirement imposed by this Act includes reference to a related rule of the Administrator adopted pursuant to this Act.

**COMMENT**

Under Section 3.201, a creditor must make disclosure in consumer credit sales and consumer loans in accordance with the Federal Truth in Lending Act, defined in Section 1.302 as including Regulation Z. If a creditor fails to comply, he has violated this Act as well as the Federal Act, and the Administrator may proceed against him pursuant to Section 6.104(2).

**§ 1.103. [Supplementary General Principles of Law Applicable]**

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

**COMMENT**

The Uniform Commercial Code is referred to in the Comments as UCC.

Many transactions are subject both to this Act and to other bodies of law, particularly the UCC. In the event of inconsistency between this Act and the UCC the provisions of this Act control. See, *e.g.,* UCC Sections 9-201 and 9-203. In other cases the provisions of this Act are supplemented by the UCC and other principles. In general such principles have not been repeated in this Act. There are exceptions, *e.g.,* the duty of good faith in UCC Section 1-203 is repeated and defined in Section 1.110.

See Note following Section 9.103 as to UCC amendments possibly needed.

**§ 1.104. [Construction Against Implicit Repeal]**

This Act being a general act intended as a unified coverage of its subject matter, no part of it shall be construed to be impliedly repealed by subsequent legislation if that construction can

reasonably be avoided.

**§ 1.105. [Severability]**

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

**§ 1.106. [Adjustment of Dollar Amounts]**

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

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

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

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

(3) If the Index is revised, the percentage of change pursuant to this section shall be

calculated on the basis of the revised Index. If a revision of the Index changes the Reference Base Index, a revised Reference Base Index shall be determined by multiplying the Reference Base Index then applicable by the rebasing factor furnished by the Bureau of Labor Statistics. If the Index is superseded, the Index referred to in this section is the one represented by the Bureau of Labor Statistics as reflecting most accurately changes in the purchasing power of the dollar for consumers.

(4) The Administrator shall adopt a rule announcing

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

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

(5) A person does not violate this Act with respect to a transaction otherwise complying with this Act if he relies on dollar amounts either determined according to subsection (2) or appearing in the last rule of the Administrator announcing the then current dollar amounts.

**COMMENT**

1. Under this section the dollar amounts designated as subject to change will automatically change on July 1 of each even-numbered year if the change in the Consumer Price Index is great enough. Assume that a state enacts the Uniform Consumer Credit Code and establishes the effective date as July 1, 1974. In this case the Consumer Price Index for December, 1973, is the Reference Base Index. For ease of illustration, assume that the Index is 100. The $300 figure appearing in Section 2.201(2)(a)(i) will be used as an illustrative dollar amount.

CASE 1: The Index for December, 1975 is 107. The change from the Reference Base Index of 100 is an increase of 7%. Since the change is less than 10% no change in dollar amounts occurs.

CASE 2: The Index for December, 1977 is 112. The change from the Reference Base Index of 100 is an increase of 12%. Since this is more than 10%, a change occurs. The portion of the 12% in excess of 10% is disregarded; hence, an increase of 10% is

indicated. 10% of $300, is $30. The dollar amount is $330, effective July 1, 1978.

CASE 3: The Index for December, 1979 is 118. The change from the Reference Base Index of 100 is an increase of 18%. The portion of 18% in excess of 10% is disregarded; hence, an increase of 10% is indicated. However, the $300 amount changed to $330 in 1978 (see CASE 2). Since the amount currently in effect ($330) is still the correct amount under this section, no change occurs.

CASE 4: The Index for December, 1981 is 122. The change from the Reference Base Index of 100 is an increase of 22%. The portion of 22% in excess of a multiple of 10% (here 20l) is disregarded and a 20% increase is indicated. 20% of $300 is $60. The dollar amount is $360, effective July 1, 1982.

CASE 5: The Index for December, 1983 is 117. The change from the Reference Base Index of 100 is an increase of 17%. The portion of 17% in excess of 10% is disregarded and a 10% increase is indicated. 10% of $300 is $30. The dollar amount is $330, effective July 1, 1984, a decrease from the $360 amount in effect since 1982 (see CASE 4).

CASE 6: In 1985, the Bureau of Labor Statistics (BLS) revises the Index, changing coverage components and selecting a new base period. If only the coverage or components were changed, the revised Index should be used for subsequent calculations. However, if a new base period is selected (1983-84 = 100), an equivalent on the scale of the revised Index must be assigned to the Reference Base Index (December, 1973). The rebasing factor supplied by the BLS is .6454545. Therefore, the Revised Reference Base Index is (100) X (.6454545) = 64.5.

A comparison of the revised Index for December 1985 (130.4) with the Revised Reference Base Index (64.5) shows that the change from the Revised Reference Base Index is an increase of 60.3%.

(103.4-64.5)/64.5 = .603 = 60.3%

Under subsection (2) 60.3% becomes 60%, and an increase of that percentage is indicated. The dollar amount is $480, effective July 1, 1986.

2. The provisions for adjustment of dollar amounts never permit the maximum rate of finance charge to rise above 36%. To reflect the needs of high-risk consumers for greater amounts of credit as a result of rising prices, the maximum rate permitted is extended to larger amounts of credit. Were this not done automatically, inflation would push creditors' operating costs against a fixed rate ceiling, gradually lessening their ability to provide small amounts of credit to high-risk consumers.

The change in maximum rates permitted by a 10% increase in the dollar amounts is shown below for various amounts financed payable in 12 monthly instalments.

| Amount Financed | Maximum rates prior to adjustment | Maximum rates after 10% increase in dollar amounts |
|---|---|---|
| $100 | 36.00% | 36.00% |
| 300 | 36.00 | 36.00 |
| 500 | 33.02 | 33.75 |
| 1000 | 28.05 | 28.64 |
| 1500 | 25.10 | 25.80 |
| 3000 | 20.73 | 21.22 |
| 5000 | 18.58 | 18.92 |

3. Subsection (1) specifies the Index for the December preceding the year in which the Act is to take effect as the Reference Base Index. Hence, changes in the Index that have occurred since promulgation of this Act but before the December preceding the effective date will not require immediate changes in dollar amounts from those specified in the U3C upon enactment.

**§ 1.107. [Waiver; Agreement to Forego Rights; Settlement of Claims]**

(1) Except as otherwise permitted in this Act, a consumer may waive or agree to forego rights or benefits under this Act only in settlement of a bona fide dispute.

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

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

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

**COMMENT**

Unlike UCC Section 1-102(3) which broadly permits variation by agreement, this Act

starts from the premise that a consumer may not in general waive or agree to forego rights or benefits under this Act. Compare UCC Section 9-501(3). If not specifically provided for in the Act, waiver or agreement to forego must be part of a settlement, and settlements are subject to review as provided for in this section.

**§ 1.108. [Effect of Act on Powers of Organizations]**

(1) This Act prescribes maximum charges for all creditors, except lessors and those excluded (Section 1.202), extending credit in consumer credit transactions (subsection (13) of Section 1.301), and displaces existing limitations on the powers of those creditors based on maximum charges.

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

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

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

(a) limitations on powers of supervised financial organizations (subsection (41) of Section 1.301) with respect to the amount of a loan to a single borrower, the ratio of a loan to the value of collateral, the duration of a loan secured by an interest in land, or other similar restrictions designed to protect deposits, or

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

## COMMENT

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

2. This section states the policy of this Act regarding the displacement of laws regulating suppliers of consumer credit and should be read as a guide for the preparation of the repealer provisions of Section 9.103, along with the explanatory note following that section.

3. This Act displaces existing usury laws; in addition, subsection (1) displaces existing limitations on maximum charges for all suppliers of consumer credit except lessors and those excluded under Section 1.202. In other respects, this Act differentiates among creditors depending on their status as either being or not being supervised financial organizations as defined in Section 1.301(41), and among supervised financial organizations depending on whether they are (1) commercial or industrial banks or trust companies, or (2) thrift institutions such as credit unions, savings banks and savings and loan associations whether mutual or not.

4. Subsection (2) frees commercial and industrial banks and trust companies and all creditors other than thrift institutions from existing limitations on their powers based solely on the amount or duration of credit, may extend, such as the typical $5,000 or $7,500 limit on the amount, and the typical 36-month or 60-month limit on the maturity, of a personal loan by a commercial or industrial bank or trust company.

5. Subsection (3) retains all existing limitations on powers of thrift institutions, other than those based on maximum charges, on the theory that those limitations may be required for the protection of their depositors or shareholders.

6. Except for limitations based on maximum charges, and limitations based solely on amount or duration of credit, subsection (4)(a) retains as to all supervised financial organizations existing limitations and restrictions of the kinds enumerated designed to protect deposits such as the typical limitation to 10% of capital and surplus funds on bank loans to a single borrower. Subject to the same exceptions, subsection (4)(b) retains as to all organizations existing limitations on the powers they are authorized by law to exercise.

### § 1.109. [Transactions Subject to Act by Agreement]

Parties to a credit transaction or modification thereof that is not a consumer credit transaction (subsection (13) of Section 1.301) may agree in a writing signed by them that the transaction is subject to the provisions of this Act applying to consumer credit transactions. If the parties so agree the transaction is a consumer credit transaction for the purposes of this Act.

## COMMENT

This section permits creditors, by inserting an appropriate clause in a contract, to be certain that the transaction is a consumer credit transaction for the purposes of this Act.

### § 1.110. [Obligation of Good Faith]

(1) Every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement.

(2) "Good faith" means honesty in fact in the conduct or transaction concerned.

## COMMENT

This section is derived from UCC Sections 1-201(19) and 1-203.

# PART 2

# SCOPE AND JURISDICTION

### § 1.201. [Territorial Application]

(1) Except as otherwise provided in this section, this Act applies to a consumer credit transaction entered into in this State. For the purposes of this Act, a consumer credit transaction is entered into in this State if:

(a) pursuant to other than open-end credit, either a signed writing evidencing the obligation or offer of the consumer is received by the creditor in this State, or the creditor induces the consumer who is a resident of this State to enter into the transaction by face-to-face solicitation in this State; or

(b) pursuant to open-end credit, either the consumer's communication or his indication of intention to establish the open-end credit arrangement is received by the creditor in this State or, if no communication or indication of intention is given by the consumer before the

first transaction, the creditor's communication notifying the consumer of the privilege of using the arrangement is mailed in this State.

(2) With respect to a consumer loan to which this Act does not otherwise apply, if a consumer who is a resident of this State, pursuant to solicitation in this State, sends a signed writing evidencing the obligation or offer of the consumer to a creditor in another state and receives the cash proceeds of the loan in this State:

(a) the creditor may not contract for or receive charges exceeding those permitted by the Article on Finance Charges and Related Provisions (Article 2); and

(b) the provisions on Powers and Functions of Administrator (Part 1) of the Article on Administration (Article 6) apply as though the loan were entered into in this State.

(3) The Part on Limitations on Creditors' Remedies (Part 1) of the Article on Remedies and Penalties (Article 5) applies to actions or other proceedings brought in this State to enforce rights arising from consumer credit transactions or extortionate extensions of credit, wherever entered into.

(4) Except as provided in subsection (2), a consumer credit transaction to which this Act does not apply entered into with a person who is a resident of this State at the time of the transaction is valid and enforceable in this State to the extent that it is valid and enforceable under the laws of another jurisdiction, but:

(a) a creditor may not collect through actions or other proceedings in this State an amount exceeding the total amount permitted if the Article on Finance Charges and Related Provisions (Article 2) were applicable; and

(b) a creditor may not enforce rights against the consumer in this State with respect to the provisions of agreements that violate the provisions on Limitations on Agreements and

Practices (Part 3) and Limitations on Consumers' Liabilities (Part 4) of the Article on Regulation of Agreements and Practices (Article 3).

(5) Except as provided in subsections (2), (3), and (4), a consumer credit transaction entered into in another jurisdiction is valid and enforceable in this State according to its terms to the extent that it is valid and enforceable under the laws of the other jurisdiction.

(6) For the purposes of this Act, the residence of a consumer is the address given by him as his residence in a writing signed by him in connection with a consumer credit transaction until he notifies the creditor of a different address as his residence, and is then the different address.

(7) Notwithstanding other provisions of this section:

(a) except as provided in subsection (3), this Act does not apply if the consumer is not a resident of this State at the time of a consumer credit transaction and the parties have agreed that the law of his residence applies; and

(b) this Act applies if the consumer is a resident of this State at the time of a consumer credit transaction and the parties have agreed that the law of his residence applies.

(8) Each of the following agreements or provisions of an agreement by a consumer who is a resident of this State at the time of a consumer credit transaction is invalid with respect to the transaction:

(a) that the law of another jurisdiction apply;

(b) that the consumer consents to be subject to the process of another jurisdiction;

(c) that the consumer appoints an agent to receive service of process;

(d) that fixes venue; and

(e) that the consumer consents to the jurisdiction of the court that does not otherwise have jurisdiction.

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

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

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

**COMMENT**

1. This section enables the enacting State to apply this Act for the protection of its own consumer residents in multi-state transactions to the extent consistent with the need for workable operating procedures on the part of creditors. The territorial applicability of the Act varies with the kind of protection safeguard involved. The major substantive protective provisions in this Act are those on rate ceilings (Parts 2 and 4 of Article 2), disclosure (Part 2 of Article 3), limitations on agreements and practices (Part 3 of Article 3), home solicitation sales (Part 5 of Article 3), limitations on consumers' liabilities (Part 4 of Article 3), and limitations on creditors' remedies (Part 1 of Article 5). Except for the disclosure provisions, this section allows the enacting State to apply all of these protective provisions to its own consumer residents when enforcement actions are brought against them in the enacting State.

In the case of a consumer who was a resident when the agreement was made, subsection (4) prohibits the creditor from collecting through actions total amounts including charges to the extent that the charges exceed those permitted by Article 2 and from enforcing rights in violation of the provisions on limitations on agreements and practices of Part 3 of Article 3 and limitations on consumers' liabilities of Part 4 of Article 3. The home solicitation provisions apply to residents because subsection (1) makes this Act apply if the buyer's agreement or offer to purchase is received by the seller in this State and a home solicitation sale is defined in Section 3.501 as one in which the buyer's agreement or offer to purchase is received by the seller, who personally solicits the sale, at a residence. Under subsection (3), a creditor is subject to the limitations on his remedies provided by Part 1 of Article 5 in actions he brings in the enacting State against all persons, whether or not they were residents at the time the credit agreement was made.

2. Subsection (1) serves as a general residual provision governing those matters not specifically treated elsewhere in the section and controls the applicability of the disclosure provisions. Under this subsection the creditor has a measure of control over the applicability of the Act with respect to the disclosure requirements and can arrange his interstate operations in a manner which minimizes the operational difficulties arising from the variations in the disclosure requirements of the different state laws. This flexibility on the part of creditors with respect to the applicability of the disclosure provisions offers no threat to consumers because the Federal

Consumer Credit Protection Act [15 U.S.C. § 1601 et seq.] assures consumers that disclosure requirements will be substantially similar in all states.

3. Creditors falling within the supervised lender category (Part 3 of Article 2) need be licensed only in the State where the loan is entered into, that is, where the debtor's writing is received [Subsection (1) ]. However, in the case of a mail order loan to a consumer residing in an enacting State, even if the debtor's writing is received by the creditor in another State, the creditor may not exceed the rate ceilings of the enacting State and the Administrator may go into the creditor's State and investigate potential violations pursuant to Part 1 of Article 6 [Subsection (2) ]. Of course, the general rule of subsection (1) that a transaction is entered into in the State where the consumer's writing is received yields whenever the creditor attempts to evade the Act by engaging in face-to-face solicitation in the State of the consumer's residence but contrives to have the consumer's writing sent the creditor in another State [Subsection (1)(a) ].

4. The danger that creditors may be able to induce consumers to agree that the applicable law will be that of a creditors' haven that has no effective consumer credit protection has led to invalidating choice of law agreements except where the law chosen is that of the State of the consumer's residence [Subsections (7) and (8) ]. Subsection (9) specifies the applicable law governing the powers of the Administrator and the notification and fees requirements.

**§ 1.202. [Exclusions]**

This Act does not apply to:

(1) extensions of credit to organizations;

(2) except as otherwise provided in the Article on Insurance (Article 4), the sale of insurance if the insured is not obligated to pay instalments of the premium and the insurance may terminate or be cancelled after non-payment of an instalment of the premium;

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

(4) transactions in securities or commodities accounts with a broker-dealer registered with the Securities and Exchange Commission; [or]

(5) except with respect to the provisions on compliance with the Federal Truth in Lending Act (Section 3.201), [civil liability for violation of disclosure provisions (Section 5.203), criminal

penalties for disclosure violations (Section 5.302) ], and powers and functions of the Administrator with respect to disclosure violations (Part 1 of Article 6), pawnbrokers who are licensed and whose rates and charges are regulated under or pursuant to ordinances or other statutes [; or

(6) ceilings on rates or limits on loan maturities of credit extended by a credit union organized under the laws of this State or of the United States if these ceilings or limits are established by these laws or by applicable regulations].

**Note 1.** If the enacting State wishes to apply for an exemption from the Federal Truth in Lending Act, the brackets before and after Sections 5.203 and 5.302 should be deleted and those sections enacted, and the brackets in subsection (5) preceding and following references to those sections should be omitted; otherwise, delete the brackets and the language enclosed within them, and delete the references to Sections 5.203 and 5.302 in the Table of Articles, Parts, and Sections.

**Note 2.** If subsection (6) is included by the enacting State, delete "[or]" at the end of subsection (4), the opening bracket at the end of subsection (5), and the closing bracket at the end of subsection (6). If subsection (6) is not included by the enacting State, delete the brackets before and after "or" at the end of subsection (4).

## COMMENT

The Consumer Credit Protection Act, 15 U.S.C. §§ 1601 et seq., will hereafter be referred to as "CCPA." Regulation Z, 12 CFR §§ 226 et seq., will hereafter be referred to as "Regulation Z."

Subsection (1) excludes transactions in which credit is extended to organizations (Section 1.301(29)). Subsection (2) makes clear that sales of insurance are not consumer credit transactions if no credit (Section 1.301(16)) has been extended. However, loans to purchase insurance are covered if they qualify as consumer loans (Section 1.301(15)), and insurance provided in connection with consumer credit transactions is regulated by Article 4. Subsection

(3) is derived from CCPA Section 104(4), 15 U.S.C. § 1603(4). Subsection (4) is derived from CCPA Section 104(2), 15 U.S.C. § 1603(2); this provision excludes stock broker loans from coverage of the Act. Subsection (5) excludes pawnbrokers from coverage of the Act, except for certain disclosure requirements, if local or state laws provide for licensing and regulation of rates and charges. Since the CCPA applies to pawnbrokers engaging in consumer credit transactions, this Act supplements the coverage of the CCPA in this respect by allowing the Administrator to consider a violation of the CCPA as a violation of this Act (Section 3.201) and to act against the violator (Section 6.104(2)). Subsection (6) is an optional provision allowing states to continue the relatively low rate limitations, as well as loan maturities, that have traditionally applied to the credit unions.

Other transactions are inferentially excluded by the definitions of the three key transactions covered by the Act, "consumer credit sale" (Section 1.301(12)), "consumer lease" (Section 1.301(14)), and "consumer loan" (Section 1.301(15)). With respect to sales and loans, these definitions exclude: sales (paragraph (a)(i)) and loans (paragraph (a)) made by creditors not regularly engaged in these transactions; sales (paragraph (a)(ii)) and loans (paragraph (a)(i)) to organizations; sales (paragraph (a)(iii)) and loans (paragraph (a)(ii)) for business purposes; sales (paragraph (a)(iv)) and loans (paragraph (a)(iii)) in which there is neither a requirement for payment of a finance charge nor for payment in instalments; sales (paragraph (a)(v)) and loans (paragraph (a)(iv)), other than real property transactions, in which the amount financed exceeds $25,000; and sales (paragraph (b)(ii)) and loans (paragraph (b)(ii)) which are real property transactions in which the finance charge is 12 per cent or less. The definition of "consumer lease" (Section 1.301(14)) excludes: leases by lessors not regularly engaged in leasing, leases made to organizations, leases for business purposes (paragraph (a)(i)); leases in which the amount payable exceeds $25,000 (paragraph (a)(ii)); and leases for a term of 4 months or less (paragraph (a)(iii)).

**§ 1.203. [Jurisdiction [and Service of Process]]**

[ (1) ] The [ ] court of this State may exercise jurisdiction over any creditor with respect to any conduct of the creditor subject to this Act or with respect to any claim arising from a transaction subject to this Act.

[ (2) In addition to any other method provided by [rule] [statute], personal jurisdiction over a creditor may be acquired in a civil action or proceeding instituted in the [ ] court by service of process in the manner provided in this section. If a creditor is not a resident of this State or is a corporation not authorized to do business in this State and engages in any conduct in this State subject to this Act or in a transaction subject to this Act, he may designate an agent upon whom service of process may be made in this State. The agent shall be a resident of this

State or a corporation authorized to do business in this State. The designation shall be in a writing and filed with the Secretary of State. If a designation is not made and filed or if process cannot be served in this State upon the designated agent, process may be served upon the Secretary of State, but service upon him is not effective unless the plaintiff or petitioner forthwith mails a copy of the process and pleading by registered or certified mail to the defendant or respondent at his last reasonably ascertainable address. An affidavit of compliance with this section shall be filed with the clerk of the court on or before the return day of the process, if any, or within any further time the court allows.]

**Note:** If the enacting State has an adequate long arm statute, the bracketed words "and Service of Process" in the section heading, the bracketed "(1)," and all of subsection (2) may be omitted.

**COMMENT**

Without limiting the jurisdiction of other courts over creditors, this section specifically grants that jurisdiction to a specified court. It also provides a method of obtaining personal jurisdiction over creditors by service of process.

PART 3

**DEFINITIONS**

**§ 1.301. [General Definitions]**

(1) "Actuarial method" means the method of allocating payments made on a debt between the amount financed and the finance charge pursuant to which a payment is applied first to the accumulated finance charge and any remainder is subtracted from, or any deficiency is added to, the unpaid balance of the amount financed. The Administrator may adopt rules not inconsistent with the Federal Truth in Lending Act further defining the term and prescribing its application.

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

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

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

(5) "Amount financed" means the total of the following items:

(a) in the case of a sale, the cash price of the goods, services, or interest in land, less the amount of any down payment made in cash or in property traded in, and the amount actually paid or to be paid by the seller pursuant to an agreement with the buyer to discharge a security interest in, a lien on, or a debt with respect to property traded in;

(b) in case of a loan, the net amount paid to, receivable by, or paid or payable for the account of the debtor, plus the amount of any discount excluded from the finance charge (paragraph (b)(iii) of subsection (20)); and

(c) in the case of a sale or loan, to the extent that payment is deferred and the amount is not otherwise included and is authorized and disclosed to the consumer as required by law:

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

(ii) permitted additional charges (Section 2.501).

(6) "Billing cycle" means the time interval between periodic billing statement dates.

(7) "Card issuer" means a person who issues a credit card.

(8) "Cardholder" means a person to whom a credit card is issued or who has agreed with the card issuer to pay obligations arising from the issuance to or use of the card by another person.

(9) "Cash price" of goods, services, or an interest in land means the price at which they are offered for sale by the seller to cash buyers in the ordinary course of business and may include (1) the cash price of accessories or services related to the sale, such as delivery, installation, alterations, modifications, and improvements, and (b) taxes to the extent imposed on a cash sale of the goods, services, or interest in land. The cash price stated by the seller to the buyer in a disclosure statement required by law is presumed to be the cash price.

(10) "Conspicuous":

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

(11) "Consumer" means the buyer, lessee, or debtor to whom credit is granted in a consumer credit transaction.

(12) "Consumer credit sale":

(a) Except as provided in paragraph (b), "consumer credit sale" means a sale of goods, services, or an interest in land in which:

(i) credit is granted either pursuant to a seller credit card or by a seller who regularly engages as a seller in credit transactions of the same kind;

(ii) the buyer is a person other than an organization;

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

(iv) the debt is payable in instalments or a finance charge is made; and

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

(b) A "consumer credit sale" does not include:

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

(ii) unless the sale is made subject to this Act by agreement (Section 1.109), a sale of an interest in land if the finance charge does not exceed 12 per cent per year calculated according to the actuarial method on the assumption that the debt will be paid according to the agreed terms and will not be paid before the end of the agreed term.

(c) The amount of $25,000 in paragraph (a)(v) is subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

(13) "Consumer credit transaction" means a consumer credit sale or consumer loan or a refinancing or consolidation thereof, or a consumer lease.

(14) "Consumer lease":

(a) "Consumer lease" means a lease of goods:

(i) which a lessor regularly engaged in the business of leasing makes to a person, except an organization, who takes under the lease primarily for a personal, family,

household, or agricultural purpose;

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

(iii) which is for a term exceeding four months; and

(iv) which is not made pursuant to a lender credit card.

(b) The amount of $25,000 in paragraph (a)(ii) is subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

(15) "Consumer loan":

(a) Except as provided in paragraph (b), "consumer loan" means a loan made by a creditor regularly engaged in the business of making loans in which:

(i) the debtor is a person other than an organization;

(ii) the debt is incurred primarily for a personal, family, household, or agricultural purpose;

(iii) the debt is payable in instalments or a finance charge is made; and

(iv) the amount financed does not exceed $25,000 or the debt, other than one incurred primarily for an agricultural purpose, is secured by an interest in land.

(b) A "consumer loan" does not include:

(i) a sale or lease in which the seller or lessor allows the buyer or lessee to purchase or lease pursuant to a seller credit card, or

(ii) unless the loan is made subject to this Act by agreement (Section 1.109), a loan secured by an interest in land if the security interest is bona fide and not for the purpose of circumvention or evasion of this Act and the finance charge does not exceed 12 per cent per year calculated according to the actuarial method on the assumption that the debt will be paid according to the agreed terms and will not be paid before the end of the agreed term.

(c) A loan that would be a consumer loan if the lender were regularly engaged in the business of making loans is a consumer loan if the loan is arranged for a commission or other compensation by a person regularly engaged in the business of arranging those loans and the lender is not regularly engaged in the business of making loans. The arranger is deemed to be the creditor making the loan.

(d) The amount of $25,000 in paragraph(a)(iv) is subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

(16) "Credit" means the right granted by a creditor to a consumer to defer payment of debt, to incur debt and defer its payment, or to purchase property or services and defer payment therefor.

(17) "Credit card" means a card or device issued under an arrangement pursuant to which a card issuer gives to a cardholder the privilege of obtaining credit from the card issuer or other person in purchasing or leasing property or services, obtaining loans, or otherwise. A transaction is "pursuant to a credit card" only if credit is obtained according to the terms of the arrangement by transmitting information contained on the card or device orally, in writing, by mechanical or electronic methods, or in any other manner. A transaction is not "pursuant to a credit card" if the card or device is used solely in that transaction to:

(a) identify the cardholder or evidence his credit-worthiness and credit is not obtained according to the terms of the arrangement;

(b) obtain a guarantee of payment from the cardholder's deposit account, whether or not the payment results in a credit extension to the cardholder by the card issuer; or

(c) effect an immediate transfer of funds from the cardholder's deposit account by electronic or other means, whether or not the transfer results in a credit extension to the

cardholder by the card issuer.

(18) "Creditor" means the person who grants credit in a consumer credit transaction or, except as otherwise provided, an assignee of a creditor's right to payment, but use of the term does not in itself impose on an assignee any obligation of his assignor. In case of credit granted pursuant to a credit card, "creditor" means the card issuer and not another person honoring the credit card.

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

(20) "Finance charge":

(a) Except as provided in paragraph (b), "finance charge" means the sum of all charges payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or as a condition of the extension of credit, including any of the following types of charges which are applicable:

(i) interest or any amount payable under a point, discount, or other system of charges, however denominated;

(ii) time-price differential, credit service, service, carrying, or other charge, however denominated;

(iii) premium or other charge for any guarantee or insurance protecting the creditor against the consumer's default or other credit loss; and

(iv) charges incurred for investigating the collateral or credit-worthiness of the consumer or for commissions or brokerage for obtaining the credit, irrespective of the person

to whom the charges are paid or payable, unless the creditor had no notice of the charges when the credit was granted.

(b) The term does not include:

(i) charges as a result of default or delinquency if made for actual unanticipated late payment, delinquency, default, or other like occurrence, unless the parties agree that these charges are finance charges; a charge is not made for actual unanticipated late payment, delinquency, default or other like occurrence if imposed on an account that is or may be debited from time to time for purchases or other debts and, under its terms, payment in full or of a specified amount is required when billed, and in the ordinary course of business the consumer is permitted to continue to have purchases or other debts debited to the account after imposition of the charge;

(ii) additional charges (Section 2.501) or deferral charges (Section 2.503); or

(iii) a discount, if a creditor purchases or satisfies obligations of a cardholder pursuant to a credit card and the purchase or satisfaction is made at less than the face amount of the obligation.

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

(22) "Insurance premium loan" means a consumer loan that (a) is made for the sole purpose of financing the payment by or on behalf of an insured of the premium on one or more policies or contracts issued by or on behalf of an insurer, (b) is secured by an assignment by the insured to the lender of the unearned premium on the policy or contract, and (c) contains an authorization to cancel the policy or contract financed.

(23) Except as otherwise provided, "lender" includes an assignee of a lender's right to payment, but use of the term does not in itself impose on an assignee any obligation of the lender.

(24) "Lender credit card" means a credit card issued by a supervised lender.

(25) "Loan":

(a) Except as provided in paragraph (b), "loan" includes:

(i) the creation of debt by the lender's payment of or agreement to pay money to the debtor or to a third person for the account of the debtor;

(ii) the creation of debt pursuant to a lender credit card in any manner, including a cash advance or the card issuer's honoring a draft or similar order for the payment of money drawn or accepted by the debtor, paying or agreeing to pay the debtor's obligation, or purchasing or otherwise acquiring the debtor's obligation from the obligee or his assignees;

(iii) the creation of debt by a cash advance to a debtor pursuant to a seller credit card;

(iv) the creation of debt by a credit to an account with the lender upon which the debtor is entitled to draw immediately; and

(v) the forbearance of debt arising from a loan.

(b) "Loan" does not include:

(i) a card issuer's payment or agreement to pay money to a third person for the account of a debtor if the debt of the debtor arises from a sale or lease and results from use of a seller credit card; or

(ii) the forbearance of debt arising from a sale or lease.

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

(27) "Official fees" means:

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

(b) premiums payable for insurance in lieu of perfecting a security interest otherwise required by the creditor in connection with the transaction, if the premium does not exceed the fees and charges described in paragraph (a) which would otherwise be payable.

(28) "Open-end credit" means an arrangement pursuant to which:

(a) a creditor may permit a consumer, from time to time, to purchase or lease on credit from the creditor or pursuant to a credit card, or to obtain loans from the creditor or pursuant to a credit card;

(b) the amounts financed and the finance and other appropriate charges are debited to an account;

(c) the finance charge, if made, is computed on the account periodically; and

(d) either the consumer has the privilege of paying in full or in instalments or the creditor periodically imposes charges computed on the account for delaying payment and permits the consumer to continue to purchase or lease on credit.

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

(30) "Payable in instalments" means that payment is required or permitted by agreement to be made in more than four periodic payments, excluding a downpayment. If any periodic payment other than the downpayment under an agreement requiring or permitting two or more periodic payments is more than twice the amount of any other periodic payment, excluding a

downpayment, a consumer credit transaction is "payable in instalments."

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

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

(33) "Precomputed consumer credit transaction" means a consumer credit transaction, other than a consumer lease, in which the debt is a sum comprising the amount financed and the amount of the finance charge computed in advance. A disclosure required by the Federal Truth in Lending Act does not in itself make a finance charge or transaction precomputed.

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

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

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

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

(38) "Seller" includes, except as otherwise provided, an assignee of the seller's right to payment, but use of the term does not in itself impose on an assignee any obligation of the seller.

(39) "Seller credit card" means either:

(a) a credit card issued primarily for the purpose of giving the cardholder the privilege of using the card to purchase or lease property or services from the card issuer, persons related to the card issuer, or persons licensed or franchised to do business under the card issuer's business or trade name or designation, or both from any of these persons and from other persons; or

(b) a credit card issued by a person except a supervised lender primarily for the purpose of giving the cardholder the privilege of using the credit card to purchase or lease property or services from at least 100 persons not related to the card issuer.

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

(41) "Supervised financial organization" means a person, except an insurance company or other organization primarily engaged in an insurance business:

(a) organized, chartered, or holding an authorization certificate under laws of this

State or of the United States that authorizes the person to make loans and to receive deposits, including a savings, share, certificate or deposit account, and

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

(42) "Supervised lender" means a person authorized to make or take assignments of supervised loans, under a license issued by the Administrator (Section 2.301) or as a supervised financial organization (subsection (41)).

(43) "Supervised loan" means a consumer loan, including a loan made pursuant to open-end credit, in which the rate of the finance charge, calculated according to the actuarial method, exceeds 18 per cent per year.

**COMMENT**

**Subsection (1):**

This subsection is derived from CCPA Section 107(a)(1)(A), 15 U.S.C. § 1606(a)(1)(A), and from Supplement I to Regulation Z(a). The intent is that with respect to the meaning and application of the defined term the Administrator will maintain by rule consistency between this Act and the Federal Truth in Lending Act.

The assumption underlying the actuarial method is that a periodic payment is applied first to the accumulated unpaid finance charge. If the payment exceeds the unpaid accumulated finance charge, the remainder of the payment is applied to reduce the unpaid balance of the amount financed.

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

| (A) Unpaid balance of amount financed | (B) Monthly Rate | (C) Application of Finance charge | (D) payment Amount financed | (E) Total monthly payment (C)+(D) |
|---|---|---|---|---|

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| 500.00 | X | 1% | = | 5.00 | | 123.14 | | 128.14 |
| 376.86 | X | 1% | = | 3.77 | | 124.37 | | 128.14 |
| 252.49 | X | 1% | = | 2.52 | | 125.62 | | 128.14 |
| 126.87 | X | 1% | = | 1.27 | | 126.87 | | 128.14 |
| | | | | 12.56 | + | 500.00 | = | 512.56 |

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

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

**Subsection (3):**

This definition is derived from UCC Section 1-201(3). The terms "course of dealing," "usage of trade," and "course of performance" should be given the same meanings under this Act as under the UCC with allowance for the different context, e.g., consumer compared to commercial, and "course of performance" should apply to lessors and lenders as well as to sellers.

**Subsection (4):**

This definition is identical to that in Regulation Z Section 226.2(c). The definition of "agricultural products" is derived from the Agricultural Marketing Act of 1946, 7 U.S.C. § 1626. Though the definition of "agricultural products" is broad, the operative definition is "agricultural purpose" and this is narrowed by the requirement that the person dealing with agricultural products be one who cultivates, plants, propagates, or nurtures the agricultural products.

**Subsection (5):**

The term "amount financed" means the amount of credit extended to the consumer and includes not only the net price in sales and the net amount advanced in loans but also other amounts such as official fees, insurance charges, and other additional charges (Section 2.501) to the extent that payment is deferred. An advance payment of finance charge or a required compensating balance is deducted from the "net amount paid" under paragraph (b) of this subsection. The term is a key definition in Parts 2 (maximum finance charges, sales) and 4 (maximum finance charges, loans) of Article 2 for it determines the amount on which the finance charge is imposed. This definition is in harmony with Regulation Z Sections 226.2(d), 226.4(b), and 226.8(c)(7) and (d)(1).

The reference in paragraph (b) to Section 1.301(20)(b)(iii) relates to the practice of credit card issuers of paying sellers honoring credit cards less than the face amount of the cardholder's obligation. Paragraph (b) makes clear that this discount is a part of the amount financed even though the amount of the discount is not paid to the seller for the cardholder's account. Since the seller absorbs the discount in the price of his product, the amount of the discount redounds to the cardholder's benefit and is properly included in the amount financed. That is, the cardholder would pay the same price for the product purchased whether he pays cash or uses a credit card. However, if the goods are sold at one price pursuant to credit cards and at a lower price for cash, then the lower price would be the cash price pursuant to Section 1.301(9) and the differential would be a finance charge pursuant to Section 1.301(20) and not part of the amount financed. The discount problem need only be specially treated when use of the credit card results in a loan, as in the case of lender credit cards (Section 1.301(25)(a)(ii)), for in the case of sales pursuant to seller credit cards (Section 1.301(12)(a)(i)) the cash price of the property or services sold includes the discount, if any, which is thereby included in the amount financed.

**Subsection (6):**

This definition is derived from Regulation Z Section 226.2(g). See also Sections 2.203(3) and 2.401(1).

**Subsection (7):**

This definition is derived from Regulation Z Section 226.13(a)(3).

**Subsection (8):**

This definition is derived from Regulation Z Section 226.13(a)(4).

**Subsection (9):**

For either rate ceilings or disclosure provisions to be meaningful in credit sales, the amount financed on which finance charges are imposed must include a true cash price. See Regulation Z Section 226.2(i). If a seller sells an item in ordinary course for $97 for cash but sells the same item for $100 to buyers wishing to pay in instalments, the $3 differential is not part of a true cash price but is a finance charge (Section 1.301(20)) imposed by the seller. Nothing in this definition prevents sellers from selling both for cash and on time for the same price. For purposes of this definition it does not matter whether the charges enumerated in (a) and (b) are included in the cash price or separately stated, for in either case the amount financed, on which the finance charge is based, will include both the cash price and the enumerated charges. See Section 1.301(5).

**Subsection (10):**

This definition is derived from UCC Section 1-201(10), but the specific examples set out in the UCC provision are omitted. Here, as under the UCC, the issue is whether attention can reasonably be expected to be called to a term, and this is a question of law and not fact.

**Subsection (12):**

Since most of the operative provisions of the Act apply to consumer credit sales, consumer leases, or consumer loans, the definitions of these terms are the key scope definitions of the Act. The definition of consumer credit sale substantially tracks with the coverage of credit sales in Regulation Z Sections 226.2(k) and (m), and 226.3(c). The requirement that a sale either be payable in instalments (Section 1.301(30)) or subject to a finance charge excludes a great mass of transactions, e.g., the 30-day retail charge account and the short-term credit furnished by professional people and artisans on a one-payment basis in connection with sales of their services for which no charge for credit is made.

Sales or leases pursuant to a lender credit card give rise to loans (Section 1.301(25)(a)(ii)) as between the card issuer and cardholder. Consumer credit sales of land are covered for rate regulation and other purposes so long as the finance charge is in excess of 12%, but the provisions on compliance with the Truth in Lending Act (Section 3.201) apply to land sales whatever the rate of finance charge. See the Comment to Section 1.301(15) "consumer loan" for discussion of the Act's policy with regard to land transactions.

**Subsection (14):**

Leasing has become a popular alternative to credit sales as a means of distributing goods to consumers and merits inclusion in a comprehensive consumer credit code. The four month term requirement in paragraph (a)(iii) excludes from the Act the innumerable hourly, daily, or weekly rental or hire agreements typically involving automobiles, trailers, home repair tools, sick room equipment, and the like. If the transaction, though in form a lease, is in substance a sale within the meaning of Section 1.301(35), it is treated as a sale for all purposes in this Act and the provisions on consumer leases are inapplicable. The Act requires disclosure of the elements of the consumer lease transaction (Section 3.202); places limits on advertising respecting consumer leases (Section 3.209); contains a number of limitations on agreements and practices applicable to consumer leases (Part 3 of Article 3) and on the lessee's liability (Part 4 of Article 3, notably Section 3.401); regulates insurance provided in relation to consumer lease transactions (Article 4); makes provisions for remedies and penalties in consumer lease transactions (Article 5); and gives the Administrator powers over consumer lease transactions (Article 6). Since a finance charge is not made in the usual consumer lease transaction, the rate ceiling provisions of the Act (Article 2) are inapplicable.

**Subsection (15):**

See Comment to Section 1.301(12) "consumer credit sale." Sales pursuant to seller credit cards are classified as credit sales and not loans (Section 1.301(25)(b)(i)).

With respect to this Act's treatment of real property transactions, the 12% cut-off was chosen as a convenient line of demarcation between two dissimilar transactions-the home mortgage and the high rate, "small loan" type of real estate loan. The exclusion of the home mortgage was made because the problems of home financing are sufficiently different to justify

separate statutory treatment. On the other hand, the high rate second mortgage transaction has been a major source of consumer complaint and merits full coverage by this Act. Since the Truth in Lending Act applies to real estate credit without regard to the rate of finance charge, the provision on compliance with Truth in Lending (Section 3.201) applies to all consumer real estate transactions without regard to the rate of the finance charge.

Paragraph (c) applies to transactions in which a professional arranger places loans for a lender not ordinarily engaged in the business of making loans and collects a commission for arranging the loan. The arranger is considered to be the creditor making the loan for purposes of compliance with the provisions on authority to make supervised loans (Section 2.301).

**Subsection (16):**

Credit is extended either when one who owes a debt is allowed to defer payment of the obligation or when one is given the right to incur an obligation in the future and to defer its payment. A commitment by a creditor to advance funds on request, as in the case of a letter of credit, is an example of the latter case. The original U3C definition of "credit" appearing in the 1968 Text, which did not contain the last clause in the present definition, was adopted by CCPA Section 103(e), 15 U.S.C. § 1602(e). For its definition of "credit," Regulation Z Section 226.2(1) added the last clause to this definition, and the definition in the U3C 1974 Text was modified to conform to Regulation Z.

**Subsection (17):**

The meanings of "credit card" and "pursuant to a credit card" are broadly defined to allow for continuing technological developments in this area. The term "credit card" is defined to encompass the varied arrangements under which creditors equip consumers with some form of "card or device" that enables them to obtain credit from the issuing creditor or others. A "credit card" may be conceived of in its broadest sense as a repository of information, and a transaction is "pursuant to a credit card" when credit is obtained in accordance with the arrangement under which the card was issued by the transmission of some information on the card. Hence, a cardholder who telephones an airline and buys a ticket by giving the agent his credit card number or a cardholder who communicates the requisite information to a seller by using a device which gives off an electronic impulse is each engaging in a transaction "pursuant to a credit card" so long as they are acting within the terms of the arrangement. However, a creditor who himself extends credit to a consumer relying on the consumer's credit card issued by another creditor merely as an identification or verification of credit-worthiness of the consumer has not extended credit "pursuant to a credit card."

Moreover, use of a credit card to obtain a guarantee of payment or to effect an immediate transfer from the cardholder's deposit account is not "pursuant to a credit card" whether or not the payment or transfer results in a credit extension to the cardholder by the card issuer.

**Subsection (18):**

Though assignees take all rights conferred by this Act on creditors, they are liable for the

obligations imposed on creditors by this Act only with respect to occurrences after assignment unless the Act provides otherwise. Various provisions of the Act apply specifically to assignees of credit grantors, *e.g.*, Sections 5.201(2), [5.203(4),] 5.301(2), 6.102(2). The second sentence makes clear that in credit card transactions the person honoring the credit card is not granting credit unless he is also the card issuer. However, even though the person honoring a credit card may not be a creditor, he does "participate in consumer credit transactions" under Section 6.102(1) and is under the jurisdiction of the Administrator.

**Subsection (19):**

This definition varies from that found in CCPA Section 302, 15 U.S.C. § 1672, in that "by an employer to an employee" is added, thereby restricting this definition to the employment relationship in contrast to the broad coverage of the federal act which would include sums owed to independent contractors.

**Subsection (20):**

This definition, together with the provisions on "additional charges" (Section 2.501), is substantially similar to the concept of finance charge embodied in Regulation Z Section 226.4. In general, charges "incident to or as a condition of the extension of credit" are finance charges, whatever the parties call them, if imposed by the creditor on the consumer, unless the charge is excluded by paragraph (b) as a default or delinquency charge, an additional or deferral charge, or a credit card discount.

True default or delinquency charges are not finance charges and are separately regulated by Section 2.502. The test prescribed by Regulation Z Section 226.4(c) and Interpretation 226.401 is adopted in paragraph (b)(i) for determining when a charge is a true default or delinquency charge. In some instances this will leave the question of the applicability of the Act to depend on the factual determination whether a given charge is (1) a true late charge, which would make the Act inapplicable if there is no provision either for payment in instalments or a finance charge, or (2) a finance charge, which would make the Act applicable even though there is no provision for payment in instalments (Section 1.301(12)(a)(iv)). An example is the case in which an oil company extends 30-day credit with no right to defer payment further and imposes a charge for late payment but does not require surrender of the credit card if full payment is not made by the consumer when billed. In such a case paragraph (b)(i) allows the creditor to avoid any uncertainty about the applicability of the Act by obtaining the consumer's agreement that the charge should be considered a finance charge.

For a discussion of the reason for the exclusion in paragraph (b)(iii) of the credit card discount, see the Comment to Section 1.301(5) "amount financed."

**Subsection (22):**

The financing of the premium for an insurance policy or contract is a loan whether made directly between lender and insured or arranged by an insurance agent or broker. An "insurance premium loan" includes neither the sale of insurance if the insured is not obligated to pay

instalments of the premium and the insurance may terminate or be cancelled after non-payment of the premium (subsection (2) of Section 1.202), nor the provision of insurance in connection with a consumer credit transaction when the charge for the insurance is a permitted "additional charge" (paragraph (e) of subsection (1), and subsection (2) of Section 2.501).

**Subsection (23):**

See Comment to Section 1.301(18) "creditor."

**Subsection (24):**

The bank credit card is the most common lender credit card; however, licensed lenders (Section 2.301) can also issue lender credit cards.

**Subsection (25):**

The distinction between loans and sales is basic to the applicability of the rate ceiling provisions (Parts 2 and 4 of Article 2), the licensing provisions (Part 3 of Article 2), provisions relating to credit cards (Section 1.301(24) "lender credit card" and (39) "seller credit card"), and other provisions of the Act. The traditional concept of a loan as an advance of money or a commitment to advance money is continued in paragraph (a)(i) and (iv). The development of the credit card has blurred somewhat accepted boundaries between loans and sales and has necessitated a clarification of the rules in this regard. See the discussion of this matter in Comment to Section 1.301(39) "seller credit card." Use of a lender credit card, whether for purchases or cash advances, results in a loan.

The arrangement for the card issuer's payment to the person honoring the credit card may take different forms. It does not matter under paragraph (a)(ii) whether the arrangement calls for the third party to be the payee of a draft drawn by the cardholder on the card issuer, for the card issuer to take an assignment of the debt from the third party, or for the card issuer merely to pay to the third party the discounted amount of the cardholder's obligation. Each of these methods is sufficiently similar in function to be treated alike by this section.

Under this Act forbearance of debt is characterized on the basis of the nature of the original debt. Thus forbearance of debt arising from sales or leases is not a loan transaction within this Act (paragraph (b)(ii)). Sellers and lessors can enter into refinancings to meet the needs of consumers without having these transactions classified as loans resulting in the applicability of the licensing provisions and other provisions of the Act designed to regulate lenders.

Occasionally seller credit card issuers may allow their cardholders to obtain nominal cash advances pursuant to their credit card. An example is an automobile rental company which extends to its cardholders as a convenience the privilege of obtaining cash advances up to $40 in emergency situations. This is a loan transaction under paragraph (a)(iii), and if the finance charge exceeds 18% (Section 2.401(1) the licensing provisions of Part 3 of Article 2 apply.

**Subsection (26):**

"Merchandise certificate" primarily means the kind of scrip issued by merchants to facilitate the purchase on credit of a number of relatively small items so that a separate contract or agreement is not required for each item purchased; it does not include a trading stamp redeemable only at a stamp redemption center.

**Subsection (27):**

This definition is derived from Regulation Z Section 226.4(b)(1) and (2).

**Subsection (28):**

The problem arises how the Act applies to a transaction in which a seller credit card issuer allows a cardholder to make purchases and add them to an account payable at a fixed time after billing with no right to defer payment further and with a charge imposed for late payment. If the charge imposed is a "true" late payment under Section 1.301(20)(b)(i), the transaction is not a consumer credit sale because there is neither a finance charge nor the privilege of paying in instalments (Section 1.301(12)(a)(iv)). The Act's only coverage of such a case is a limit on the amount of the late charge (Section 2.601(2)). If the late charge is in fact a finance charge under the test set out in Section 1.301(20)(b)(i), the transaction is a consumer credit sale and the Act applies fully. The last "or" clause in paragraph (d) directs that such a transaction be treated as open-end credit. A similar result is reached by Regulation Z Section 226.2(r) and Interpretation 226.401.

**Subsection (30):**

Two guiding principles in determining the scope of the Act are: (1) The Act should not apply to the myriad credit transactions in which no finance charge is made and no substantial period of credit extension is involved. The old-fashioned 30-day department store charge account is an example. (2) The Act should apply to credit extended over a substantial period of time even though the creditor does not separately state a finance charge. The transactions of the credit jeweler who "buries" his finance charge and sells his merchandise for the same price on a 12-month instalment contract as for cash is an example. The drafting technique by which these ends are attained is the definition of consumer credit sales (Section 1.301(12)(a)(iv)) and consumer loans (Section 1.301(15)(a)(iii)) as transactions in which either a finance charge is made or which are payable in instalments. In the definition of "payable in instalments," the Act adopts the more-than-four-payment rule as the dividing line for transactions meriting coverage by the Act. This test has been incorporated into Regulation Z Section 226.2(k) and was sustained in Mourning v. Family Publications Serv., Inc., 411 U.S. 356, 93 S.Ct. 1652, 36 L.Ed.2d 318 (1973). A consumer transaction is payable in instalments if the consumer has the option either of paying the debt in full within a given period of time without a finance charge or of paying the balance in instalments plus a finance charge.

**Subsection (33):**

A credit transaction is precomputed whether the finance charge is "added-on" to the amount financed or, as is common in loan situations, the "discount" method is used and the finance charge is deducted from the face amount of the credit at the time of the credit extension. In both transactions the debt is expressed as a sum comprising the amount financed and the amount of the finance charge. If a loan transaction involves a principal of $2,000 repayable in 12 monthly instalments at an interest rate of 10% on the declining balance, the transaction is not precomputed even though the creditor must for purposes of the Federal Truth in Lending Act disclose a sum including both the $2,000 and the amount of the finance charge the debtor would pay if each instalment were paid on time.

**Subsection (34):**

This definition is derived from UCC Section 1-201(31).

**Subsection (35):**

This definition is derived from Regulation Z Section 226.2(n).

**Subsection (36):**

This definition parallels that in subsection (35).

**Subsection (38):**

See definition of "creditor" in subsection (18).

**Subsection (39):**

Seller credit cards are issued primarily for the purpose of enabling cardholders to purchase property or services. Paragraph (a) applies to cards issued by card issuers who are themselves involved in the selling process either as retailers or as distributors who license or franchise retailers. So long as the card is issued for the purpose of purchasing from the issuer, a person related to the issuer, or a licensee or franchisee of the issuer, the card falls within paragraph (a) even though it may also be honored by sellers having no relation to the card issuer. For example, an oil distributor may issue a card for the purpose of allowing cardholders to buy petroleum products from independently owned franchisees of the issuer; the card falls within paragraph (a) even though it may also be honored by hotels, motels, and other service stations unrelated to the card issuer.

Paragraph (b) covers credit cards issued for the purpose of enabling cardholders to purchase from sellers unrelated to the card issuer. "Travel and entertainment" credit cards are the stereotype. The requirement that the card be honored by at least 100 unrelated retailers is designed to assure that this kind of card will be issued for bona fide sales purposes by entities large enough to be visible to the Administrator and will not be used as a subterfuge for masking unlicensed loans.

Although lender credit cards (Section 1.301(24)) are also used for purchasing property or services, they are increasingly utilized for cash loans. By classifying the use of credit cards issued by banks and licensed lenders as creating loans (Section 1.301(25)(a)(ii)), whether the card was used for purchases or cash advanced, the Act recognizes that credit card transactions are but one of many ways in which banks and other financial institutions extend credit and that it is not operationally desirable to introduce regulatory distinctions that would force these institutions to treat sales and loans pursuant to credit cards differently for purposes of maximum charges and other provisions of the Act.

**Subsection (40):**

The retail instalment sales acts often excluded from the definition of services those furnished by members of professions-physicians, dentists, and the like. This Act makes no such exclusion, but the definition of consumer credit sale in Section 1.301(12) excludes the usual arrangement that professional men use in selling their services in that they usually do not enter into instalment contracts with their patients or clients and do not impose finance charges. However, this Act does apply to the so-called "credit dentist" who sells his services on instalment contract with or without provision for a finance charge.

**Subsection (41):**

This definition defines the class of lender which may engage in the business of making supervised loans or taking assignments of such loans for collection without first being licensed under the Act by the Administrator. Sections 2.301 and 2.302. If a lender of this class is subject to supervision by an official or agency other than the Administrator, the powers of examination, investigation, and enforcement under this Act may be exercised by that official or agency. Section 6.105. This class of lender typically includes persons authorized to make loans and receive deposits or their equivalents, such as commercial banks, savings banks, savings and loan associations, and credit unions.

**Subsection (43):**

Although all persons making consumer loans (Section 1.301(15)) are regulated by this Act, those making high rate loans must either be licensed by the Administrator or be supervised financial organizations (Section 2.301). This Act has settled on the 18% finance charge rate as the dividing line, above which a creditor's right to operate may be conditioned on meeting the tests of Section 2.302(2) for licensing or qualifying as a supervised financial organization.

**§ 1.302. [Definition: "Federal Truth in Lending Act"]**

In this Act, as applicable, "Federal Truth in Lending Act" means Title I of the Consumer Credit Protection Act (Public Law 90-321; 82 Stat. 146; 15 U.S.C. §§ 1601 et seq.; as amended), except for the provisions concerning issuance, liability of holders, and fraudulent use

of credit cards (Sections 132-134, as added by Public Law 90-321; 84 Stat. 1126; 15 U.S.C. §§ 1642-1644), and includes regulations issued by the Board of Governors of the Federal Reserve System pursuant to that Act except those relating to the excepted provisions.

**COMMENT**

See Comment to Section 1.102.

**§ 1.303. [Other Defined Terms]**

Other defined terms in this Act and the sections in which they appear are:

"Closing costs" Section 2.501(1)

"Computational period" Section 2.503(1)

"Deferral" Section 2.503(1)

"Deferral period" Section 2.503(1)

"Disposable earnings" Section 5.105

"Garnishment" Section 5.105

"Home solicitation sale" Section 3.501

"Interval" Section 2.503(1)

"Periodic balance" Section 2.503(1)

"Pursuant to a credit card" Section 1.301(17)

"Residence" Section 1.201(6)

"Rule of 78" Section 2.503(1)

"Standard deferral" Section 2.503(1)

"Sum of the balances method" Section 2.503(1)

"Transaction" Section 2.503(1)

# ARTICLE 2

## FINANCE CHARGES AND RELATED PROVISIONS

### Part 1

### GENERAL PROVISIONS

Section


### Part 2

### CONSUMER CREDIT SALES: MAXIMUM FINANCE CHARGES



### Part 3

### CONSUMER LOANS: SUPERVISED LENDERS



### Part 4

### CONSUMER LOANS: MAXIMUM FINANCE CHARGES



### Part 5

### CONSUMER CREDIT TRANSACTIONS: OTHER CHARGES AND MODIFICATIONS

PART 1

## GENERAL PROVISIONS

### § 2.101. [Short Title]

This Article shall be known and may be cited as Uniform Consumer Credit Code-Finance Charges and Related Provisions.

### § 2.102. [Scope]

Part 2 of this Article applies to consumer credit sales. Parts 3 and 4 apply to consumer loans, including loans made by supervised lenders. Part 5 applies to other charges and modifications with respect to consumer credit transactions. Part 6 applies to other credit transactions.

PART 2

## CONSUMER CREDIT SALES: MAXIMUM FINANCE CHARGES

**§ 2.201. [Finance Charge for Consumer Credit Sales Not Pursuant to Open-End Credit]**

(1) With respect to a consumer credit sale, except a sale pursuant to open-end credit, a creditor may contract for and receive a finance charge not exceeding that permitted in this section.

(2) The finance charge, calculated according to the actuarial method, may not exceed the equivalent of the greater of either of the following:

(a) the total of:

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

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

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

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

(3) This section does not limit or restrict the manner of calculating the finance charge whether by way of add-on, discount, single annual percentage rate, or otherwise, so long as the rate of the finance charge does not exceed that permitted by this section. The finance charge may be contracted for and earned at the single annual percentage rate that would earn the same finance charge as the graduated rates when the debt is paid according to the agreed terms and the calculations are made according to the actuarial method. If the sale is a precomputed consumer credit transaction:

(a) the finance charge may be calculated on the assumption that all scheduled

payments will be made when due, and

(b) the effect of prepayment is governed by the provisions on rebate upon prepayment (Section 2.510).

(4) For purposes of this section, the term of a sale agreement commences with the date the credit is granted or, if goods are delivered or services performed ten days or more after that date, with the date of commencement of delivery or performance. Any month may be counted as 1/12th of a year, but a day is counted as 1/365th of a year. Subject to classifications and differentiations the seller may reasonably establish, a part of a month in excess of 15 days may be treated as a full month if periods of 15 days or less are disregarded and that procedure is not consistently used to obtain a greater yield than would otherwise be permitted. The Administrator may adopt rules not inconsistent with the Federal Truth in Lending Act with respect to treating as regular other minor irregularities in amount or time.

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

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

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

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

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

## COMMENT

1. *Purpose of rate ceilings provisions.* The purpose of this section and subsection (2) of Section 2.401 (Finance Charge for Consumer Loans) is to set ceilings and not to fix rates. Even under present statutes, considerable rate competition exists. The intent of this Act is to provide even more effective competition. Therefore, while this section sets rate ceilings, several sections are designed to generate sufficient competition to set rates. In addition, other provisions have been omitted by design, because they would have tended to restrict competition. Other provisions related to this section include:

(1) Disclosure of the finance charge both in dollar amounts and as annual percentages, as required by the Federal Truth in Lending Act and Section 3.201, is designed to facilitate comparative shopping. This is the most effective means of limiting prices. For most goods and services offered for sale in competitive markets, disclosure of the price generally has been deemed sufficient to regulate prices.

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

(3) Greater freedom of entry to the credit field is fostered by several provisions, as well as by several deliberate omissions. Open-end credit may be offered both in connection with consumer credit sales, consumer loans, and supervised loans. No type of credit grantor is limited by this Act in the amount of credit that may be extended. By design the license required to make supervised loans is made readily accessible to those showing financial responsibility, character, and fitness. Provisions for minimum financial assets and for a showing of convenience and advantage have been deliberately omitted, since their inclusion would tend to restrict competition and require establishment of rates, rather than ceilings.

Because of the different cost structures that will be developed as a result of this Act, comparison of these rate ceilings cannot be made to existing rate ceilings. In this respect, the rate ceilings in this section are intimately related to other parts of the Act which provide for limitations on agreements and practices (Article 3, Part 3), limitations on creditors' remedies (Article 5, Part 1), limitations on consumers' liabilities (Article 3, Part 4), and consumers' remedies (Article 5, Part 2). These provisions will tend to raise operating costs of credit grantors above current levels. Other things being equal, these provisions would require higher rate ceilings than now exist to assure the same availability of credit to consumers. If they were not provided, the least credit-worthy consumers now in the market would be relegated to the illegal market.

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

2**.** *Explanation of operation of rate ceilings.* This explanation of maximum rates applies equally to finance charges made under Section 2.201 (finance charge for consumer credit sales not pursuant to open-end credit) and under subsection (2) of Section 2.401 (finance charge for consumer loans).

(1) *Other than precomputed transactions***:** With respect to other than precomputed transactions the graduated rates permitted are calculated on unpaid principal balances. For example, Table A below illustrates the calculation of the monthly finance charge at the graduated rates on unpaid principal balances of various dollar amounts up to $1,500.

(2) *Precomputed transactions***:** With respect to precomputed transactions, the graduated rates permitted are calculated on the periodic declining unpaid balances. The provisions for graduated rates should not be construed as requiring simultaneous liquidation of different portions of the original unpaid balance. Thus, the 21% annual rate permitted on unpaid balances exceeding $300, but not exceeding $1,000, does not apply to the initial unpaid balance in that range for the scheduled maturity of the transaction, but only to the extent that periodic declining unpaid balances fall within the range from $300.01 to $1,000.

The operation of this principle with respect to a precomputed transaction involving a $1,500 principal amount to be repaid in twelve months is illustrated in Table A below. The table shows the total dollar charge, the monthly payments and the charge earned each month when the rates stated in Sections 2.201 and 2.401(2) are computed on the unpaid balance as of each scheduled payment date and each payment is applied first to the earned charge and then to principal. It also shows the unpaid balances which result from applying the rates stated in Sections 2.201 and 2.401(2) and the parts of each unpaid balance to which each rate applies each month. The total dollar charge so computed is $211.71, but three cents is waived rather than increase the final payment.

3. *Explanation of subsection (5).* With respect to Sections 2.201(5) and 2.401(5), the variation permitted is limited to 8% of the rate of the finance charge and does not permit an eight percentage point variation. For example, if a credit grantor were to levy an annual add-on finance charge of $10 per $100 of initial unpaid balance, under the provisions of this section he could establish the following maximum range for one-year contracts:

| Amount Financed | Finance Charge |
|---|---|
| $92.45-$107.55 | $10.00 |

The median amount financed is $100; that is, this amount is $7.55 from both the upper and lower limits of the specified range. Alternatively, it is just halfway between $92.45 and $107.55.

The specified range is limited by the 8% requirement. On one-year contracts the add-on finance charge results in an actuarial rate of 17.972%. Sections 2.201(5)(b) and 2.401(5)(b) specify that the yield on the lowest amount within the range may not be more than 8% higher than the yield provided on the median amount. Thus the yield on the lowest amount may not exceed 19.40% [17.972 + (.08 X 17.972) = 19.4098]. It follows that the lower amount must be such that the $10 credit service charge produces an annual rate not in excess of 19.40%. Interpolation from annuity tables shows that the lower amount must be about $92.45. Since the median is halfway between the upper and lower limits, the upper amount must be $107.55. These are close approximations; in actual practice precise limits can be determined.

To gain the convenience of using a single dollar amount of finance charge for a specified range of amounts financed the credit grantor must undercharge for amounts financed above the median. Thus the $10 finance charge is about $0.76 less than the $10.76 finance charge that could have been received by precise application of an add-on rate of $10 per $100 per annum on the initial unpaid balance. These results are summarized below for one-year monthly instalment contracts.

| (A) Amount financed | (B) Actual finance charge | (C) Accurate finance charge | (D) Dollar difference (C) – (B) | (E) Annual percentage rate |
|---|---|---|---|---|
| $107.55 | $10.00 | $10.755 | -$0.755 | 16.74% |
| $100.00 | $10.00 | $10.00 | 0.00 | 17.97% |
| $92.45 | $10.00 | $9.245 | +$0.755 | 19.40% |

The 8% variation is derived from Regulation Z Section 226.5(c).

TABLE A

Amortization Schedule for $1,500 to be paid in 12 equal and consecutive monthly instalments of Principal Amount and Finance Charge combined with the charge computed at maximum graduated rates authorized by Sections 2.201 and 2.401(2)-36% per year on that part of the unpaid balances not exceeding $300, plus 21% per year on that part of the unpaid balances exceeding $300 but not exceeding $1,000, plus 15% per year on that part of the unpaid balances exceeding $1,000, yields $211.68.

| | Unpaid Principal Balances Outstanding During Month | | | | Application of $142.64 Monthly Payments | |
|---|---|---|---|---|---|---|
| Mo. | 36% | 21% | 15% | Total | Charges | Principal |
| 1 | $300.00 | $700.00 | $500 | $1500.00 | $27.50 | $115.14 |

| | | | | | | |
|---|---|---|---|---|---|---|
| 2 | 300.00 | 700.00 | 384.86 | 1384.86 | 26.06 | 116.58 |
| 3 | 300.00 | 700.00 | 268.28 | 1268.28 | 24.60 | 118.04 |
| 4 | 300.00 | 700.00 | 150.24 | 1150.24 | 23.13 | 119.51 |
| 5 | 300.00 | 700.00 | 30.73 | 1030.73 | 21.63* | 121.01 |
| 6 | 300.00 | 609.72 | … | 909.72 | 19.67 | 122.97 |
| 7 | 300.00 | 486.75 | … | 786.75 | 17.52 | 125.12 |
| 8 | 300.00 | 361.63 | … | 661.63 | 15.33 | 127.31 |
| 9 | 300.00 | 234.32 | … | 534.32 | 13.10 | 129.54 |
| 10 | 300.00 | 104.78 | … | 404.78 | 10.83 | 131.81 |
| 11 | 272.97 | … | … | 272.97 | 8.19 | 134.45 |
| 12 | 138.52 | … | … | 138.52 | 4.12** | 138.52 |
| | TOTALS... | ……... | ……... | ……... | $211.68 | $1500.00 |

* Finance Charge rates are applied to parts of Unpaid Principal Balances scheduled to be outstanding. For example, the Finance Charge on $1030.73 is computed as follows:

| | | | | | | |
|---|---|---|---|---|---|---|
| 1/12 | X | 36% | on | $ 300.00 | = | $ 9.00 |
| 1/12 | X | 21% | on | 700.00 | = | 12.25 |
| 1/12 | X | 15% | on | 30.73 | = | .38 |
| | | | | $1030.73 | | $21.63 |

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

For purposes of disclosure under the Truth in Lending Act the credit grantor must determine the single annual percentage rate, which, when applied according to the actuarial method, earns the same dollar amount of finance charge that is produced by the graduated rates. Table B shows that an annual rate of 25.10% applied monthly to the periodic declining unpaid balances produces the same total dollar charge of $211.68 calculated by application of graduated rates in Table A.

## TABLE B

Amortization Schedule for $1500 to be paid in 12 equal and consecutive monthly instalments of Principal Amount and Finance Charge combined showing that the Single Annual Percentage Rate of 25.10% computed by the Actuarial Method yields $211.68.

| Mo. | Unpaid Principal Balances | Application of $142.64 Monthly Payments: Charges | Principal |
|---|---|---|---|
| 1 | $1500.00 | $31.38 | $111.26 |
| 2 | 1388.74 | 29.05 | 113.59 |

| | | | |
|---|---|---|---|
| 3 | 1275.15 | 26.67 | 115.97 |
| 4 | 1159.18 | 24.25 | 118.39 |
| 5 | 1040.79 | 21.77 | 120.87 |
| 6 | 919.92 | 19.24 | 123.40 |
| 7 | 796.52 | 16.66 | 125.98 |
| 8 | 670.54 | 14.03 | 128.61 |
| 9 | 541.93 | 11.34 | 131.30 |
| 10 | 410.63 | 8.59 | 134.05 |
| 11 | 276.58 | 5.79 | 136.85 |
| 12 | 139.73 | 2.91* | 139.73 |
| TOTALS | …… | …..…..$211.68 | $1500.00 |

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

This Act is intended to give creditors the following choice in making their charges under Sections 2.201 and 2.401(2).

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

A precomputed transaction is subject to delinquency charges pursuant to Section 2.502 or deferral charges pursuant to Section 2.503 in case of delinquency or deferral and to rebate for prepayment pursuant to Section 2.510 in case of prepayment in full.

(2) The contract need not be precomputed, but may provide for: (a) the addition of finance charges, computed on unpaid balances of the principal amount, at the rates specified in Sections 2.201 and 2.401(2); in this case there is no rebate for prepayment in full because charges are collected only as earned, and there are no separate charges for default or deferment; or (b) not more than the maximum single annual percentage rate computed on actual unpaid balances for the actual time outstanding. The single annual percentage is the rate which yields the charge for payment according to schedule when the rate is computed according to the actuarial method. In the example, the rate is 25.10%. In this case there is no rebate for prepayment in full because the charges are collected only as earned, and there are no separate charges for default or deferment.

4. *Explanation of Section 2.201(6).* Subsection (6) of this section permits minimum charges equal to finance charges for which the CCPA (15 U.S.C. § 1601 et seq.) requires no annual percentage rate disclosure. The CCPA does not set limits on the amounts of minimum charges, but does require annual percentage rate disclosure when the minimum charges exceed those permitted by subsection (6). Subsection (6) also sets limits on the amounts of minimum charges.

5. *Operation of 18% APR finance charge ceiling.* According to tables furnished by

Financial Publishing Company, the 18% APR finance charge ceiling rate on unpaid balances of the amount financed permitted by subsection (2)(b) yields a greater finance charge than the sliding scale ceiling rates of 36%, 21% and 15% when applied to unpaid balances of the amount financed on amounts equal to or exceeding the following for the respective following number of equal monthly instalments (the corresponding Total of Payments, Finance Charge and amount of equal monthly instalments is set out below):

| No. of Monthly Instalments | Unpaid Balance of Amount to be Financed | Total of Payments | Finance Charge | Amount of Monthly Instalments |
|---|---|---|---|---|
| 3 | $5190.00 | $5346.51 | $156.51 | $1782.17 |
| 6 | 5853.00 | 6164.16 | 311.16 | 1027.36 |
| 9 | 5953.00 | 6408.45 | 455.45 | 712.15 |
| 12 | 6016.00 | 6618.72 | 602.72 | 551.56 |
| 15 | 6011.00 | 6757.50 | 746.50 | 450.50 |
| 18 | 5985.00 | 6874.02 | 889.02 | 381.89 |
| 24 | 5906.00 | 7076.64 | 1170.64 | 294.86 |
| 30 | 5800.00 | 7245.60 | 1445.60 | 241.52 |
| 36 | 5695.00 | 7412.40 | 1717.40 | 205.90 |
| 42 | 5594.00 | 7581.00 | 1987.00 | 180.50 |
| 48 | 5491.00 | 7742.88 | 2251.88 | 161.31 |
| 54 | 5393.00 | 7907.76 | 2514.76 | 146.44 |
| 60 | 5301.00 | 8077.20 | 2776.20 | 134.62 |
| 66 | 5209.00 | 8242.74 | 3033.74 | 124.89 |
| 72 | 5121.00 | 8410.32 | 3289.32 | 116.81 |
| 78 | 5041.00 | 8587.02 | 3546.02 | 110.09 |
| 84 | 4958.00 | 8754.48 | 3796.48 | 104.22 |
| 90 | 4882.00 | 8929.80 | 4047.80 | 99.22 |
| 96 | 4810.00 | 9108.48 | 4298.48 | 94.88 |
| 102 | 4741.00 | 9289.14 | 4548.14 | 91.07 |
| 108 | 4676.00 | 9473.76 | 4797.76 | 87.72 |
| 114 | 4615.00 | 9662.64 | 5047.64 | 84.76 |
| 120 | 4554.00 | 9848.40 | 5294.40 | 82.07 |

**§ 2.202. [Finance Charge for Consumer Credit Sales Pursuant to Open-End Credit]**

(1) With respect to a consumer credit sale pursuant to open-end credit, a creditor may contract for and receive a finance charge not exceeding that permitted in this section.

(2) For each billing cycle a finance charge may be made which is a percentage of an amount not exceeding the greatest of:

(a) the average daily balance of the open-end account in the billing cycle for which

the charge is made, which is the sum of the amount unpaid each day during that cycle, divided by the number of days in that cycle; the amount unpaid on a day is determined by adding to any balance unpaid as of the beginning of that day all purchases and other debits and deducting all payments and other credits made or received as of that day;

(b) the balance of the open-end account at the beginning of the first day of the billing cycle [after deducting all payments and credits made in the cycle except credits attributable to purchases charged to the account during the cycle]; or

(c) the median amount within a specified range including the balance of the open-end account not exceeding that permitted by paragraph (a) or (b); a finance charge may be made pursuant to this paragraph only if the creditor, subject to classifications and differentiations he may reasonably establish, makes the same charge on all balances within the specified range and if the percentage when applied to the median amount within the range does not produce a charge exceeding the charge resulting from applying that percentage to the lowest amount within the range by more than eight per cent of the charge on the median amount.

(3) If the billing cycle is monthly, the finance charge may not exceed an amount equal to two per cent of that part of the maximum amount pursuant to subsection (2) which is $500 or less and one and one-half per cent of that part of the maximum amount which is more than $500. If the billing cycle is not monthly, the maximum charge for the billing cycle shall bear the same relation to the applicable monthly maximum charge as the number of days in the billing cycle bears to 365 divided by 12. A billing cycle is monthly if the closing date of the cycle is the same date each month or does not vary by more than four days from the regular date. Without regard to the length of the billing cycle, the finance charge may be computed at a daily rate that does not exceed 1/365ths of 12 times the monthly charge permitted by this section for a billing cycle that is

monthly.

(4) If the finance charge determined pursuant to subsection (3) is less than 50 cents, a finance charge may be made which does not exceed 50 cents if the billing cycle is monthly or longer, or the pro rata part of 50 cents which bears the same relation to 50 cents as the number of days in the billing cycle bears to 365 divided by 12 if the billing cycle is shorter than monthly.

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

**COMMENT**

1. See Comment 1 to Section 2.201 for an explanation of the theory of rate regulation adopted by the Act.

2. Subsection (2) allows the creditor an option with respect to the balance on which the finance charge is imposed. The Federal Truth in Lending Act requires the creditor to disclose the method of determining the balance on which the finance charge is imposed (Regulation Z Section 226.7(a)(2) and (b)(8)). The average daily balance method authorized by paragraph (a) of subsection (2) is that commonly utilized by creditors employing electronic data processing equipment. Paragraph (b) of subsection (2), read with the bracketed material included, states the adjusted balance method under which the balance at the beginning of the cycle is reduced by all payments and credits during the cycle. Although under this method the balance is adjusted downward by payments and credits during the cycle, it is not adjusted upward by new purchases made within the cycle. The except clause is necessary to prevent the beginning balance from being reduced by returns of merchandise attributable to purchases made within the cycle the amounts of which had not been included in that balance. Paragraph (b) of subsection (2), read without the bracketed material, states the previous or beginning balance method under which the opening balance is neither decreased by payments or credits during the billing cycle nor increased by new purchases made during that period. Either the previous balance or the adjusted balance method is usable by a creditor with a manual system of entries. The brackets in paragraph (b) of subsection (2) acknowledge the as yet unresolved controversy in the Congress and the state legislatures about the comparative merit of the previous and adjusted balance methods.

3. See Comment 3 to Section 2.201 for a discussion of the median amount method of computing the balance on which the finance charge is imposed under paragraph (c) of subsection (2). The "classifications and differentiations" language in paragraph (c) is intended to give the seller some flexibility in using this method of determining the finance charge. The creditor need not use this method for all his customers nor need he use it for all his transactions with one customer, but he may classify his transactions and customers on reasonable bases.

4. In requiring a complex disclosure procedure if the maximum charge exceeds 50J per month (CCPA Section 127(b)(6), 15 U.S.C. § 1637(b)(6)), Congress indirectly recognized the fairness of the 50J minimum figure. This Act adopts the 50J limit in recognition of this Congressional guidance as well as the difficulties inherent in disclosing the annual percentage rate of a higher charge.

## PART 3

## CONSUMER LOANS: SUPERVISED LENDERS

### § 2.301. [Authority to Make Supervised Loans]

Unless a person is a supervised financial organization or has obtained a license from the Administrator authorizing him so to do, he may not engage in the business of:

(1) making supervised loans, or

(2) taking assignments of and undertaking direct collection of payments from or enforcement of rights against consumers arising from supervised loans, but he may collect and enforce for three months without a license if he promptly applies for a license and his application has not been denied.

### COMMENT

1. Since supervised financial organizations are already subject to supervision by a state or federal official or agency, such organizations are not required to obtain a license under this Act from the Administrator, but their powers may be limited by statutes other than this Act. Section 1.108. Other persons making supervised loans in this State or taking assignments of supervised loans for collection or enforcement in this State must obtain a license from the Administrator.

2. Out-of-state lenders who make loans through the mail normally will not be subject to the licensing requirement if the evidence of debt is received by the lender out of the enacting State; however, in such a case the lender may not exceed the rate ceilings of the enacting State and the Administrator may go into the lender's State and investigate potential violations pursuant to Part 1 of Article 6. See Section 1.201(1) and (2). An out-of-state lender who opens a loan office in this State at which evidence of debt for supervised loans is received must be licensed in this State.

3. If an unlicensed assignee not previously engaged in this State in the business of making collection or enforcing rights under the paper assigned to him undertakes collection or enforcement of rights, subsection (2) gives him a 3-month grace period during which he can operate before obtaining a license.

**§ 2.302. [License to Make Supervised Loans]**

(1) The Administrator shall receive and act on all applications for licenses to make supervised loans under this Act. Applications shall be in the form and filed in the manner prescribed by the Administrator and contain or be accompanied by the information the Administrator requires by rule.

(2) The Administrator may not issue a license unless upon investigation he finds that the financial responsibility, character, and fitness of the applicant, and of the members thereof if the applicant is a partnership or association or of the officers and directors thereof if the applicant is a corporation, warrant belief that the business will be operated honestly and fairly within the purposes of this Act. In determining the financial responsibility of an applicant proposing to engage in making insurance premium loans, the Administrator shall consider the liabilities the lender may incur for erroneous cancellation of insurance.

(3) Upon written request, the applicant is entitled to a hearing on the question of his qualifications for a license if (a) the Administrator notifies the applicant in writing that his application has been denied, or (b) the Administrator does not issue a license within 60 days after the application for the license was filed. A request for a hearing may not be made more than 15 days after the Administrator mails a writing to the applicant notifying him that the application has been denied and stating in substance the Administrator's findings supporting denial of the application.

(4) The Administrator shall issue additional licenses to the same licensee upon compliance

with all the provisions of this Act governing issuance of a single license. A separate license is required for each place of business. Each license remains in full force and effect until surrendered, suspended, or revoked.

(5) A licensee may not change the location of any place of business without giving the Administrator at least 15 days prior written notice.

(6) A licensee may conduct the business of making supervised loans only at or from a place of business for which he holds a license and only under the name in the license. Credit granted pursuant to a lender credit card does not violate this subsection.

**COMMENT**

1. This section is intimately related to the provisions on maximum finance charges (Parts 2 and 4 of Article 2) and disclosure (Part 2 of Article 3). A major objective of this Act is to facilitate entry into the cash loan field so that the resultant rate competition fostered by disclosure will generally force rates below the permitted maximum charges. To this end this section adopts a test of "financial responsibility, character and fitness" rather than the test of "convenience and advantage" often used in prior small loan laws. Competition is further encouraged by the absence of licensing requirements in consumer credit sales (Section 2.201) and in consumer loans not made by supervised lenders (subsection (1) of Section 2.401).

2. A secondary purpose is to reduce the likelihood of establishing localized monopolies in the granting of cash credit. Such monopolies tend to push rates charged to maximum permitted levels and to establish conditions under which some share of the anticipated monopoly profits are devoted to direct or indirect pressures to obtain the license.

3. This section does not apply to supervised financial organizations. Their authority to open new offices at which they may receive deposits and make loans is found not in this Act but in the statutes otherwise governing those organizations.

4. If increased competition should cause the development of undesirable credit practices, these practices are subject to controls by the Administrator's powers to revoke or suspend a license (Section 2.303), and by the other powers of the Administrator (Article 6) as well as by the provisions on remedies and penalties available to aggrieved consumers (Article 5).

5. Licensees must obtain a license for each place of business and may do business only at these locations. A lender credit card issuer does not conduct business at a place where a third person honors its card within the meaning of the section. There is no requirement that the license be renewed annually or that the licensee pay a fee for a license. Income for the operation of the

office of the Administrator is derived from general appropriations rather than from the licensing of supervised lenders. Annual fees are required by Section 6.203 of all persons required to file notification under Section 6.202, not just licensees. This includes all persons making consumer credit sales, consumer leases, or consumer loans and certain persons taking assignments of and undertaking direct collection of payments from or enforcement of rights against debtors arising from such sales, leases, or loans.

**§ 2.303. [Revocation or Suspension of License]**

(1) The Administrator may issue to a person licensed to make supervised loans an order to show cause why his license with respect to one or more specific places of business should not be suspended for a period not in excess of six months or be revoked. The order shall set a place for a hearing and a time therefor that is no less than ten days from the date of the order. After the hearing the Administrator shall revoke or suspend the license or, if there are mitigating circumstances, may accept an assurance of discontinuance (Section 6.109) and allow retention of the license, if he finds that:

(a) the licensee has repeatedly and intentionally violated this Act or any rule or order lawfully made pursuant to this Act, or has violated an assurance of discontinuance; or

(b) facts or conditions exist which clearly would have justified the Administrator in refusing to grant a license for that place or those places of business were these facts or conditions known to exist at the time the application for the license was made.

(2) A revocation or suspension of a license is not lawful unless the Administrator, before instituting proceedings, gives notice to the licensee of the facts or conduct which warrant the intended action, and the licensee is afforded an opportunity to show compliance with all lawful requirements for retention of the license.

(3) If the Administrator finds that probable cause for revocation of a license exists and that enforcement of this Act requires immediate suspension of the license pending investigation, he, after a hearing upon five days' written notice, may enter an order suspending the license for not

more than 30 days.

(4) Whenever the Administrator revokes or suspends a license, he shall enter an order to that effect and forthwith notify the licensee of the revocation or suspension. Within five days after entry of the order he shall deliver to the licensee a copy of the order and the findings supporting the order.

(5) A person holding a license to make supervised loans may relinquish the license by notifying the Administrator in writing of its relinquishment, but the relinquishment does not affect his liability for acts previously committed.

(6) Revocation, suspension, or relinquishment of a license does not impair or affect the obligation of any preexisting lawful contract between the licensee and any consumer.

(7) The administrator may reinstate or license, terminate a suspension, or grant a new license to a person whose license has been revoked or suspended if no fact or condition then exists which clearly would have justified the Administrator in refusing to grant a license.

**COMMENT**

This section provides the Administrator with a range of alternatives in cases in which creditors violate the Act. If after a noticed hearing the Administrator finds repeated and intentional violations, he may revoke the license, suspend the license for up to six months, or, if mitigating circumstances warrant, accept an assurance of discontinuance. Subsequent violation of the assurance of discontinuance may be a basis for revocation or suspension.

**§ 2.304. [Records; Annual Reports]**

(1) Every licensee shall maintain records in conformity with generally accepted accounting principles and practices in a manner that will enable the Administrator to determine whether the licensee is complying with this Act. The record keeping system of a licensee is sufficient if he makes the required information reasonably available. The records need not be kept in the place of business where supervised loans are made, if the Administrator is given free

access to the records wherever located. The records pertaining to any loan need not be preserved for more than two years after making the final entry relating to the loan, but in the case of open-end credit the two years are measured from the date of each entry.

(2) On or before April 15 each year every licensee shall file with the Administrator a composite annual report in the form prescribed by the Administrator relating to all supervised loans made by him. The Administrator shall consult with comparable officials in other states for the purpose of making the kinds of information required in annual reports uniform among the states. Information contained in annual reports shall be confidential and may be published only in composite form.

**COMMENT**

1. This section seeks to give to the licensee wide discretion in the method of keeping records. No rigid requirements are imposed with respect to the method of record keeping. Instead, records are acceptable if kept in accordance with generally accepted accounting principles, and if they enable the Administrator to determine whether the licensee is complying with the Act. Modern techniques frequently require that records be kept in one central place, which in the case of multi-state lenders may be outside the State. This section allows central record keeping and allows records to be kept anywhere so long as the Administrator is given free access to them. See Section 2.305(2).

2. Licensees are required to file composite annual reports; information need not be given as to individual loan outlets. This allows the Administrator to compile statistics to aid him in his duties and to provide the Legislature with information necessary for a proper evaluation of the effectiveness of the Act. This section provides for confidential treatment by the Administrator of information contained in annual reports. The Administrator may not publish information concerning individual lenders; all information published must be in composite form.

**§ 2.305. [Examinations and Investigations]**

(1) The Administrator shall examine periodically at intervals he deems appropriate the loans, business, and records of every licensee. In addition, for the purpose of discovering violations of this Act or securing information lawfully required, the Administrator or the official or agency to whose supervision the organization is subject (Section 6.105) at any time may

investigate the loans, business, and records of any lender. For these purposes he shall have free and reasonable access to the offices, places of business, and records of the lender.

(2) If the lender's records are located outside this State, the lender at his option shall make them available to the Administrator at a convenient location within this State, or pay the reasonable and necessary expenses for the Administrator or his representative to examine them where they are located. The Administrator may designate representatives, including comparable officials of the state in which the records are located, to inspect them on his behalf.

(3) For purposes of this section, the Administrator may administer oaths or affirmations, and upon request of a party or his own motion may subpoena witnesses, compel their attendance, adduce evidence, and require the production of any matter which is relevant to the investigation, including the existence, description, nature, custody, condition, and location of any books, documents, or other tangible things and the identity and location of persons having knowledge of relevant facts, or any other matter reasonably calculated to lead to the discovery of admissible evidence.

(4) Upon failure without lawful excuse to obey a subpoena or to give testimony and upon reasonable notice to all persons affected thereby, the Administrator may apply to the [ ] court for an order compelling compliance.

**COMMENT**

1. This section provides for periodic examinations of supervised lenders but there is no requirement of annual examinations. The Administrator may tailor his examination policy as he sees fit. With respect to other lenders who are not supervised lenders, the Act does not provide for periodic examinations; however, for the purpose of discovering violations of the Act or securing necessary information, investigations may be made by the Administrator, or in the case of supervised financial organizations, by the appropriate supervisory authority. Under Section 6.106 the Administrator has general authority to investigate any person who he has cause to believe has engaged in an act which is subject to action by the Administrator. The power of the Administrator with respect to lenders is somewhat broader than his general authority in that

investigations can be made without cause to believe a violation has occurred and are not restricted to the purpose of discovering violations.

2. Lenders are authorized to maintain records outside the State. The lender is given the option of making the records available to the Administrator within the State or paying the expenses of the Administrator to have them examined outside the State. Where records are kept outside the State the Act authorizes the examination to be made by officials of the state in which the records are kept. In that case these officials act as agents of the Administrator.

3. For the purpose of facilitating investigations, the Administrator is given wide powers, including the subpoena power and the power to require the giving of testimony under oath. These powers are similar to those given to the Administrator by Section 6.106. The Administrator may apply to the appropriate court for an order compelling compliance with his orders.

**§ 2.306. [Application of [Administrative Procedure Act] [Part on Administrative Procedure and Judicial Review] to Part]**

Except as otherwise provided, the [State administrative procedure act] [Part on Administrative Procedure and Judicial Review (Part 4) of the Article on Administration (Article 6) ] applies to and governs all administrative action taken by the Administrator pursuant to this Part.

**COMMENT**

If the State has an adequate State administrative procedure act reference should be made to it in this section. Otherwise Part 4 of Article 6 should be enacted and referred to here. Brackets and bracketed language in the section and its caption should be retained or deleted dependent upon which course is followed. See Comment to Section 6.401.

**§ 2.307. [Restrictions on Interest in Land as Security]**

(1) A lender may contract for an interest in land as security, except to secure a supervised loan in which the amount financed is $1,000 or less. A security interest taken in violation of this section is unenforceable to the extent of that loan.

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

## COMMENT

This section continues the policy recognized in a number of states of denying the lender in relatively small loan transactions the great leverage that results from a security interest in land. See Section 3.301 and the Comment thereto.

### § 2.308. [Regular Schedule of Payments; Maximum Loan Term]

(1) Supervised loans, not made pursuant to open-end credit and in which the amount financed is $1,000 or less, shall be scheduled to be payable in substantially equal instalments at substantially equal periodic intervals except to the extent that the schedule of payments is adjusted to the seasonal or irregular income of the debtor, and

(a) over a period not exceeding 37 months if the amount financed exceeds $300, or

(b) over a period not exceeding 25 months if the amount financed is $300 or less.

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

## COMMENT

This provision is similar to that commonly found in small loan laws requiring equal payments and a maximum loan term. Balloon payments are not permitted in supervised loans of $1,000 or less unless appropriate to meet the debtor's needs with respect to seasonal or irregular income. See Section 3.308.

### § 2.309. [No Other Business for Purpose of Evasion]

A supervised lender may not carry on other business for the purpose of evasion or violation of this Act at a location where he makes supervised loans.

## COMMENT

Some supervised lenders legitimately engage in transactions on their premises other than loaning money. For example, commercial banks typically sell their customers a variety of services with no purpose of violating provisions on maximum charges or other provisions of this Act. On the other hand, tie-in sales of goods or services in connection with loans are flagrant violations of this Act because they are carried on to evade rate ceilings.

PART 4

## CONSUMER LOANS: MAXIMUM FINANCE CHARGES

### § 2.401. [Finance Charge for Consumer Loans]

(1)With respect to a consumer loan, including a loan pursuant to open-end credit, a lender who is not a supervised lender may contract for and receive a finance charge, calculated according to the actuarial method, not exceeding 18 per cent per year. With respect to a consumer loan made pursuant to open-end credit, the finance charge shall be deemed not to exceed 18 per cent per year if the finance charge contracted for and received does not exceed a charge for each monthly billing cycle which is one and one-half per cent of the average daily balance of the open-end account in the billing cycle for which the charge is made. The average daily balance of the open-end account is the sum of the amount unpaid each day during that cycle divided by the number of days in the cycle. The amount unpaid on a day is determined by adding to any balance unpaid as of the beginning of that day all purchases, loans, and other debits and deducting all payments and other credits made or received as of that day. If the billing cycle is not monthly, the finance charge shall be deemed not to exceed 18 per cent per year if the finance charge contracted for and received does not exceed a percentage which bears the same relation to one and one-half per cent as the number of days in the billing cycle bears to 365 divided by 12. A billing cycle is monthly if the closing date of the cycle is the same date each month or does not vary by more than four days from the regular date.

(2) With respect to a consumer loan, including a loan pursuant to open-end credit, a supervised lender may contract for and receive a finance charge, calculated according to the actuarial method, not exceeding the equivalent of the greater of either of the following:

(a) the total of:

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

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

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

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

(3) This section does not limit or restrict the manner of calculating the finance charge, whether by way of add-on, discount, single annual percentage rate, or otherwise, so long as the rate of the finance charge does not exceed that permitted by this section. The finance charge may be contracted for and earned at the single annual percentage rate that would earn the same finance charge as the graduated rates when the debt is paid according to the agreed terms and the calculations are made according to the actuarial method. If the loan is a precomputed consumer credit transaction:

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

(b) the effect of prepayment is governed by the provisions on rebate upon prepayment (Section 2.510).

(4) Except as provided in subsection (6), the term of a loan for purposes of this section commences on the day the loan is made. Any month my be counted as 1/12th of a year, but a day is counted as 1/365th of a year. Subject to classifications and differentiations the lender may reasonably establish, a part of a month in excess of 15 days may be treated as a full month if

periods of 15 days or less are disregarded and that procedure is not consistently used to obtain a greater yield than would otherwise be permitted. The Administrator may adopt rules not inconsistent with the Federal Truth in Lending Act with respect to treating as regular other minor irregularities in amount or time.

(5) Subject to classifications and differentiations the lender may reasonably establish, he may make the same finance charge on all amounts financed within a specified range. A finance charge so made does not violate subsection (1) or (2) if:

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

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

(6) With respect to an insurance premium loan, the term of the loan commences on the earliest inception date of a policy or contract of insurance payment of the premium on which is financed by the loan.

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

**COMMENT**

1. For an extensive explanation of the purposes and operation of the rate ceilings provisions of this Act, see the Comment to Section 2.201. Subsection (1) sets the ceilings for all consumer loans not made by supervised lenders at 18% per annum, and this ceiling applies to open-end credit as well as to closed-end credit. The operation of open-credit is such that a creditor cannot know whether he is exceeding a rate ceiling stated in terms of a rate calculated according to the actuarial method unless he calculates the rate on daily balances. In "deeming" that 11/2% per month on the average daily balance is the equivalent of 18% per year, this subsection allows the creditor to use a somewhat simplified method of calculation.

2. The ceilings for loans by supervised lenders in subsection (2) also apply to open-end

credit. This enables supervised lenders to serve the needs of higher risk consumers by the use of credit cards and other open-end credit plans.

Lenders are not required to use a graduated rate, but may find it more economical to use a single annual rate provided that it does not exceed the rate ceiling specified. Lenders may not levy delinquency charges (Section 2.502) and deferral charges (Section 2.503) on open-end credit accounts. By the same token a debtor is not entitled to rebates upon prepayment with respect to open-end accounts since at the time of his prepayment there will be no unearned prepaid finance charges on the open-end account.

3. Subsection (6) makes specific provision for the time a loan commences with respect to an insurance premium loan. The term commences when the insurance first covers the consumer whether or not the loan proceeds have as yet been paid over by the creditor for the insurance.

## PART 5

## CONSUMER CREDIT TRANSACTIONS: OTHER CHARGES AND MODIFICATIONS

### § 2.501. [Additional Charges]

(1) In addition to the finance charge permitted by the parts of this Article on maximum finance charges for consumer credit sales and consumer loans (Parts 2 and 4), a creditor may contract for and receive the following additional charges:

(a) official fees and taxes;

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

(c) annual charges, payable in advance, for the privilege of using a credit card which entitles the cardholder to purchase or lease goods or services from at least 100 persons not related to the card issuer, under an arrangement pursuant to which the debts resulting from the purchases or leases are payable to the card issuer;

(d) with respect to a debt secured by an interest in land, the following "closing costs," if they are bona fide, reasonable in amount, and not for the purpose of circumvention or evasion of this Act:

(i) fees or premiums for title examination, abstract of title, title insurance, surveys, or similar purposes,

(ii) fees for preparation of a deed, settlement statement, or other documents, if not paid to the creditor or a person related to the creditor,

(iii) escrows for future payments of taxes, including assessments for improvements, insurance, and water, sewer and land rents, and

(iv) fees for notarizing deeds and other documents, if not paid to the creditor or a person related to the creditor; and

(e) charges for other benefits, including insurance, conferred on the consumer, if the benefits are of value to him and if the charges are reasonable in relation to the benefits, are of a type that is not for credit, and are authorized as permissible additional charges by rule adopted by the Administrator.

(2) An additional charge may be made for insurance written in connection with the transaction:

(a) with respect to insurance against loss of or damage to property, or against liability arising out of the ownership or use of property, if the creditor furnishes a clear, conspicuous, and specific statement in writing to the consumer setting forth the cost of the insurance if obtained from or through the creditor and stating that the consumer may choose the person through whom the insurance is to be obtained;

(b) with respect to consumer credit insurance providing life, accident, or health coverage, if the insurance coverage is not required by the creditor, and this fact is clearly and conspicuously disclosed in writing to the consumer, and if, in order to obtain the insurance in connection with the extension of credit, the consumer gives specific, dated, and separately signed

affirmative written indication of his desire to do so after written disclosure to him of the cost thereof; and

(c) with respect to vendor's single interest insurance, but only (i) to the extent that the insurer has no right of subrogation against the consumer, and (ii) to the extent that the insurance does not duplicate the coverage of other insurance under which loss is payable to the creditor as his interest may appear, against loss of or damage to property for which a separate charge is made to the consumer pursuant to paragraph (a), and (iii) if a clear, conspicuous, and specific statement in writing is furnished by the creditor to the consumer setting forth the cost of the insurance if obtained from or through the creditor and stating that the consumer may choose the person through whom the insurance is to be obtained.

**COMMENT**

1. The two categories of charges a creditor is permitted to make at the inception of a credit extension are finance charges (Section 1.301(20)) and additional charges as enumerated in this section. In general, the charges designated as additional charges fall roughly into three classes: (1) those that would likely have been incurred had there been no credit extension (*e.g.*, closing costs); (2) those closely related to the extension of credit but providing valuable subsidiary benefits to the consumer (*e.g.*, the front-end credit card charge; life, accident, health, and property insurance); and (3) those ultimately payable to third parties with no portion of the charge returnable to the creditor by commission or otherwise (*e.g.*, taxes; official fees for perfecting security interests). These classes are nonexclusive; for instance property insurance would sometimes fall within class (1) and closing costs fit into class (3) as well as in (1). Paragraph (e) of subsection (1) provides the Administrator with the flexibility needed to allow him to deal with new kinds of charges as new credit transactions evolve.

2. Though this section coincides with Regulation Z Section 226.4(a) in excluding premiums for insurance from the finance charge under certain stated conditions, it varies from Regulation Z Section 226.4(e) in that it does not include appraisal fees and credit report charges as additional charges. Section 1.301(20)(a)(iv) expressly designates these charges as part of the finance charge. Another variation from Truth in Lending is the treatment of vendor's single interest insurance (V.S.I.). Federal Reserve Interpretation 226.404 allows exclusion of the premium for V.S.I. insurance from the finance charge. Paragraph (c) of subsection (2) adopts a more sophisticated test and allows the premium to be treated as an additional charge in limited situations in which the vendor's single interest coverage does not duplicate the coverage of other insurance under which loss is payable to the creditor as his interest may appear, against loss of or damage to property for which a separate charge is made to the consumer. In this case, the charge

is sufficiently beneficial to the consumer to justify classifying the premium as in additional charge.

**§ 2.502. [Delinquency Charges]**

(1) With respect to a precomputed consumer credit transaction, the parties may contract for a delinquency charge on any instalment not paid in full within ten days after its due date, as originally scheduled or as deferred, in an amount, not exceeding $5, which is not more than five per cent of the unpaid amount of the instalment.

(2) A delinquency charge under subsection (1) may be collected only once on an instalment however long it remains in default. No delinquency charge may be collected with respect to a deferred instalment unless the instalment is not paid in full within ten days after its deferred due date. A delinquency charge may be collected at the time it accrues or at any time thereafter.

(3) A delinquency charge under subsection (1) may not be collected on an instalment paid in full within ten days after its scheduled or deferred instalment due date even though an earlier maturing instalment or a delinquency or deferral charge on an earlier instalment has not been paid in full. For purposes of this subsection a payment is deemed to have been applied first to any instalment due in the computational period (paragraph (a) of subsection (1) of Section 2.503) in which it is received and then to delinquent instalments and charges.

(4) If two instalments or parts thereof of a precomputed consumer loan are in default for ten days or more, the lender may elect to convert the loan from a precomputed loan to one in which the finance charge is based on unpaid balances. In this event he shall make a rebate pursuant to the provisions on rebate upon prepayment (Section 2.510) as if the date of prepayment were one day before the maturity date of a delinquent instalment, and thereafter may

make a finance charge as authorized by the provisions on finance charge for consumer loans by lenders not supervised lenders (subsection (1) of Section 2.401) or finance charge for consumer loans by supervised lenders (subsection (2) of Section 2.401), whichever is appropriate. The amount of the rebate shall not be reduced by the amount of any permitted minimum charge (Section 2.510). If the creditor proceeds under this subsection, any delinquency or deferral charges made with respect to instalments due at or after the maturity date of the first delinquent instalment shall be rebated, and no further delinquency or deferral charges shall be made.

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

**COMMENT**

1. If a consumer is late in making a payment under a precomputed credit transaction, the creditor would receive no income for the period of delay unless a delinquency charge were permitted. The alternative of not permitting delinquency charges is rejected because the result would be to enforce a lower effective ceiling on finance charge rates for delinquent consumers than for consumers who pay promptly. Delinquency charges are inapplicable to open-end credit plans under which the finance charge continues to accumulate through any period of delay thus compensating the creditor for this period.

2. The principal consumer abuse at which the section is aimed is that of precluding multiple delinquency charges stemming from a single delayed payment. Under law before this Act if the consumer's payments were due on the first of the month and the January payment of $100 was not made until the 15th, the creditor could assess a late payment of $5 (assuming that to be the correct figure under state law) and allocate the $100 payment received on February 1st, $95 to the February payment and $5 to the unpaid delinquency charge, thus causing the consumer to be delinquent in February as well. If the consumer made his $100 payment on time for each of the remaining months of the contract, he would incur a delinquency charge for each month remaining on the contract because of the rule allowing the creditor to allocate current payments to unpaid charges incurred in past periods. Subsection (3) meets this problem by compelling the creditor to apply the full $100 payment received on February 1 to the payment due that month. Hence, the creditor could collect the delinquency charge only for January if all other payments were made on time.

**§ 2.503. [Deferral Charges]**

(1) In this section and in the provisions on rebate upon prepayment (Section 2.510) the

following defined terms apply with respect to a precomputed consumer credit transaction:

(a) "Computational period" means (i) the interval between scheduled due dates of the instalments under the transaction if the intervals are substantially equal or, (ii) if the intervals are not substantially equal, one month if the smallest interval between the scheduled due dates of instalments under the transaction is one month or more, and, otherwise, one week.

(b) "Deferral" means a postponement of the scheduled due date of an instalment as originally scheduled or as previously deferred.

(c) "Deferral period" means a period in which no instalment is scheduled to be paid by reason of a deferral.

(d) The "interval" between specified dates means the interval between them including one or the other but not both of them; if the interval between the date of a transaction and the due date of the first scheduled instalment does not exceed one month by more than 15 days when the computational period is one month, or does not exceed 11 days when the computational period is on week, the interval may be considered by the creditor as one computational period.

(e) "Periodic balance" means the amount scheduled to be outstanding on the last day of a computational period before deducting the instalment, if any, scheduled to be paid on that day.

(f) "Standard deferral" means a deferral with respect to a transaction made as of the due date of an instalment as scheduled before the deferral by which the due dates of that instalment and all subsequent instalments as scheduled before the deferral are deferred for a period equal to the deferral period. A standard deferral may be for one or more full computational periods or a portion of one computational period or a combination of any of these.

(g) "Sum of the balances method," also known as the "Rule of 78," means a method employed with respect to a transaction to determine the portion of the finance charge attributable to a period of time before the scheduled due date of the final instalment of the transaction. The amount so attributable is determined by multiplying the finance charge by a fraction the numerator of which is the sum of the periodic balances included within the period and the denominator of which is the sum of all periodic balances under the transaction. According to the sum of the balances method the portion of the finance charge attributable to a specified computational period is the difference between the portions of the finance charge attributable to the periods of time including and excluding, respectively, the computational period, both determined according to the sum of the balances method.

(h) "Transaction" means a precomputed consumer credit transaction unless the context otherwise requires.

(2) Before or after default in payment of a scheduled instalment of a transaction, the parties to the transaction may agree in writing to a deferral of all or part of one or more unpaid instalments and the creditor may make at the time of deferral and receive at that time or at any time thereafter a deferral charge not exceeding that provided in this section.

(3) A standard deferral may be made with respect to a transaction as of the due date, as originally scheduled or as deferred pursuant to a standard deferral, of an instalment with respect to which no delinquency charge (Section 2.502) has been made or, if made, is deducted from the deferral charge computed according to this subsection. The deferral charge for a standard deferral may equal but not exceed the portion of the finance charge attributable to the computational period immediately preceding the due date of the earliest maturing instalment deferred as determined according to the sum of the balances method multiplied by the whole or fractional

number of computational periods in the deferral period, counting each day as 1/30th of a month without regard to differences in lengths of months when the computational period is one month or as 1/7th of a week when the computation period is one week. A deferral charge computed according to this subsection is earned pro rata during the deferral period and is fully earned on the last day of the deferral period.

(4) With respect to a transaction as to which a creditor elects not to make and does not make a standard deferral or a deferral charge for a standard deferral, a deferral charge computed according to this subsection may be made as of the due date, as scheduled originally or as deferred pursuant to either subsection (3) or this subsection, of an instalment with respect to which no delinquency charge (Section 2.502) has been made or, if made, is deducted from the deferral charge computed according to this subsection. A deferral charge pursuant to this subsection may equal but not exceed the rate of finance charge required to be disclosed to the consumer pursuant to law applied to each amount deferred for the period for which it is deferred computed without regard to differences in lengths of months, but proportionately for a part of a month, counting each day as 1/30th of a month or as 1/7th of a week. A deferral charge computed according to this subsection is earned pro rata with respect to each amount deferred during the period for which it is deferred.

(5) In addition to the deferral charge permitted by this section, a creditor may make and receive appropriate additional charges (Section 2.501), and any amount of these charges which is not paid may be added to the deferral charge computed according to subsection (3) or to the amount deferred for the purpose of computing the deferral charge computed according to subsection (4).

(6) The parties may agree in writing at the time of a transaction that, if an instalment is not

paid within ten days after its due date, the creditor may unilaterally grant a deferral and make charges as provided in this section. A deferral charge may not be made for a period after the date that the creditor elects to accelerate the maturity of the transaction.

## COMMENT

1. The definitions in subsection (1) apply to Section 2.510 as well. See subsection (3) of Section 2.510.

2. These definitions and the other provisions of this section can be illustrated more readily than explained.

Assume the loan transaction specified in the example in Comment 2 to Section 2.201, and that the loan is made on July 1, 1974. It is then a "precomputed consumer credit transaction" (subsections (13) and (33) of Section 1.301), *e.g.,* a "consumer loan" (subsection (15) of Section 1.301), of which the "amount financed" (subsection (5) of Section 1.301) is $1500, the "finance charge" (subsection (20) of Section 1.301) is $211.68, computed at an annual percentage rate of 25.10%, and the "total of payments" is $1711.68 and is payable in 12 equal monthly instalments of $142.64 each beginning on Aug. 1, 1974, and ending on July 1, 1975.

The "computational period" (paragraph (a) of subsection (1) of this section) is one month. The "periodic balances" (paragraph (e) of subsection (1) of this section) of, and other calculations applicable to, the transaction are

| Col. 1 | Col. 2 | Col. 3 | Col. 4 | Col. 5 | Col. 6 |
|---|---|---|---|---|---|
| Inst. No. | Inst. Due Date & Last Day of Each Comptnl. Period | Periodic Balances | Col. 3 / $11,125.92 | Sum of Periodic Balances | Col. 5 / $11,125.92 |
| 1 | Aug. 1, 1974 | $1,711.68 | 12/78 | $1,711.68 | 12/78 |
| 2 | Sept. 1, 1974 | 1,569.04 | 11/78 | 3,280.72 | 23/78 |
| 3 | Oct. 1, 1974 | 1,426.40 | 10/78 | 4,707.12 | 33/78 |
| 4 | Nov. 1, 1974 | 1,283.76 | 9/78 | 5,990.88 | 42/78 |
| 5 | Dec. 1, 1974 | 1,141.12 | 8/78 | 7,132.00 | 50/78 |
| 6 | Jan. 1, 1975 | 998.48 | 7/78 | 8,130.48 | 57/78 |
| 7 | Feb. 1, 1975 | 855.84 | 6/78 | 8,986.32 | 63/78 |
| 8 | Mar. 1, 1975 | 713.20 | 5/78 | 9,699.52 | 68/78 |
| 9 | Apr. 1, 1975 | 570.56 | 4/78 | 10,270.08 | 72/78 |
| 10 | May 1, 1975 | 427.92 | 3/78 | 10,698.00 | 75/78 |
| 11 | June 1, 1975 | 285.28 | 2/78 | 10,983.28 | 77/78 |
| 12 | July 1, 1975 | 142.64 | 1/78 | 11,125.92 | 78/78 |
| 78 | | $11,125.92 | 78/78 | | |

Col. 4 sets forth the fraction of the finance charge earned in each computational period as

computed according to the "sum of the balances method" (paragraph (g) of subsection (1) of this section). Col. 6 sets forth the fraction of the finance charge earned at the end of each computational period, also computed according to the sum of the balances method.

It will be noted that the fractions in Col. 4 and Col. 6, respectively, express more simply the fractions:

$$\frac{\text{Periodic balance}}{\text{Sum of all periodic balances under the transactionlb6}}.$$

and

$$\frac{\text{Sum of all periodic balances including computational period}}{\text{Sum of all periodic balances under the transaction}}$$

According to the "sum of the balances method" (paragraph (g) of subsection (1) of this section) the portion of the finance charge attributable to a period of time prior to the scheduled due date of the final instalment of the transaction is determined by multiplying the finance charge by a fraction the numerator of which is the sum of the periodic balances included within the period and the denominator is the total of all periodic balances under the transaction. Accordingly, in the assumed example, the portions of the total finance charge of $211.68 attributable to the periods ending, respectively, on Jan. 1, 1975, and Feb. 1, 1975, are 57/78ths and 63/78ths. Moreover, according to the "sum of the balances method" (the last sentence of paragraph (g) of subsection (1) of this section), the portion of the finance charge attributable to a specified computational period is the difference between the portions of the finance charge attributable to the periods of time including and excluding, respectively, that computational period; accordingly, in the assumed example the portion of the finance charge of $211.68 attributable to the computational period ending on Feb. 1, 1975, is 6/78ths (.e., 63/78ths minus 57/78ths) of $211.68, or $16.28.

3. Assume, further, that the consumer has paid the first 6 instalments, and that the parties have agreed to the deferral of the 7th instalment of $142.64 originally scheduled to be payable on Feb. 1, 1975, by 6 months until Aug. 1, 1975, or its equivalent, a deferral of the 7th and each of the five subsequent instalments of $142.64 each by one month each so that the 12th instalment originally scheduled for July, 1975 is payable on Aug. 1, 1975. The deferral is then a "standard deferral" (paragraph (f) of subsection (1) of this section) and the maximum deferral charge under subsection (3) of this section is $16.28, the finance charge so attributable to the computational period ending on Feb. 1, 1975, since the number of computational periods in the deferral period, the period in which no instalment is scheduled to be paid by reason of the deferral (paragraph (c) of subsection (1) of Section 2.503), is one.

The method of calculating deferral charges prescribed in subsection (3) of this section is that prescribed in the small loan laws of many States, e.g., New York Banking Law § 352(d)(4).

Were the deferral charge to be computed by the application of the annual percentage rate of 25.10% (or 2.09 1/6% per month) to each amount deferred for the period of its deferral, as

provided in U3C (1968 Draft) Sections 2.204(1) and 3.204(1) or subsection (4) of this section, the deferral charge would be $142.64 X 6 X .0209 X 1/6 = $17.90, or $1.62 more than the deferral charge of $16.28 as calculated according to subsection (3) of this section.

4. Under subsection (4) of this section if the creditor elects not to make and does not make a "standard deferral" (paragraph (f) of subsection (1) of this section) or a deferral charge for a standard deferral, the maximum deferral charge may be computed at the rate of finance charge applying to the transaction, i.e., the rate required to be disclosed to the consumer pursuant to law and, in the assumed example, 25.10% per annum upon each amount deferred for the period it is deferred.

5. Under subsection (2) of this section, the agreement of the parties for deferral and for deferral charges must be in writing and may be made before or after default in the payment of a scheduled instalment and the deferral charge may be made and received by the creditor at the time of or after the deferral.

"Before" in subsection (2) means either "at the time of the transaction" as provided in subsection (6), or later at any time before default. However, if the agreement is made at the time of the transaction or before the default, the creditor may not make the deferral until 10 days after default. In both cases, the deferral charge begins to accrue on the due date of the instalment which is in default or unpaid.

6. Under subsection (5) of this section, the creditor may make and receive appropriate additional charges (Section 2.501) and add them to the deferral charges computed according to subsection (3) or to the amount deferred for the computation of the deferral charges computed according to subsection (4).

7. Under subsection (6) of this section, the parties may agree in writing at the time of a precomputed consumer credit transaction that the creditor may unilaterally grant a deferral and make deferral charges as provided in this section if an instalment is not paid within 10 days after its due date. No deferral charge may be made for a period after the creditor elects to accelerate the maturity of a transaction.

**§ 2.504. [Finance Charge on Refinancing]**

With respect to a consumer credit transaction except a consumer lease, the creditor by agreement with the consumer may refinance the unpaid balance and contract for and receive a finance charge based on the amount financed resulting from the refinancing at a rate not exceeding that permitted by the provisions on finance charge for consumer credit sales other than open-end credit (Section 2.201) if a consumer credit sale is refinanced, or for consumer loans (subsection (1) or (2) of Section 2.401, whichever is appropriate) if a consumer loan is

refinanced. For the purpose of determining the finance charge permitted, the amount financed resulting from the refinancing comprises the following:

(1) if the transaction was not precomputed, the total of the unpaid balance and the accrued charges on the date of the refinancing, or, if the transaction was precomputed, the amount which the consumer would have been required to pay upon prepayment pursuant to the provisions on rebate upon prepayment (Section 2.510) on the date of refinancing, but for the purpose of computing this amount no minimum charge is permitted; and

(2) appropriate additional charges (Section 2.501), payment of which is deferred.

**COMMENT**

This section provides the method of obtaining the amount financed on which the finance charge is based when a consumer credit sale or consumer loan is refinanced, and sets the ceiling for the charge. In the refinancing of a precomputed transaction the balance owing is treated as though it is prepaid and the consumer is credited with all refunds computed, except that minimum charges permitted under Section 2.510(2) for prepayments of precomputed transactions are not allowed in refinancing in order to remove any incentive the creditor may have to "flip" the consumer through repeated refinancings. A finance charge is then calculated on an amount financed which is the balance owing less refunds. If the refinanced transaction is not precomputed no refunds need be credited to the consumer, and the amount financed is found merely by taking the unpaid balance and accrued charges at the date of refinancing.

**§ 2.505. [Finance Charge on Consolidation]**

(1) In this section "consumer credit transaction" does not include a consumer lease.

(2) If a consumer owes an unpaid balance to a creditor with respect to a consumer credit transaction and becomes obligated on another consumer credit transaction with the same creditor, the parties may agree to a consolidation resulting in a single schedule of payments. If the previous consumer credit transaction was not precomputed, the parties may agree to add the unpaid amount of the amount financed and accrued charges on the date of consolidation to the amount financed with respect to the subsequent consumer credit transaction. If the previous

consumer credit transaction was precomputed, the parties may agree to refinance the unpaid balance pursuant to the provisions on refinancing (Section 2.504) and to consolidate the amount financed resulting from the refinancing by adding it to the amount financed with respect to the subsequent consumer credit transaction. In either case the creditor may contract for and receive a finance charge as provided in subsection (3) based on the aggregate amount financed resulting from the consolidation.

(3) If the debts consolidated arise exclusively from consumer credit sales, the transaction is a consolidation with respect to a consumer credit sale and the creditor may make a finance charge not exceeding that permitted by the provisions on finance charge for consumer credit sales other than one-end credit (Section 2.201). If the debts consolidated include a debt arising from a prior or contemporaneous consumer loan, the transaction is a consolidation with respect to a consumer loan and the creditor may make a finance charge not exceeding that permitted by the provisions on finance charge for consumer loans by lenders not supervised lenders (subsection (1) of Section 2.401) or consumer loans by supervised lenders (subsection (2) of Section 2.401), whichever is appropriate.

(4) If a consumer owes an unpaid balance to a creditor with respect to a consumer credit transaction arising out of a consumer credit sale, and becomes obligated on another consumer credit transaction arising out of another consumer credit sale by the same seller, the parties may agree to a consolidation resulting in a single schedule of payments either pursuant to subsection (2) or by adding together the unpaid balances with respect to the two sales.

**COMMENT**

This section permits two methods of consolidating balances arising from different transactions. Subsection (2) permits the familiar "rewrite:" the old balance is refinanced under Section 2.504 and added to the amount financed under the new transaction. The finance charge

is based on the aggregate amounts financed. Under subsection (4) no refinancing entailing a refund of finance charge is involved. The balance owing are simply added together and made payable on one schedule of payments. This usually means that the maturity of the first transaction is extended.

**§ 2.506. [Advances to Perform Covenants of Consumer]**

(1) If the agreement with respect to a consumer credit transaction other than a consumer lease contains covenants by the consumer to perform certain duties pertaining to insuring or preserving collateral and the creditor pursuant to the agreement pays for performance of the duties on behalf of the consumer, he may add the amounts paid to the debt. Within a reasonable time after advancing any sums, he shall state to the consumer in writing the amount of sums advanced, any charges with respect to this amount, and any revised payment schedule and, if the duties of the consumer performed by the creditor pertain to insurance, a brief description of the insurance paid for by the creditor including the type and amount of coverages. Further information need not be given.

(2) A finance charge may be made for sums advanced pursuant to subsection (1) at a rate not exceeding the rate of finance charge required to be stated to the consumer pursuant to law in a disclosure statement, but with respect to open-end credit the amount of the advance may be added to the unpaid balance of the debt and the creditor may make a finance charge not exceeding that permitted by the appropriate provisions on finance charge for consumer credit sales pursuant to open-end credit (Section 2.202) or for consumer loans (subsection (1) or (2) of Section 2.401), whichever is appropriate.

**COMMENT**

If the agreement so provides the creditor may add to the debt sums that he pays for the performance of duties on behalf of the consumer. If he does so he must disclose the details of the transaction to the consumer. If the original transaction was made pursuant to open-end credit, the creditor may add the amount of the advance to the unpaid balance of the account. In other cases the creditor may make a finance charge on these additional amounts at a rate not in

excess of the rate disclosed to the consumer for the original transaction. Normally he would compute this charge for the remaining period of the credit term, and increase the amounts of the consumer's remaining payments accordingly.

*Alternative A:*

**§ 2.507. [Attorney's Fees]**

With respect to a consumer credit transaction, the agreement may not provide for payment by the consumer of attorney's fees. A provision in violation of this section is unenforceable.

**COMMENT**

This Act not only places limitations on the amount that a creditor may charge a consumer for credit at the time the agreement is entered into (Parts 2 and 4 of Article 2) but also on the amount that he may charge a defaulting consumer for collecting from him (e.g., this section and Section 3.402). In providing that no charge may be made for attorney's fees, this section reflects a policy decision to follow some small loan acts in treating this expense, like other collection costs, as part of the creditor's cost of doing business, rather than as a charge to be imposed on the defaulting consumer. The provisions made in this Act for rate ceilings and additional charges are generous enough to justify this treatment of attorney's fees and collection costs as part of general overhead.

*Alternative B:*

**§ 2.507. [Attorney's Fees]**

(1) With respect to a consumer loan in which the finance charge calculated according to the actuarial method is more than 18 per cent per year, the agreement may not provide for payment by the consumer of attorney's fees:

(a) if the loan is not pursuant to open-end credit and the amount financed is $1,000 or less; or

(b) if the loan is pursuant to open-end credit and the balance of the account at the time of default is $1,000 or less.

A provision in violation of this subsection is unenforceable.

(2) With respect to any other consumer credit transaction, the agreement may provide for

payment by the consumer of reasonable attorney's fees not in excess of 15 per cent of the unpaid debt after default and referral to an attorney not a salaried employee of the creditor. A provision in violation of this subsection is unenforceable.

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

**COMMENT**

This Act not only places limitations on the amount that a creditor may charge a consumer for credit at the time the agreement is entered into (*e.g.*, Parts 2 and 4 of Article 2) but also on the amount that he may charge a defaulting consumer for collecting from him (*e.g.*, this section and Section 3.402). In providing in subsection (1) that no charge may be made for attorney's fees in supervised loans of $1,000 or less this section follows some small loan acts in treating this expense, like other collection costs, as part of the creditor's cost of doing business, rather than as a charge to be imposed on the defaulting consumer. Subsection (2) reflects a policy decision in other consumer transactions of treating attorney's fees not as part of the creditor's general overhead to be indirectly borne by all of his customers but as a charge to be imposed, at least in part, on the defaulting consumer who gives rise to the expense. This section allows the parties to agree that upon default and referral of the claim to an attorney a charge can be made. However, the charge may not exceed 15% of the unpaid debt at the time of default for reasonable attorney's fees actually incurred. There is no requirement that the attorney must file suit against the consumer to earn the fee.

**§ 2.508. [Conversion to Open-End Credit]**

The parties may agree at or within ten days before the time of conversion to add the unpaid balance of a consumer credit transaction, except a consumer lease, not made pursuant to open-end credit to the consumer's open-end credit account with the creditor. The unpaid balance so added is an amount equal to the amount financed determined according to the provisions on finance charge on refinancing (Section 2.504).

**COMMENT**

The parties may agree to add a closed-end consumer loan or consumer credit sale to an open-end credit account. This section provides that the loan or sale is treated as refinanced at the time of the conversion and the unpaid balance resulting from the refinancing is added to the open-end credit account. Since the agreement must be entered into within 10 days prior to the

time of conversion, a clause in the original credit agreement would not be effective to authorize a conversion occurring more than 10 days after the agreement.

**§ 2.509. [Right to Prepay]**

Subject to the provisions on rebate upon prepayment (Section 2.510), the consumer may prepay in full the unpaid balance of a consumer credit transaction, except a consumer lease, at any time without penalty.

**COMMENT**

This section does not apply to real property credit transactions in which the finance charge does not exceed 12% because these are not consumer credit transactions. Sections 1.301(12) and 1.301(15). Nor does the consumer have the right to receive a rebate upon making a partial prepayment without the consent of the creditor. Application of the provisions on rebate upon prepayment (Section 2.510) is not the exaction of a penalty by a creditor within the meaning of this section.

**§ 2.510. [Rebate Upon Prepayment]**

(1) Except as otherwise provided in this section, upon prepayment in full of a precomputed consumer credit transaction, the creditor shall rebate to the consumer an amount not less than the unearned portion of the finance charge computed according to this section. If the rebate otherwise required is less than $1, no rebate need be made.

(2) Upon prepayment of a consumer credit transaction, whether or not precomputed, except a consumer lease or one pursuant to open-end credit, the creditor may collect or retain a minimum charge not exceeding $5 in a transaction which had an amount financed of $75 or less, or not exceeding $7.50 in a transaction which had an amount financed of more than $75, if the minimum charge was contracted for and the finance charge earned at the time of prepayment is less than the minimum charge contracted for.

(3) In the following subsections these terms have the meanings ascribed to them in subsection (1) of Section 2.503: computational period, deferral, deferral period, periodic balance,

standard deferral, sum of the balances method, and transaction.

(4) If, with respect to a transaction payable according to its original terms in no more than [48] instalments, the creditor has made either:

(a) no deferral or deferral charge, the unearned portion of the finance charge is no less than the portion thereof attributable according to the sum of the balances method to the period from the first day of the computational period following that in which prepayment occurs to the scheduled due date of the final instalment of the transaction; or

(b) a standard deferral and a deferral charge pursuant to the provisions on a standard deferral, the unpaid balance of the transaction includes any unpaid portions of the deferral charge and any appropriate additional charges incident to the deferral, and the unearned portion of the finance charge is no less than the portion thereof attributable according to the sum of the balances method to the period from the first day of the computational period following that in which prepayment occurs except that the numerator of the fraction is the sum of the periodic balances, after rescheduling to give effect to any standard deferral, scheduled to follow the computational period in which prepayment occurs. A separate rebate of the deferral charge is not required unless the unpaid balance of the transaction is paid in full during the deferral period, in which event the creditor shall also rebate the unearned portion of the deferral charge.

(5) In lieu of computing a rebate of the unearned portion of the finance charge as provided in subsection (4) of this section, the creditor:

(a) shall, with respect to a transaction payable according to its original terms in more than [48] instalments, and a transaction payable according to its original terms in no more than [48] instalments as to which the creditor has made a deferral other than a standard deferral, and

(b) may, in other cases,

recompute or redetermine the earned finance charge by applying, according to the actuarial method, the annual percentage rate of finance charge required to be disclosed to the consumer pursuant to law to the actual unpaid balances of the amount financed for the actual time that the unpaid balances were outstanding as of the date of prepayment, giving effect to each payment, including payments of any deferral and delinquency charges, as of the date of the payment. The Administrator shall adopt rules to simplify the calculation of the unearned portion of the finance charge, including allowance of the use of tables or other methods derived by application of a percentage rate which deviates by not more than one-half of one per cent from the rate of the finance charge required to be disclosed to the consumer pursuant to law, and based on the assumption that all payments were made as originally scheduled or as deferred.

(6) Except as otherwise provided in subsection (5), this section does not preclude the collection or retention by the creditor of delinquency charges (Section 2.502).

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

(8) Upon prepayment in full of a precomputed consumer credit transaction by the proceeds of consumer credit insurance (Section 4.103), the consumer or his estate is entitled to the same rebate as though the consumer had prepaid the agreement on the date the proceeds of insurance are paid to the creditor, but no later than 20 business days after satisfactory proof of loss is furnished to the creditor.

**COMMENT**

1. This section uses terms defined in Section 2.503. For illustrations of those terms, see the Comment to that section.

2. Upon prepayment in full of a precomputed consumer credit transaction, subsection (1)

of this section requires the creditor to rebate to the consumer the unearned portion of the finance charge computed according to this section if the rebate amounts to $1 or more.

3. Subsection (2) of this section permits the creditor to collect or retain specified minimum charges upon prepayment of any consumer credit transaction, whether or not precomputed, if the minimum charge is contracted for and if the finance charge earned at the time of prepayment is less than the minimum charge. The permitted minimum charges specified ($5 if the amount financed is $75 or less, or $7.50 if the amount financed is more than $75) are those for which Regulation Z Section 226.8(b)(2) requires no annual percentage rate disclosure.

4. Subsection (4) of this section prescribes a method for computing the unearned portion of the finance charge and hence the rebate upon prepayment of a transaction payable according to its original terms in no more than [48] instalments as to which the creditor has made either no deferral or a "standard deferral" and a deferral charge according to the provisions applying to a standard deferral.

Assume the transactions described in Comment 2 to Section 2.201 and in Comments 2 and 3 to Section 2.503. Assume, further, that the consumer has paid not only $855.84, the total of the first six monthly instalments payable before the deferral, but also the deferral charge of $16.28, calculated according to subsection (3) of Section 2.503, $285.28, the total of the 7th and 8th instalments of $142.64 each payable as deferred in Mar. 1 and Apr. 1, 1975, and has prepaid on Apr. 15, 1975, $570.56, the then unpaid balance of his "total of payments." His total payments then aggregate $1,727.96. Then:

(1) According to subsection (4) of this section, the fraction of the finance charge of $211.68 to be used to determine the rebate is the fraction of which the numerator is the sum of periodic balances as rescheduled pursuant to the deferral, viz., $1,426.40 (the total of $570.56, $427.92, $285.28, and $142.64 payable as deferred on the 1st days of May, June, July, and August, 1975, respectively) divided by $11,125.92 (the sum of all the periodic balances under the original transaction). The fraction then is $1,426.40/11,125.92, or dividing both numerator and denominator by $142.64 (the amount of each instalment), 10/78. The rebate, the unearned portion of the total finance charge of $211.68, is $211.68 X 10/78 = $27.14.

(2) Deducting $27.14 from $1,727.96, the total paid on the transaction by the consumer, produces $1,700.82 as its net cost to the consumer.

Make the same assumptions as above, except that the deferral charge has been computed according to U3C (1968 Draft) Sections 2.204(1) and 3.204(1) or according to subsection (4) of Section 2.503 of this Act. His total payments then aggregate $1,729.58, the total of $1,711.68 (12 payments of $142.64 each) and the deferral charge of $17.90 calculated according to subsection (4) of Section 2.503. Then were the unearned portions of the finance charge and the deferral charge to be computed separately as formerly required by U3C (1968 Text) Sections 2.210(6) and 3.210(6):

(1) The unearned portion of the finance charge would have been computed without regard to the deferral, *i.e.,* as the fraction of which the numerator is $855.84 (the total of the four

prepaid periodic balances of $427.92, $285.28, and $142.64, and $00., as originally scheduled) and the denominator is $11,125.92 (the total of the 12 periodic balances as originally scheduled), or $855.84/$11,125.92, or, dividing both the numerator and the denominator by $142.64 (the amount of each instalment), 6/78. The rebate, the unearned portion of the finance charge of $211.68, is $211.68 X 6/78 = $16.28.

(2) As noted in Comment 3 to Section 2.503, the deferral charge, calculated as provided in U3C (1968 Draft) Sections 2.204(1) and 3.204(1), was $17.90. The unearned portion of that deferral charge is the fraction of which the numerator is four (the number of instalments remaining to earn the deferral charge) and the denominator is six (the number of instalments deferred). The unearned portion of the deferral charge of $17.90 is $17.90 X 4/6 = $11.93.

(3) Deducting $28.21, the total of (a) $16.28, the unearned portion of the finance charge, and (b) $11.93, the unearned portion of the deferral charge, from $1,729.58, the total paid by the consumer, produces $1,701.37 as the net cost of the transaction to the consumer.

Consequently, the methods of calculating deferral charges according to subsection (3) of Section 2.503 of this Act and rebate of unearned finance charge according to subsection (4) of this Section not only permit more simple calculations, but also produce a lower cost to the consumer than under the corresponding provisions of the 1968 Draft of the U3C, viz. under the illustrations above, $1,700.82 as compared to $1,701.37.

5. Subsection (4) of this section permits the "sum of the balances method" or the "Rule of 78 method" of calculating the unearned portion of the finance charge when the transaction according to its original terms was payable in no more than [48] instalments and when there has been either no deferral or a "standard deferral." It thus permits under those circumstances the relatively simple method of calculating rebate upon prepayment commonly provided for in "small loan" acts.

6. Subsection (5) requires the unearned finance charge to be calculated as the excess of this charge over that earned according to the actuarial method (subsection (1) of Section 1.301) before the computational period following that in which prepayment occurs:

(1) when the transaction according to the original terms was payable in more than [48] instalments; or

(2) when there has been a deferral other than a standard deferral with respect to a transaction payable according to its original terms in no more than [48] instalments.

Subsection (5) also gives the creditor the option of using the actuarial method in all other cases.

The [48] instalment provision recognizes that the calculation of rebates according to the actuarial method produces a higher rebate to the consumer than the sum of the balances method particularly in the case of a transaction payable in a large number of instalments and prepaid shortly after the date of its inception.

Subsection (5) also requires the Administrator to adopt rules to simplify the calculation of the unearned portion of the finance charge, including allowance of the use of tables or other methods.

7. Except as provided in subsection (5), subsection (6) of this section does not preclude collection or retention of delinquency charges (Section 2.502).

8. Subsection (7) of this section entitles the consumer to the same rebate calculated as of the date of entry of judgment if maturity is accelerated and judgment is entered.

9. Subsection (8) of this section provides for a rebate computed according to this section if a precomputed consumer credit transaction is prepaid by proceeds of consumer credit insurance calculated as of the date of payment of the proceeds to the creditor, but no later than 20 days after satisfactory proof of loss is furnished to him.

**NOTE**

The following Administrator's rule is suggested to carry out the direction in the last sentence of subsection (5):

In accordance with the provisions of the last sentence of subsection (5) of Section 2.510, the creditor may calculate the unearned portion of the finance charge as follows:

(1) The unearned portion of the finance charge shall be no less than the excess of the finance charge over the portion thereof attributable according to the actuarial method at, as the creditor elects, either the rate required to be disclosed to the consumer pursuant to law or at that rate rounded to the nearest l1p/2 of 1%, to the period before the first day of the computational period following that in which prepayment occurs, determined without regard to any deferral.

(2) Each instalment which was payable as originally scheduled or as deferred before the date of prepayment and which either was paid before its due date as so scheduled or deferred or as to which a delinquency charge was made pursuant to the provisions on delinquency charges (Section 2.502) shall be considered as having been paid on its due date as so scheduled or deferred.

(3) The amount of any deferral charge earned at the date of prepayment shall also be computed. If the deferral charge earned is less than the deferral charge paid, the difference shall be added to the unearned portion of the finance charge. If any part of a deferral charge has been earned but has not been paid, that part shall be subtracted from the unearned portion of the finance charge or shall be added to the unpaid balance.

(4) This rule does not preclude the collection or retention by the creditor of delinquency or deferral charges.

PART 6

## OTHER CREDIT TRANSACTIONS

### §2.601. [Charges for Other Credit Transactions]

(1) Except as provided in subsection (2), with respect to a credit transaction other than a consumer credit transaction, the parties may contract for payment by the debtor of any finance or other charge.

(2) With respect to a credit transaction which would be a consumer credit transaction if a finance charge were made, a charge for delinquency may not exceed amounts allowed for finance charges for consumer credit sales pursuant to open-end credit (Section 2.202).

### COMMENT

1. An economic fundamental of this Act is that too low a rate ceiling prevents both consumer and commercial debtors who need credit from getting credit at reasonable rates from legitimate creditors. Because basic usury laws had that effect, the legislatures in almost all the States have enacted myriad exceptions to the usury statutes for consumer and commercial transactions such as small, industrial and instalment loan laws and prohibitions against a defense of usury by a corporation. The sale of goods, services, or interests in land on credit, whether in a consumer or commercial context, has been held by the courts of most of the States to be exempt from their usury laws under the time-price doctrine. That doctrine has been recognized and limited by the legislatures of most States which have enacted laws regulating consumer instalment sales.

This Act repeals the general usury statute as well as the exceptions to it, sets reasonable ceilings on all consumer credit rates, and in this section leaves the finance charge and other charges in transactions other than consumer credit transactions, such as:

(a) A transaction by a seller or lender not regularly engaged in similar credit transactions,

(b) A transaction over $25,000 in amount not involving real property,

(c) A transaction in which an organization is the debtor, and

(d) A transaction for a business purpose,

basically to the agreement of the parties. In all these types of transactions except the first, which is usually a family transaction or may be within subsection (15)(c) of Section 1.301, the debtors are usually sophisticated enough to take care of themselves in negotiating credit charges. It is difficult to impose an arbitrary rate ceiling for these transactions that will be high enough to allow for high risk business transactions without setting a limit that is so high as to be virtually meaningless. This Act contemplates the repeal of the general usury statute in any State which enacts it; hence the need for the time-price doctrine is eliminated in any such State. Given the basic philosophy of this Act, it should not be interpreted as rejecting the time-price doctrine in either its consumer or commercial context in any State which has not enacted the Act or which continues to have a general usury statute.

2. Some transactions involving open accounts are not consumer credit transactions within this Act because there is neither provision for a finance charge nor for payment in instalments (Sections 1.301(12) and 1.301(15)). Some oil company credit card accounts are examples. Subsection (2) limits delinquency charges in such cases to amounts allowed by finance charge ceilings in open-end credit.

ARTICLE 3

## REGULATION OF AGREEMENTS AND PRACTICES

Part 1

## GENERAL PROVISIONS

Section
3.101. Short Title.
3.102. Scope.

Part 2

## DISCLOSURE

3.201. Compliance with Federal Truth in Lending Act.
3.202. Consumer Leases.
3.203. Notice to Consumer.
3.204. Notice of Assignment.
3.205. Change in Terms of Open-End Credit Accounts.
3.206. Receipts; Statements of Account; Evidence of Payment.
3.207. Form of Insurance Premium Loan Agreement.
3.208. Notice to Co-Signers and Similar Parties.
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Part 3

## LIMITATIONS ON AGREEMENTS AND PRACTICES



Part 4

## LIMITATIONS ON CONSUMERS' LIABILITIES



Part 5

## HOME SOLICITATION SALES



PART 1

## GENERAL PROVISIONS

### § 3.101. [Short Title]

This Article shall be known and may be cited as Uniform Consumer Credit Code-Regulation of Agreements and Practices.

**§ 3.102. [Scope]**

Part 2 of this Article applies to disclosure with respect to consumer credit transactions. The provision on compliance with the Federal Truth in Lending Act (Section 3.201) applies to a sale of an interest in land or a loan secured by an interest in land, without regard to the rate of finance charge, if the sale or loan is otherwise a consumer credit sale or consumer loan. Parts 3 and 4 of this Article apply, respectively, to limitations on agreements and practices, and limitations on consumers' liabilities with respect to certain consumer credit transactions. Part 5 applies to home solicitation sales.

**COMMENT**

This Act does not apply to real property credit transactions in which the finance charge does not exceed 12% because these transactions are not consumer credit sales or consumer loans pursuant to Sections 1.301(12) and 1.301(15). In order to make coverage of this Act coterminous for disclosure purposes with that of the Federal Truth in Lending Act which applies to all consumer credit transactions in real property, this section expressly provides that the provision on compliance with Truth in Lending applies to real property consumer credit transactions without regard to the rate of finance charge.

PART 2

**DISCLOSURE**

**§ 3.201. [Compliance with Federal Truth in Lending Act]**

(1) A person upon whom the Federal Truth in Lending Act imposes duties or obligations shall make or give to the consumer the disclosures, information, and notices required of him by that Act and in all respects comply with that Act. To the extent the Federal Truth in Lending Act does not impose duties or obligations upon a person in a credit transaction, except a consumer

lease, that is a consumer credit transaction under this Act, the person shall make or give to the consumer disclosures, information, and notices in accordance with the Federal Truth in Lending Act with respect to the credit transaction.

(2) The Federal Truth in Lending Act is deemed to apply to a credit transaction which is a consumer credit transaction under this Act, notwithstanding its inclusion in a class of transactions within this State which, by regulation of the Board of Governors of the Federal Reserve System, is exempt from the Federal Truth in Lending Act.

**COMMENT**

This section incorporates the Federal Truth in Lending Act, defined by Section 1.302 as including Regulation Z, as the law of the adopting State. Section 6.104(2) empowers the Administrator to enforce this body of law. The purpose is to attain the dual administrative enforcement of Truth in Lending as recommended by the Report of the National Commission on Consumer Finance p. 60 (1972). The second sentence of subsection (1) and subsection (2) impose on creditors in all transactions covered by this Act the duty to disclose as though the Federal Truth in Lending Act applied even though the latter Act might not actually apply to the transaction.

**§ 3.202. [Consumer Leases]**

(1) With respect to a consumer lease the lessor shall give to the lessee the following information:

(a) brief description or identification of the goods;

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

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

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

(e) brief description of insurance to be provided or paid for by the lessor, including

the types and amounts of the coverages;

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

(g) statement of the conditions under which the lessee may terminate the lease before the end of the term; and

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

(2) The disclosures required by this section:

(a) shall be made clearly and conspicuously in writing, a copy of which shall be delivered to the lessee;

(b) may be supplemented by additional information or explanations supplied by the lessor, but none shall be stated, utilized, or placed so as to mislead or confuse the lessee or contradict, obscure, or detract attention from the information required to be disclosed by this section;

(c) need be made only to the extent applicable;

(d) shall be made on the assumption that all scheduled payments will be made when due and will comply with this section although rendered inaccurate by an act, occurrence, or agreement after the required disclosure; and

(e) shall be made before the lease transaction is consummated, but may be made in the lease to be signed by the lessee.

**COMMENT**

This Act recognizes the consumer lease to be an increasingly popular alternative to consumer credit sales as a method of distributing consumer goods on a periodic payment basis.

See Comment to Section 1.301(14). The consumer lessee is given full disclosure of all charges imposed as well as information concerning the amounts, number, and schedule of payments. The lessor must also set out the terms under which the lessee may terminate the lease prior to the end of its term and any liabilities the lessee may incur at the end of the term of the lease. See Section 3.401. Subsection (2) makes the time and manner of disclosure for consumer leases consistent with the requirements of the Federal Truth in Lending Act.

**§ 3.203. [Notice to Consumer]**

The creditor shall give to the consumer a copy of any writing evidencing a consumer credit transaction, except one pursuant to open-end credit, if the writing requires or provides for the signature of the consumer. The writing evidencing the consumer's obligation to pay the debt shall contain a clear and conspicuous notice informing the consumer that he should not sign it before reading it, that he is entitled to a copy of it, and, except in case of a consumer lease, that he is entitled to prepay the unpaid balance at any time without penalty and may be entitled to receive a refund of unearned charges in accordance with law. The following notice if clear and conspicuous complies with this section:

NOTICE TO CONSUMER:

1. Do not sign this paper before you read it.

2. You are entitled to a copy of this paper.

3. You may prepay the unpaid balance at any time without penalty and may be entitled to receive a refund of unearned charges in accordance with law.

**COMMENT**

Under this section the consumer must receive a copy of the credit agreement in closed-end transactions and that agreement must contain a conspicuous legend cautioning the consumer to read before he signs and notifying him of his rights to a copy and to prepayment. These requirements are not made for open-end credit transactions. Some of the information in the notice is inapplicable to open-end credit, i.e. the right to prepay.

Moreover, the consumer's obligation to pay in open-end credit may be evidenced by sales slips or the like, and it is operationally infeasible to require statutory legends on these informal

writings. Then, too, Truth in Lending assures that the consumer will receive a copy of the terms under which the open-credit account will operate and will receive periodic statements. Regulation Z Section 226.7(a) and (b).

**§ 3.204. [Notice of Assignment]**

A consumer may pay the original creditor until he receives notification of assignment of rights to payment pursuant to a consumer credit transaction and that payment is to be made to the assignee. A notification which does not reasonably identify the rights assigned is ineffective. If requested by the consumer, the assignee shall seasonably furnish reasonable proof that the assignment has been made and unless he does so the consumer may pay the original creditor.

**COMMENT**

The consumer is protected in paying the original creditor until he receives notice of an assignment. This section is derived from UCC Section 9-318(3) and overrides the provisions of UCC Section 3-603(1) in connection with a consumer loan evidenced by a negotiable instrument.

**§ 3.205. [Change in Terms of Open-End Credit Accounts]**

(1) Whether or not a change is authorized by prior agreement, a creditor may change the terms of an open-end credit account applying to any balance incurred before or after the effective date of the change. If the change increases the rate of the finance charge or of additional charges, alters the method of determining the balance upon which charges are made so that increased charges may result, or imposes or increases minimum charges, the change is effective with respect to a balance incurred before the effective date of the change only if the consumer after receiving disclosure of the change agrees to it in writing or the creditor delivers or mails to the consumer two written disclosures of the change, the first at least three months before the effective date of the change and the second at a later time before the effective date of the change.

(2) A disclosure provided for in subsection (1) is mailed to the consumer when mailed to him at his address used by the creditor for mailing him periodic billing statements.

(3) If a creditor attempts to change the terms of an open-end credit account as provided in subsection (1) without complying with this section, any additional cost or charge to the consumer resulting from the change is an excess charge and is subject to the remedies available to the consumer (Section 5.201) and to the Administrator (Section 6.113).

**COMMENT**

1. New developments in consumer credit practices may require changes in open-end credit accounts from time to time. A national department store or commercial bank issuing credit cards may have hundreds of thousands of cardholders. Insurmountable difficulties would confront such creditors were it necessary for them to obtain from each consumer his signed consent to a change in terms. Experience indicates that only a minority of customers take the trouble to return an express approval or disapproval of a change in terms. Nevertheless, merchants and banks should not be permitted to take advantage of customers by changes which are unfair, unanticipated, or inadequately communicated. This provision is designed to allow creditors to change the terms of their open-end accounts in a manner which is feasible from their standpoint but which safeguards the interests of their customers.

2. Truth in Lending requires 15-days' notice of certain changes in an open-end credit account (Regulation Z Section 226.7(e)), and if the change either does not increase credit costs or, if costs are increased, affects only balances incurred after the date of the change, the creditor need only give the 15-day Truth in Lending notice. However, under this section if the change increases credit costs for consumers and applies to balances already incurred, the creditor must either obtain the consumer's written consent to the change or comply with the notice provisions of this section, as well as comply with Truth in Lending.

**§ 3.206. [Receipts; Statements of Account; Evidence of Payment]**

(1) The creditor shall deliver or mail to the consumer, without request, a written receipt for each payment by coin or currency on an obligation pursuant to a consumer credit transaction. A periodic statement showing a payment received by mail complies with this subsection.

(2) Upon written request of a consumer, the person to whom an obligation is owed pursuant to a consumer credit transaction, except one pursuant to open-end credit, shall provide a written statement of the dates and amounts of payments made within the 12 months preceding the month in which the request is received and the total amount unpaid as of the end of the period

covered by the statement. The statement shall be provided without charge once during each year of the term of the obligation. If additional statements are requested the creditor may charge not in excess of [$_____] for each additional statement.

(3) After a consumer has fulfilled all obligations with respect to a consumer credit transaction, except one pursuant to open-end credit, the person to whom the obligation was owed, upon request of the consumer, shall deliver or mail to the consumer written evidence acknowledging payment in full of all obligations with respect to the transaction.

**COMMENT**

Subsection (1) assures consumers of receipts for payments made in money but imposes no duty on creditors to give receipts for payments made by check, money order, or the like. Sending periodic statements pursuant to open-end credit (Regulation Z Section 228.7(b)) or closed-end credit (Regulation Z Section 228.8(n) note 13) showing payments made relieves the creditor of any further duty to send receipts.

Subsection (2) allows consumers to obtain a statement of account in closed-end transactions. The consumer's receipt of periodic statements serves this need in open-end credit accounts. Subsection (3) allows the consumer to obtain evidence of satisfaction upon payment in full of closed-end credit obligations. Again, this requirement is unnecessary in open-end credit owing to the creditor's duty to reflect payments in periodic statements.

**§ 3.207. [Form of Insurance Premium Loan Agreement]**

An agreement pursuant to which an insurance premium loan is made shall contain the names of the insurance agent or broker negotiating each policy or contract and of the insurer issuing each policy or contract, the number and inception date of, and premium for, each policy or contract, the date on which the term of the loan begins, and a clear and conspicuous notice that each policy or contract may be cancelled if payment is not made in accordance with the agreement. If a policy or contract has not been issued by the time the agreement is signed, the agreement may provide that the insurance agent or broker may insert the appropriate information in the agreement, and, if he does so, shall furnish the information promptly in writing to the

insured.

**COMMENT**

This section requires that in insurance premium financing transactions the consumer be given pertinent information regarding the insurance contract and the fact that it may be cancelled upon his default. If the required information is unavailable at the time the agreement is entered into because the policy has not been issued, the agent must furnish the information promptly when the policy is issued.

**§ 3.208. [Notice to Co-Signers and Similar Parties]**

(1) A natural person, other than the spouse of the consumer, is not obligated as a co-signer, co-maker, guarantor, indorser, surety, or similar party with respect to a consumer credit transaction, unless before or contemporaneously with signing any separate agreement of obligation or any writing setting forth the terms of the debtor's agreement, the person receives a separate written notice that contains a completed identification of the debt he may have to pay and reasonably informs him of his obligation with respect to it.

(2) A clear and conspicuous notice in substantially the following form complies with this section:

NOTICE

You agree to pay the debt identified below although you may not personally receive any property, services, or money. You may be sued for payment although the person who receives the property, services, or money is able to pay. This notice is not the contract that obligates you to pay the debt. Read the contract for the exact terms of your obligation.

IDENTIFICATION OF DEBT YOU MAY HAVE TO PAY

_____

(Name of Debtor)

_____

(Name of Creditor)

_____

(Date)

_____

(Kind of Debt)

I have received a copy of this notice.

_____

(Date)

_____

(Signed)

(3) The notice required by this section need not be given to a seller, lessor, or lender who is obligated to an assignee of his rights.

(4) A person entitled to notice under this section shall also be given a copy of any writing setting forth the terms of the debtor's agreement and of any separate agreement of obligation signed by the person entitled to the notice.

**COMMENT**

The Report of the National Commission on Consumer Finance pp. 39-40 (1972) expresses concern that persons who assist consumers in obtaining credit by lending their signatures as sureties, or otherwise, may not understand the consequences of their act. This section responds to the Report's recommendation by requiring that the accommodation party be given a separate notice informing him of his potential liabilities as a condition of his being bound on his agreement; he must as well be given a copy of the agreement he is guaranteeing. Creditors who incur the liabilities of a transferor or indorser in assigning consumer paper are not entitled to the notice provided by this section. (Subsection (3)).

**§ 3.209. [Advertising]**

(1) A seller, lessor, or lender may not advertise, print, display, publish, distribute, broadcast, or cause to be advertised, printed, displayed, published, distributed, or broadcast in any manner any statement or representation with regard to the rates, terms, or conditions of credit with respect to a consumer credit transaction that is false, misleading, or deceptive.

(2) Advertising that complies with the Federal Truth in Lending Act does not violate this section.

(3) This section does not apply to the owner or personnel, as such, of any medium in which an advertisement appears or through which it is disseminated.

## COMMENT

This section supplements the provisions on advertising appearing in the Truth in Lending Act, 15 U.S.C. §§ 1661-1665. It should be noted that the exemption granted to States by the Board of Governors of the Federal Reserve System pursuant to 15 U.S.C. § 1633 does not extend to advertising. Hence, even in States that obtain exemption from the Federal Truth in Lending Act, the provisions on advertising in the Federal Act will coexist with this section in the enacting State.

# PART 3

# LIMITATIONS ON AGREEMENTS AND PRACTICES

### § 3.301. [Security in Sales and Leases]

(1) With respect to a consumer credit sale, a seller may take a security interest in the property sold. In addition, a seller may take a security interest in goods upon which services are performed or in which goods sold are installed or to which they are annexed, or in land to which the goods are affixed or which is maintained, repaired or improved as a result of the sale of the goods or services, if in the case of a security interest in land the debt secured is $1,000 or more, or, in the case of a security interest in goods the debt secured is $300 or more. The seller may also take a security interest in property to secure the debt arising from a consumer credit sale primarily for an agricultural purpose. Except as provided with respect to cross-collateral (Section 3.302) a seller may not otherwise take a security interest in property to secure the debt arising from a consumer credit sale.

(2) With respect to a consumer lease, except one primarily for an agricultural purpose, a lessor may not take a security interest in property to secure the debt arising from the lease. This subsection does not apply to a security deposit for a consumer lease.

(3) A security interest taken in violation of this section is void.

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

**COMMENT**

This section limits sellers and lessors with respect to the manner in which they may secure the obligation arising from a consumer credit sale (Section 1.301(12)) or consumer lease (Section 1.301(14)). See Section 5.116 for limitations on the creditor's right to realize on collateral exempt under the law of this State.

1. Sales of goods. A seller may take a security interest in the goods sold but not in other goods or land unless the goods sold become closely connected with the goods or land in which the security interest is taken. Under this section an appliance dealer may retain a security interest in a washing machine sold but may not take a security interest in other appliances to secure the sale obligation unless he complies with Section 3.302. Except as provided in Section 3.302, a seller of goods may take additional security for the sale obligation in other goods or land only if the debt secured is substantial-$300 in the case of a security interest in goods, $1,000 in the case of a security interest in land-and then only if the goods or land in which the additional security interest is taken are goods in which the goods sold are installed or to which they are annexed or land to which the goods sold are annexed or which is maintained, repaired, or improved by the goods sold.

2. Sales of services. The seller may not take a security interest in goods or land to secure an obligation arising out of the sale of services unless the services are performed on the goods or are used to maintain, repair, or improve the land. Even then, the debt secured must be $300 in the case of a security interest in goods and $1,000 in the case of a security interest in land. Thus a seller of dancing lessons may not take a security interest in goods or lands, and a carpenter or painter may take a security interest in a residence only if the debt arising from the sale of services is $1,000 or more.

3. Sales of land. The seller can retain a security interest only in the land sold and not in other goods or land. It should be noted, however, that this section applies only to consumer credit sales and a sale of an interest in land in which the finance charge is 12% or less is not a consumer credit sale. Section 1.301(12).

4. Consumer leases. A lessor may not secure the lease obligation by taking a security interest in property.

5. Sales for agricultural purposes. Farmers sometimes secure the unpaid balance of a sale obligation by giving security interests in their land or farm equipment. In order not to disturb this practice, an exception in the application of this section is made for sales and leases for agricultural purposes.

**§ 3.302. [Cross-Collateral]**

(1) In addition to contracting for a security interest pursuant to the provisions on security in sales and leases (Section 3.301), a seller in a consumer credit sale may secure the debt arising from the sale by contracting for a security interest in other property if as a result of a prior sale the seller has an existing security interest in the other property. The seller may also contract for a security interest in the property sold in the subsequent sale as security for the previous debt.

(2) If the seller contracts for a security interest in other property pursuant to this section, the rate of finance charge thereafter on the aggregate unpaid balances so secured may not exceed that permitted if the balances so secured were consolidated pursuant to the provisions on finance charge on consolidation (subsection (2) of Section 2.505). The seller has a reasonable time after so contracting in which to make any adjustments required by this section.

**COMMENT**

1. A seller who sells goods on credit to a buyer in more than one sale may secure the debts arising from each sale by a cross-security interest in the other goods sold so long as the seller has an existing security interest in the other goods. Section 3.303 specifies when a seller loses his security interest in goods in a cross-collateral situation.

2. Subsection (1) allows cross-collateral to be taken either for separate debts or for consolidated debts, but subsection (2) limits the rate of the finance charge that a seller may charge in the separate debt case to that chargeable had the debts been consolidated pursuant to Section 2.505(2). To illustrate, if a buyer who owes seller a $275 balance from one sale makes a subsequent $250 purchase, the seller may consolidate these debts under Section 2.505(2) so that the finance charge would be calculated on the sum of the refinanced balance of the first sale, e.g., $260, and the amount financed under the second sale, $250, or a total of $510. Under Section 2.201, the seller may then charge a maximum rate of 36% on the first $300 and 21% on the next $210. However, if the debts were kept separate, the seller might charge the maximum of 36% on both the $275 and $250 balances. In effect subsection (2) prevents the seller from taking the advantages of cross-collateral without also offering the buyer the lower rates that would have resulted had the debts been consolidated pursuant to Section 2.505(2).

**§ 3.303. [Debt Secured by Cross-Collateral]**

(1) If debts arising from two or more consumer credit sales, except sales primarily for an agricultural purpose or pursuant to open-end credit, are secured by cross-collateral (Section

3.302) or consolidated into one debt payable on a single schedule of payments, and the debt is secured by security interests taken with respect to one or more of the sales, payments received by the seller after the taking of cross-collateral or the consolidation are deemed, for the purpose of determining the amount of the debt secured by the various security interests, to have been applied first to the payment of the debts arising from the sales first made. To the extent debts are paid according to this section, security interests in items of property terminate as the debt originally incurred with respect to each item is paid.

(2) Payments received by the seller upon an open-end credit account are deemed, for the purpose of determining the amount of the debt secured by the various security interests, to have been applied first to the payment of finance charges in the order of their entry to the account and then to the payment of debts in the order in which the entries to the account showing the debts were made.

3. If the debts consolidated arose from two or more sales made on the same day, payments received by the seller are deemed, for the purpose of determining the amount of the debt secured by the various security interests, to have been applied first to the payment of the smallest debt.

**COMMENT**

1. When a seller consolidates debts arising from sales and secures the consolidated debt by security interests in the goods sold in these sales or when a seller secures separate debts by cross-collateral (Section 3.302), this section prevents the seller from retaining a security interest in all of the goods until the buyer's entire debt is paid. The basis of the section is that a security interest in goods terminates when the debt incurred in the sale of the goods is paid. For the purpose of determining when this debt is paid, subsection (1) allocates the buyer's payments first to the debts first incurred. Thus if the seller consolidates debts of $100, $200, and $300 arising from sales made in that order, the security interest in the goods purchased pursuant to the $100 sale terminates when $100 of the consolidated debt is paid. If the seller does not consolidate these debts but secures them by cross-collateral, he must allocate all of the buyer's payments to the $100 debt until it is paid off, and so forth. Subsection (2) applies this first-payments-against-first-debts rule to open-end accounts.

2. Subsection (3) applies to the case in which the buyer purchases a $750 TV in one apartment at 9:30 a.m. and a $150 typewriter in another department at 10:00 a.m. Subsequently the debts are consolidated. This subsection relieves the seller of having to keep records of the exact hour a sale is made. It is derived from Regulation Z Section 226.8(h).

**§ 3.304. [Use of Multiple Agreements]**

(1) A creditor may not use multiple agreements with respect to a single consumer credit transaction with intent to obtain a higher finance charge than otherwise would be permitted by the provisions of the Article on Finance Charges and Related Provisions (Article 2).

(2) The excess amount of finance charge resulting from a violation of subsection (1) is an excess charge for the purposes of the provisions on rights of parties (Section 5.201) and the provisions on civil actions by Administrator (Section 6.113).

**COMMENT**

The graduated rate ceiling structure of this Act (Sections 2.201 and 2.401) allows a creditor to charge higher rates on smaller balances. In order to achieve maximum rates a seller might arbitrarily divide a transaction into two or more agreements in order that the amount financed under each is within the $300 amount on which the highest rate can be charged. If he does so the excess amount of finance charge provided for is made by subsection (2) an excess charge for purposes of the provisions on remedies by consumers and the Administrator. A supervised lender would violate this provision if he directed a consumer seeking a $500 loan to sign one note for $250 and to have his wife sign another for $250. On the other hand, a supervised lender would not be in violation of this provision if a husband borrowed $250 at one time and his wife on a voluntary separate loan application borrowed $250 at some other time.

**§ 3.305. [No Assignment of Earnings]**

(1) A creditor may not take an assignment of earnings of the consumer for payment or as security for payment of a debt arising out of a consumer credit transaction. An assignment of earnings in violation of this section is unenforceable by the assignee of the earnings and revocable by the consumer. This section does not prohibit a consumer from authorizing deductions from his earnings in favor of his creditor if the authorization is revocable, the consumer is given a complete copy of the writing evidencing the authorization at the time he signs it, and the writing

contains on its face a conspicuous notice of the consumer's right to revoke the authorization.

(2) A sale of unpaid earnings made in consideration of the payment of money to or for the account of the seller of the earnings is deemed to be a loan to him secured by an assignment of earnings.

**COMMENT**

This Act recognizes the potential for hardship for a consumer and his dependents which may result from a disruption of the steady flow of family income. Just as Section 5.104 prevents a creditor from attaching unpaid earnings of a consumer before he obtains judgment, this provision precludes a creditor from reaching the consumer's earnings pursuant to an irrevocable wage assignment obtained from the consumer. The purpose of both sections is to afford the consumer an opportunity to have his debt determined by a court before his unpaid earnings are taken against his will by a creditor. This provision prohibits a creditor from taking either an assignment of earnings as payment or as security for payment for a debt or a sale of earnings in payment of the price or rental. A revocable payroll deduction authorization in favor of a creditor is not forbidden by this section so long as the requisite notice is given to the consumer of his right to revoke.

**§ 3.306. [Authorization to Confess Judgment Prohibited]**

A consumer may not authorize any person to confess judgment on a claim arising out of a consumer credit transaction. An authorization in violation of this section is void.

**COMMENT**

This section reflects the view of the great majority of States in prohibiting authorizations to confess judgment. It is consistent with the policy of the Act of assuring the consumer a right to a judicial hearing before judgment is entered against him or his rights are otherwise affected. See Sections 3.305 and 5.104. This section follows a recommendation of the National Commission on Consumer Finance (NCCF Report, p. 26 (1972)). It does not prohibit the consumer himself from confessing judgment pursuant to the laws of this State.

**§ 3.307. [Certain Negotiable Instruments Prohibited]**

With respect to a consumer credit sale or consumer lease, [except a sale or lease primarily for an agricultural purpose,] the creditor may not take a negotiable instrument other than a check dated not later than ten days after its issuance as evidence of the obligation of the consumer.

## COMMENT

This section, together with Sections 3.403, 3.404, and 3.405, states a major tenet of this Act: that the holder in due course doctrine should be abrogated in consumer cases. Whatever beneficial effects this doctrine may have in promoting the currency of paper is greatly outweighed by the harshness of its consequences in denying consumers the right to raise valid defenses arising out of credit transactions. The first step in abolition of the doctrine is the prohibition found in this section of the use of negotiable instruments in consumer credit sales and consumer leases. The presence of the bracketed language recognizes the strong tradition of the use of negotiable instruments in agricultural transactions in some States.

### § 3.308. [Balloon Payments]

(1) Except as provided in subsection (2), if any scheduled payment of a consumer credit transaction is more than twice as large as the average of earlier scheduled payments, the consumer has the right to refinance, without penalty, the amount of that payment at the time it is due. The terms of the refinancing shall be no less favorable to the consumer than the terms of the original transaction.

(2) This section does not apply to:

(a) a consumer lease;

(b) a transaction pursuant to open-end credit;

(c) a transaction primarily for an agricultural purpose;

(d) a transaction to the extent that the payment schedule is adjusted to the seasonal or irregular income or scheduled payments or obligations of the consumer; or

(e) a transaction of a class defined by rule of the Administrator as not requiring for the protection of the consumer his right to refinance as provided in this section.

## COMMENT

1. Balloon payments may have legitimate uses, but they may also be used to induce a consumer to enter into a burdensome contract by offering him invitingly small instalment payments until the end of the contract when the consumer is confronted with a balloon payment too large to pay. See Section 2.308 requiring a regular schedule of payments in supervised loans

not in excess of $1,000. This section meets the threat of misuse of balloon payments by giving the consumer the right to compel refinancing of the amount of the balloon payment at the time it is due without penalty under terms no less favorable than those of the original transaction. Under the refinancing the size of the instalment payments may not exceed the average scheduled payments excluding the balloon payment and the rate of the finance charge may not exceed that under the original agreement.

2. Subsection (2) excludes use of the option to refinance in cases in which balloon payments may be beneficial to the consumer, e.g., paragraph (d) disallows the refinancing option when the payments were made irregular to meet the requirements of an irregular income flow on the part of the consumer or to mesh with a changing schedule of payments on the consumer's other obligations. Paragraph (a) recognizes that balloon payments in consumer leases are treated in Section 3.401. Open-end credit is excluded by paragraph (b) because payments are necessarily irregular in open-end transactions. There are so many instances in which irregular payments are mutually beneficial in agricultural financing that it was thought desirable to make a blanket exception for agricultural transactions in paragraph (c). Since the purpose of this section is to protect consumers against deceptive or unfair use of irregular payments and not to inhibit their use in cases in which they are to the advantage of both parties, paragraph (e) offers a safety valve provision authorizing the Administrator to exempt transactions if he believes the interests of all would be best served by doing so.

**§ 3.309. [Referral Sales and Leases]**

With respect to a consumer credit sale or consumer lease, the seller or lessor may not give or offer to give a rebate or discount or otherwise pay or offer to pay value to the consumer as an inducement for a sale or lease for the consumer giving to the seller or lessor the names of prospective buyers or lessees, or otherwise aiding the seller or lessor in making a sale or lease to another person, if the earning of the rebate, discount or other value is contingent upon the occurrence of an event after the time the consumer agrees to buy or lease. If a consumer is induced by a violation of this section to enter into a consumer credit sale or consumer lease, the agreement is unenforceable by the seller or lessor and the consumer, at his option, may rescind the agreement or retain the property delivered and the benefit of any services performed, without any obligation to pay for them. A sale or lease that would be a referral sale or lease if credit were extended by the seller or lessor is nonetheless so because the property or services are paid for in whole or in part by use of a credit card or by a consumer loan with respect to which the lender is

subject to claims and defenses arising from the sale or lease (Section 3.405), and the consumer has the same rights against the card issuer or lender that he has against the seller or lessor under this section.

**COMMENT**

1. The typical referral sale scheme which would be barred by this section is one in which the seller, before closing the sale, offers to reduce the price by $25 for every name of a person the buyer supplies who will agree to buy from the seller. The seller may be able to make an inflated price tag much more palatable to a buyer if he can convince the buyer that the referral plan will greatly reduce the amount he will actually have to pay. The buyer may not realize until later that his friends whose names he submitted are not as gullible as he and that he is bound to pay the original balance of the contract price.

2. The evil this section is aimed at is the raising of expectations in a buyer of benefits to accrue to him from events which are to occur in the future. This provision has no effect on a seller's agreement to reduce at the time of the sale the price of an item in exchange for the buyer's giving the seller a list of prospective purchasers or assisting in other ways if the price reduction is not contingent on whether the purchasers do in fact buy or on whether other events occur in the future.

3. The misuse of the referral sale scheme has been so pervasive in some segments of vendor credit that this provision, in an effort to halt these practices, not only makes agreements in violation of this section unenforceable but also allows the buyer to retain the goods sold or the benefit of services rendered with no obligation to pay for them. Alternatively, the buyer may rescind the agreement, return the goods, and recover any payment. Use of a referral scheme subjects the offending seller or lessor to a penalty under Section 5.201. Creditors cannot evade this section by the use of credit cards or consumer loans.

PART 4

## LIMITATIONS ON CONSUMERS' LIABILITIES

### § 3.401. [Restriction on Liability in Consumer Lease]

The obligation of a lessee upon expiration of a consumer lease [, except one primarily for an agricultural purpose,] may not exceed twice the average payment allocable to a monthly period under the lease. This limitation does not apply to charges for damages to the leased property or

for other default.

**COMMENT**

This section is designed to protect consumer lessees against abuses associated with what are described in some areas of the country as "open-end" leases. Under such an agreement the parties contract that at the expiration of the lease the article leased, usually an automobile, will have a certain depreciated value and will be sold. If it brings less than the agreed depreciated value, the lessee is liable for the difference; if it brings more, the lessee is entitled to the surplus. Under such an agreement, the lessee will have no understanding of how much the lease might cost him unless he can accurately predict what the second hand market will be at the expiration of lease. Moreover, if the lessor sets an unrealistically high depreciated value the contingent liability of the lessee will increase accordingly, and the lessor can offer deceptively low rental payments to a gullible customer.

Under this section the liability, contingent or otherwise, of the lessee at the end of the term of the lease is limited to twice the average monthly rental payment. This limitation not only avoids the possibility of a large contingent liability on the part of the lessee at the end of the term but also gives the lessee a basis for comprehending how much the lease will actually cost him.

**§ 3.402. [Limitation on Default Charges]**

Except for reasonable expenses incurred in realizing on a security interest, the agreement with respect to a consumer credit transaction other than a consumer lease may not provide for any charges as a result of default by the consumer except those authorized by this Act. A provision in violation of this section is unenforceable.

**COMMENT**

This Act limits the credit related charges a creditor may impose on a consumer not only at the outset of the contract but also at the default stage. Except for delinquency charges (Section 2.502) [, attorney's fees (Section 2.507),] and expenses arising from realizing on collateral (UCC Section 9-504), the creditor may impose no collection or default charges on a consumer.

[The bracketed language in this Comment should be omitted if Alternative A of Section 2.507 is selected.]

**§ 3.403. [Card Issuer Subject to Claims and Defenses]**

(1) This section neither limits the liability of nor imposes liability on a card issuer as a manufacturer, supplier, seller, or lessor of property or services sold or leased pursuant to the

credit card. This section may subject a card issuer to claims and defenses of a cardholder against a seller or lessor arising from sales or leases made pursuant to the credit card.

(2) A card issuer is subject to claims and defenses of a cardholder against the seller or lessor arising from the sale or lease of property or services by a seller or lessor licensed, franchised, or permitted by the card issuer or a person related to the card issuer to do business under the trade name or designation of the card issuer or a person related to the card issuer, to the extent of the original amount owing to the card issuer with respect to the sale or lease of the property or services as to which the claim or defense arose.

(3) Except as otherwise provided in this section, a card issuer, including a lender credit card issuer, is subject to all claims and defenses of a cardholder against the seller or lessor arising from the sale or lease of property or services pursuant to the credit card:

(a) if the original amount owing to the card issuer with respect to the sale or lease of the property or services as to which the claim or defense arose exceeds $50;

(b) if the residence of the cardholder and the place where the sale or lease occurred are [in the same state or] within 100 miles of each other;

(c) if the cardholder has made a good faith attempt to obtain satisfaction from the seller or lessor with respect to the claim or defense; and

(d) to the extent of the amount owing to the card issuer with respect to the sale or lease of the property or services as to which the claim or defense arose at the time the card issuer has notice of the claim or defense. Notice of the claim or defense may be given before the attempt specified in paragraph (c). Oral notice is effective unless the card issuer requests written confirmation when or promptly after oral notice is given and the cardholder fails to give the card issuer written confirmation within the period of time, not less than 14 days, stated to the

cardholder when written confirmation is requested.

(4) For the purpose of determining the amount owing to the card issuer with respect to a sale or lease upon an open-end credit account, payments received for the account are deemed to have been applied first to the payment of finance charges in the order of their entry to the account and then to the payment of debts in the order in which the entries of the debts are made to the account.

(5) An agreement may not limit or waive the claims or defenses of a cardholder under this section.

**COMMENT**

1. The policies stated in Sections 3.307 and 3.404 of abolition of the holder in due course doctrine could be thwarted if the parties could deprive consumers of their claims and defenses merely by recasting assigned paper transactions into credit card transactions. Thus subsection (3) subjects credit card issuers to consumer claims and defenses in those transactions in which the credit card is more likely to be used as a true credit device (sales or leases in excess of $50) and in which the great volume of credit card use takes place (sales or leases [within the consumer's state of residence or] within 100 miles of the residence). For a discussion of the amount of the debt owing against which the claim or defense can be asserted, see Comment 2 to Section 3.404.

2. The first sentence of subsection (1) recognizes that some credit card issuers (e.g., the major retail chains) are themselves the sellers or lessors of products or services, and their liability as sellers or lessors is in no way affected by their status as credit card issuers. Subsection (2) provides that when the card issuer (*e.g.*, oil distributors), allows others to sell products while operating under the issuer's name, the card issuer should be liable to the full amount of the credit extended in the sale as the financer of the transaction but should bear no further liability for products defects or the like merely because the sale was made pursuant to its credit card. If such a card issuer was in fact the manufacturer or processor of the defective products sold pursuant to its credit card by its franchised dealer, then the case would fall within the first sentence of subsection (1) and the presence of the credit card would be irrelevant to the manufacturer's or processor's liability. Subsection (3) imposes liability on the card issuer as described in Comment 1 because of the card issuer's status as the financer of the sale or lease transaction made pursuant to its card. See the second sentence of subsection (1).

**§ 3.404. [Assignee Subject to Claims and Defenses]**

(1) With respect to a consumer credit sale or consumer lease [, except one primarily for an

agricultural purpose], an assignee of the rights of the seller or lessor is subject to all claims and defenses of the consumer against the seller or lessor arising from the sale or lease of property or services, notwithstanding that the assignee is a holder in due course of a negotiable instrument issued in violation of the provisions prohibiting certain negotiable instruments (Section 3.307).

(2) A claim or defense of a consumer specified in subsection (1) may be asserted against the assignee under this section only if the consumer has made a good faith attempt to obtain satisfaction from the seller or lessor with respect to the claim or defense and then only to the extent of the amount owing to the assignee with respect to the sale or lease of the property or services as to which the claim or defense arose at the time the assignee has notice of the claim or defense. Notice of the claim or defense may be given before the attempt specified in this subsection. Oral notice is effective unless the assignee requests written confirmation when or promptly after oral notice is given and the consumer fails to give the assignee written confirmation within the period of time, not less than 14 days, stated to the consumer when written confirmation is requested.

(3) For the purpose of determining the amount owing to the assignee with respect to the sale or lease:

(a) payments received by the assignee after the consolidation of two or more consumer credit sales, except pursuant to open-end credit, are deemed to have been applied first to the payment of the sales first made; if the sales consolidated arose from sales made on the same day, payments are deemed to have been applied first to the smallest sale; and

(b) payments received for an open-end credit account are deemed to have been applied first to the payment of finance charges in the order of their entry to the account and then to the payment of debts in the order in which the entries of the debts are made to the account.

(4) An agreement may not limit or waive the claims or defenses of a consumer under this section.

**COMMENT**

1. This section codifies a growing body of case law under UCC Section 9-206 to the effect that assignees take consumer paper subject to consumer claims and defenses. This section explicitly provides for preservation of consumer defenses even though the assignee is a holder in due course (subsection (1)) or the consumer has purported to waive his claims and defenses as against the assignee (subsection (4)). The policy justifications for the section are to protect the consumer from the harshness of the holder in due course doctrine as well as to encourage financial institutions taking assignments of consumer paper to use discretion in dealing with sellers and lessors whose transactions give rise to an unusual percentage of consumer complaints. See Section 3.307.

2. The consumer, upon making a good faith attempt to obtain satisfaction from his seller or lessor, can assert his claim or defense against the assignee to the extent of the amount still owing to the assignee at the time the assignee learns of the claim or defense. If the assignee knows of the defense before any payments are made to him, the consumer can raise his claim or defense to the full amount of the assigned debt. Orderly procedures will necessitate some written record on the part of the assignee of the consumer's notification regarding his claim or defense, but the consumer ought to be able to rely on having given oral notification unless the assignee requests written confirmation. Hence, the assignee has the option of making his own written record upon receiving oral notice from the consumer or of requesting written notice from the consumer and allowing 14 days for the consumer to send his written confirmation. Subsection (3) uses the same tests for determining the amount owing on a debt as are used in Section 3.303.

**§ 3.405. [Lender Subject to Claims and Defenses Arising from Sales and Leases]**

(1) A lender, except the issuer of a lender credit card, who, with respect to a particular transaction, makes a consumer loan to enable a consumer to buy or lease from a particular seller or lessor property or services [, except primarily for an agricultural purpose,] is subject to all claims and defenses of the consumer against the seller or lessor arising from that sale or lease of the property or services if:

(a) the lender knows that the seller or lessor arranged for the extension of credit by the lender for a commission, brokerage, or referral fee;

(b) the lender is a person related to the seller or lessor, unless the relationship is

remote or is not a factor in the transaction;

(c) the seller or lessor guarantees the loan or otherwise assumes the risk of loss by the lender upon the loan;

(d) the lender directly supplies the seller or lessor with the contract document used by the consumer to evidence the loan, and the seller or lessor has knowledge of the credit terms and participates in preparation of the document;

(e) the loan is conditioned upon the consumer's purchase or lease of the property or services from the particular seller or lessor, but the lender's payment of proceeds of the loan to the seller or lessor does not in itself establish that the loan was so conditioned; or

(f) the lender, before he makes the consumer loan, has knowledge or, from his course of dealing with the particular seller or lessor or his records, notice of substantial complaints by other buyers or lessees of the particular seller's or lessor's failure or refusal to perform his contracts with them and of the particular seller's or lessor's failure to remedy his defaults within a reasonable time after notice to him of the complaints.

(2) A claim or defense of a consumer specified in subsection (1) may be asserted against the lender under this section only if the consumer has made a good faith attempt to obtain satisfaction from the seller or lessor with respect to the claim or defense and then only to the extent of the amount owing to the lender with respect to the sale or lease of the property or services as to which the claim or defense arose at the time the lender has notice of the claim or defense. Notice of the claim or defense may be given before the attempt specified in this subsection. Oral notice is effective unless the lender requests written confirmation when or promptly after oral notice is given and the consumer fails to give the lender written confirmation within the period of time, not less than 14 days, stated to the consumer when written confirmation

is requested.

(3) For the purpose of determining the amount owing to the lender with respect to the sale or lease:

(a) payments received by the lender after consolidation of two or more consumer loans, except pursuant to open-end credit, are deemed to have been applied first to the payment of the loans first made; if the loans consolidated arose from loans made on the same day, payments are deemed to have been applied first to the smallest loan; and

(b) payments received for an open-end credit account are deemed to have been applied first to the payment of finance charges in the order of their entry to the account and then to the payment of debts in the order in which the entries of the debts are made to the account.

(4) An agreement may not limit or waive the claims or defenses of a consumer under this section.

**COMMENT**

1. This section extends this Act's policy of preserving consumer claims and defenses to direct loan cases in those situations in which the relationship between the seller or lessor and the lender justifies allowing the consumer to raise claims or defenses against the lender. The requisite relationship exists when the seller or lessor arranges for the extension of credit in paragraphs (a) and (d) of subsection (1) within the meaning of Regulation Z Section 226.2(f), is related to the lender in paragraph (b), or guarantees the loan in paragraph (c), and in cases in which the lender conditions the loan on the purchase or lease from a particular seller or lessor in paragraph (e), or knows before he makes the loan of a history of consumer complaints about the seller or lessor in paragraph (f).

2. For a discussion of the amount of the debt owing against which the claim or defense can be asserted under subsections (2) and (3), see Comment 2 to Section 3.404.

PART 5

## HOME SOLICITATION SALES

### § 3.501. [Definition: "Home Solicitation Sale"]

"Home solicitation sale" means a consumer credit sale of goods or services, except primarily for an agricultural purpose, in which the seller or a person acting for him personally solicits the sale, and the buyer's agreement or offer to purchase is given to the seller or a person acting from him, at a residence. It does not include a sale made pursuant to a pre-existing open-end credit account with the seller or pursuant to prior negotiations between the parties at a business establishment at a fixed location where goods or services are offered or exhibited for sale, a transaction conducted and consummated entirely by mail or telephone, or a sale which is subject to the provisions of the Federal Truth in Lending Act on the consumer's right to rescind certain transactions. A sale that would be a home solicitation sale if credit were extended by the seller is nonetheless so because the goods or services are paid for in whole or in part by use of a credit card or by a consumer loan with respect to which the lender is subject to claims and defenses arising from the sale (Section 3.405), and the buyer has the same rights against the card issuer or lender that he has against the seller under this Part.

**COMMENT**

1. The Act singles out for special treatment consumer credit sales in which the buyer's order is given to the seller at a residence. An underlying consideration for Part 5 is the belief that in a significant proportion of such sales the consumer is induced to sign a sales contract by high pressure techniques. The Act recognizes that many buyers in such cases may be unwilling parties to the transaction and gives to them a limited right to cancel the sale. Section 3.502. The right of cancellation applies to "home solicitation sales."

2. The definition of "home solicitation sales" differentiates between those types of transactions which have been the subject of particular abuse and those which have not. Although high pressure salesmanship can be practiced anywhere, the underlying theory of Section 3.501 is that the sale in the home is particularly susceptible to such methods. Two elements are required to bring a transaction within the definition. First, there must be personal solicitation at a residence. Second, the act of the buyer in binding himself by agreeing or offering to purchase, must also take place at a residence. The phrase "at a residence" rather than "in a residence" is used to prevent avoidance of the Act by the expedient of having the buyer sign the contract outside of, but in the immediate vicinity of, the home.

3. Sellers who sell by means of solicitation in the home can avoid the application of Part 5 [Section 3.501 et seq.] by having the contract or offer to purchase signed by the buyer at the office of the seller or at some place other than a residence. If the buyer must go to the seller's office or some other place to sign the contract or offer there is less likelihood that he is acting because of undue pressure by the seller. Similarly, where the buyer has already established a prior relationship with the seller by having a pre-existing open-end account or by having previously negotiated with the seller with respect to the sale at the seller's business establishment the likelihood of coercion of the buyer is substantially less. This Part does not apply in these cases.

4. Sellers may not avoid operation of this Part by permitting consumers to buy by using credit cards or by using loan proceeds provided by the seller or obtained through loans arranged by the seller or with respect to which the seller and lender share one of the other relationships described by Section 3.405.

5. A seller subject to this Part may also be subject to the FTC Regulation on Cooling Off Period for Door-to-Door Sales. In the event of direct inconsistency between that Regulation and this Act, that Regulation prevails. Subsection (2) of Section 3.503 provides that the seller complies with this Act if he uses the notice of cancellation prescribed by that Regulation. With regard to other areas in which FTC Regulation overlaps with this Act, the Administrator by rule (Section 6.104(1)(e) may prescribe the compliance required by the seller under this Act in relation to that Regulation.

**§ 3.502. [Buyer's Right to Cancel]**

(1) Except as provided in subsection (5), in addition to any right otherwise to revoke an offer, the buyer may cancel a home solicitation sale until midnight of the third business day after the day on which the buyer signs an agreement or offer to purchase which complies with this Part.

(2) Cancellation occurs when the buyer gives written notice of cancellation to the seller at the address stated in the agreement or offer to purchase.

(3) Notice of cancellation, if given by mail, is given when it is properly addressed with postage prepaid and deposited in a mailbox.

(4) Notice of cancellation given by the buyer need not take a particular form and is sufficient if it indicates by any form of written expression the intention of the buyer not to be bound by the home solicitation sale.

(5) The buyer may not cancel a home solicitation sale if, by a separate dated and signed

statement that is not as to its material provisions a printed form and describes an emergency requiring immediate remedy, the buyer requests the seller to provide goods or services without delay in order to safeguard the health, safety, or welfare of natural persons or to prevent damage to property the buyer owns or for which he is responsible, and

(a) the seller in good faith makes a substantial beginning of performance of the contract before the buyer gives notice of cancellation, and

(b) in the case of goods, they cannot be returned to the seller in substantially as good condition as when received by the buyer.

**COMMENT**

1. The buyer has a right to cancel a home solicitation sale pursuant to this section. The notice of cancellation must be in writing, given to the seller at the address stated in the agreement signed by the buyer, and given prior to midnight of the third business day after the day the buyer signs an agreement or offer to purchase which complies with Section 3.503. These are the only formal requirements of the Act with respect to the buyer's cancellation.

2. Although the Act does not require that a notice of cancellation be mailed it is assumed that this will be the normal method of cancellation. Notice of cancellation is given at the time of mailing. The risk of non-receipt of a mailed notice of cancellation is placed on the seller, but the buyer has the burden of proving that the notice was properly mailed.

3. Goods and services are frequently sold on credit to a buyer at his home because of an emergency. Common examples are emergency repairs to broken water pipes, furnaces, appliances and the like. Since such transactions may come within the definition of home solicitation sales, sellers may be reluctant to perform services or deliver goods before expiration of the 3-day cancellation period. Application of the right of cancellation to emergency situations would have the undesirable effect of seriously deterring credit sellers from performing in time to deal with emergencies. Subsection (5) therefore provides that the buyer may not cancel a sale if the stated conditions are met. A portion of subsection (5) is derived from Regulation Z Section 226.9(e).

4. The right to cancel provided by Section 3.502 is not exclusive. It in no way affects the right that the buyer may have independent of the Act to revoke an offer to purchase which has not been accepted by the seller, or to rescind because of fraud, duress, breach of warranty, or other causes, or under the Federal Truth in Lending Act.

**§ 3.503. [Form of Agreement or Offer; Statement of Buyer's Rights]**

(1) In a home solicitation sale, unless the buyer requests the seller to provide goods or services without delay in an emergency (subsection (5) of Section 3.502), the seller shall present to the buyer and obtain his signature to a written agreement or offer to purchase that designates as the date of the transaction the date on which the buyer actually signs and contains a statement of the buyer's rights that complies with subsection (2). A copy of any writing required by this subsection to be signed by the buyer, completed at least as to the date of the transaction and the name and mailing address of the seller, shall be given to the buyer at the time he signs the writing.

(2) The statement shall either:

(a) comply with any notice of cancellation or similar requirement of any trade regulation rule of the Federal Trade Commission which by its terms applies to the home solicitation sale; or

(b) appear under the conspicuous caption: "BUYER'S RIGHT TO CANCEL," and read as follows: "If you decide you do not want the goods or services, you may cancel this agreement by mailing a notice to the seller. The notice must say that you do not want the goods or services and must be mailed before midnight of the third business day after you sign this agreement. The notice must be mailed to: _____ ."

(insert name & mailing address of seller)

(3) Until the seller has complied with this section the buyer may cancel the home solicitation sale by notifying the seller in any manner and by any means of his intention to cancel.

**COMMENT**

The 3-day period for cancellation does not begin to run until the buyer signs a written agreement or offer to purchase complying with this section. To comply, the agreement or offer must contain the date on which the buyer actually signs it and the caption and completed statement required by subsection (2). A notice of cancellation complying with the Federal Trade Commission Rule on "door-to-door sales" complies with this section.

**§ 3.504. [Restoration of Down Payment]**

(1) Within ten days after a notice of cancellation has been received by the seller or an offer to purchase has been otherwise revoked, the seller shall tender to the buyer any payments made by the buyer, any note or other evidence of indebtedness, and any goods traded in. A provision permitting the seller to keep all or any part of any goods traded in, payment, note, or evidence of indebtedness is in violation of this section and unenforceable.

(2) If the down payment includes goods traded in, the goods shall be tendered in substantially as good condition as when received by the seller. If the seller fails to tender the goods as provided by this section, the buyer may elect to recover an amount equal to the trade-in allowance stated in the agreement.

(3) Until the seller has complied with the obligations imposed by this section the buyer may retain possession of goods delivered to him by the seller and has a lien on the goods in his possession or control for any recovery to which he is entitled.

**COMMENT**

1. The 10-day period during which the seller must tender to the buyer any payments, any evidence of indebtedness, and any goods traded in runs from the time the notice of cancellation has been received by the seller.

2. If the seller took a trade-in as part of a home solicitation sale which has been cancelled he must tender the goods traded in. The risk of loss or damage to the goods rests with the seller. If he cannot tender the goods in substantially as good condition as when received, the buyer may elect to take in cash the trade-in allowance fixed by the parties in the contract. This provision is designed to protect the buyer where goods traded in have not been tendered or have been damaged. In such case he is given an election to sue either for return of the goods or for the trade-in allowance.

3. As a means of assuring compliance by the seller, subsection (3) provides that the buyer may retain possession of any goods delivered to him by the seller with respect to a sale cancelled under Section 3.502 until the seller complies with his obligations under this section. While in possession of the goods the buyer has a lien as security for his claim against the seller.

**§ 3.505. [Duty of Buyer; No Compensation for Services Before Cancellation]**

(1) Except as provided by the provisions on retention of goods by the buyer (subsection (3) of Section 3.504), and allowing for ordinary wear and tear or consumption of the goods contemplated by the transaction, within a reasonable time after a home solicitation sale has been cancelled or an offer to purchase revoked, the buyer upon demand shall tender to the seller any goods delivered by the seller pursuant to the sale, but he is not obligated to tender at any place other than his residence. If the seller fails to demand possession of goods within a reasonable time after cancellation or revocation, the goods become the property of the buyer without obligation to pay for them. For the purpose of this section, a reasonable time is presumed to be 40 days.

(2) The buyer shall take reasonable care of the goods in his possession before cancellation or revocation and for a reasonable time thereafter, during which time the goods are otherwise at the seller's risk.

(3) If a home solicitation sale is cancelled, the seller is not entitled to compensation for any services he performed pursuant to it.

**COMMENT**

1. Subsections (1) and (2) state the obligations of the buyer in the case of a cancelled home solicitation sale. To protect the buyer from the seller who may seek to impose an obligation on the buyer by unreasonable delays in demanding delivery of the goods the seller must demand possession within a reasonable time and 40 days is presumed to be a reasonable time. Goods not demanded within a reasonable time become the property of the buyer without obligation to pay for them.

2. To protect the seller the section imposes on the buyer a duty to take reasonable care of the goods while they are in his possession. Except for this duty of care, under subsection (2) the goods delivered under a home solicitation sale are at the seller's risk both prior to and after cancellation by the buyer; a buyer may cancel a sale after destruction of the goods without his fault if the destruction occurred during the cancellation period.

3. With respect to home solicitation sales involving the sale of services it is not possible to restore the parties to their original positions if services have been performed prior to cancellation. Subsection (3) discourages a seller from performing any services during the cancellation period by requiring him to act entirely at his own risk. He is entitled to no compensation for any services performed during this period if the contract is cancelled.

## ARTICLE 4

## INSURANCE

Part 1

## INSURANCE IN GENERAL

Section
4.101. Short Title.
4.102. Scope [; Relation to Credit Insurance Act; Applicability to Parties].
4.103. Definition[s]; "Consumer Credit Insurance" [; "Credit Insurance Act"].
4.104. Creditor's Provision of and Charge for Insurance; Excess Amount of Charge.
4.105. Conditions Applying to Insurance to Be Provided by Creditor.
4.106. Unconscionability.
4.107. Maximum Charge by Creditor for Insurance.
4.108. Refund Required; Amount.
4.109. Existing Insurance; Choice of Insurer.
4.110. Charge for Insurance in Connection with a Deferral, Refinancing, or Consolidation; Duplicate Charges.
4.111. Cooperation Between Administrator and [Commissioner] of Insurance.
4.112. Administrative Action of [Commissioner] of Insurance.

Part 2

## CONSUMER CREDIT INSURANCE

4.201. Term of Insurance.
4.202. Amount of Insurance.
4.203. Filing and Approval of Rates and Forms.

Part 3

## PROPERTY AND LIABILITY INSURANCE

4.301. Property Insurance.

PART 1

## INSURANCE IN GENERAL

### § 4.101. [Short Title]

This Article shall be known and may be cited as Uniform Consumer Credit Code-Insurance.

#### COMMENT

The provisions of this Article are derived in large part from Article 4 of the U3C 1968 Text. However, a number of changes both in style and in substance have been made. The style changes are not intended to change the meaning of the provisions in which they appear.

### § 4.102. [Scope [; Relation to Credit Insurance Act; Applicability to Parties]]

[(1)] This Article applies to insurance provided or to be provided in relation to a consumer credit transaction.

[(2) This Article supplements and does not repeal the Credit Insurance Act but to the extent of inconsistency between this Act and the Credit Insurance Act this Act controls. The provisions of this Act concerning administrative controls, liabilities, and penalties do not apply to persons acting as insurers, and the similar provisions of the Credit Insurance Act do not apply to creditors and debtors.]

#### COMMENT

1. A number of provisions of this Article are derived from the NAIC Model Act, prepared by the National Association of Insurance Commissioners, "to provide for the regulation of credit life insurance and credit accident and health insurance." In jurisdictions where the NAIC Model

Act has been adopted there are many local variations in the text; and in some states where it has not been adopted parallel provisions appear in its insurance law or in insurance department regulations issued under enabling legislation. In view of these diversities this Act does not refer to the NAIC Model Act as such, but reference is made to any local version of it by the expression "Credit Insurance Act." Section 4.103(2). The scope of this Article is broader than that of the NAIC Model Act.

2. If the enacting State has enacted the NAIC Model Act or a similar statute, complete Section 4.102 as follows:

a. Remove brackets after "Scope" and before period in section heading of Section 4.102; and

b. Remove brackets before and after "(1)" and subsection (2) of Section 4.102.

3. If the enacting State has not enacted the NAIC Model Act or a similar statute, complete Section 4.102 as follows:

a. Revise section heading to read Section 4.102 [Scope]

b. Delete "[(1)]" in line 3; and

c. Delete all of subsection (2).

**§ 4.103. [Definition[s]: "Consumer Credit Insurance" [; "Credit Insurance Act"]]**

In this Act:

[(1)] "Consumer credit insurance" means insurance, except insurance on property, by which the satisfaction of debt in whole or in part is a benefit provided, but does not include

(a) insurance provided in relation to a consumer credit transaction in which a payment is scheduled more than ten years after the extension of credit;

(b) insurance issued by an insurer as an isolated transaction not related to an agreement or plan for insuring consumers of or from the creditor; or

(c) insurance indemnifying the creditor against loss due to the consumer's default.

[(2) "Credit Insurance Act" means [NAIC Model Act, or any similar statute].]

**COMMENT**

1. The usual forms of consumer credit insurance provide benefits conditioned on the death or disability of the consumer, the contracts being described as credit life insurance and credit accident and health insurance. The insured event might also be loss of earnings in other ways, as by loss of employment. A type of insurance not embraced in the term "consumer credit insurance" is that procured by a creditor to guard against the uncollectibility of his accounts. Insurance of this type, although historically and properly called "credit insurance," is conditioned on the nonpayment of debt, and does not serve any interest of consumers of the insured person. This is true also of insurance indemnifying the creditor against loss due to non-filing of instruments. By contrast, the benefit of consumer credit insurance runs to consumers as well as creditors; any payment made to the creditor by the insurer under the policy satisfies the consumer's obligation to the extent of the payment.

2. The definition of "consumer credit insurance" excludes insurance related to long-term credit, following a similar but broader exclusion from the scope of the NAIC Model Act.

3. Exceptionally, there are occasions when credit life insurance or the like is appropriate but cannot be provided under a general arrangement for insuring consumers of the creditor. On these occasions the consumer may be expected to bargain actively about the insurance feature of the credit transaction. Therefore insurance issued as an isolated transaction is excluded from the definition of consumer credit insurance. It is also excluded from the scope of the NAIC Model Act.

4. If the enacting State has enacted the NAIC Model Act or a similar statute, complete Section 4.103 as follows:

a. Remove inner brackets in section heading of Section 4.103;

b. Remove brackets before and after "(1)" in line 4 of Section 4.103;

c. Remove brackets before and after subsection (2) of Section 4.103; and

d. Describe in subsection (2) the NAIC Model Act, or any similar statute.

5. If the enacting State has not enacted the NAIC Model Act or a similar statute, complete Section 4.103 as follows:

a. Revise section heading to read Section 4.103 [*Definition: "Consumer Credit Insurance*"];

b. Delete "[(1)]" in line 4 of Section 4.103; and

c. Delete all of subsection (2) of Section 4.103.

**§ 4.104. [Creditor's Provision of and Charge for Insurance; Excess Amount of Charge]**

(1) Except as otherwise provided in this Article and subject to the provisions on additional

charges (Section 2.501) and maximum finance charges (Parts 2 and 4 of Article 2), a creditor may agree to provide insurance, and may contract for and receive a charge for insurance separate from and in addition to other charges. A creditor need not make a separate charge for insurance provided or required by him. This Act does not authorize the issuance of the insurance prohibited under any statute, or rule thereunder, governing the business of insurance.

(2) The excess amount of a charge for insurance provided for in agreements in violation of this Article is an excess charge for purposes of the provisions of the Article on Remedies and Penalties (Article 5) as to effect of violations on rights of parties (Section 5.201) and of the provisions of the Article on Administration (Article 6) as to civil actions by the Administrator (Section 6.113).

**COMMENT**

1. Subsection (1) broadly authorizes creditors to contract for and receive payments for providing insurance in the whole range of transactions within the scope of this Article. Section 4.102. A creditor may provide insurance without making a separate charge in addition to the finance charge. If, however, the creditor requires insurance in connection with a consumer credit sale or consumer loan, the fact that he includes the cost of providing it in the finance charge, giving the insurance "free," will not necessarily exclude him from restrictions under the other insurance laws or this Article.

Limitations are placed on the making of an additional or separate charge for insurance in Section 2.501, and the authorization of this section is subject to those provisions. In addition, such a charge must be limited as provided in this Article. Section 4.107.

2. This Act does not purport to define "separate charge" for insurance. The question has been raised whether there is a separate charge for insurance when a creditor's finance charge varies depending upon whether or not consumer credit insurance is provided. This Act does not resolve that question.

**§ 4.105. [Conditions Applying to Insurance to Be Provided by Creditor]**

If a creditor agrees with a consumer to provide insurance:

(1) the insurance shall be evidenced by an individual policy or certificate of insurance delivered to the consumer, or mailed to him at his address as stated by him, within 30 days after

the term of the insurance commences under the agreement between the creditor and consumer, or the creditor shall promptly notify the consumer of any failure or delay in providing the insurance; and

(2) the creditor shall pay to the consumer or his estate all proceeds of consumer credit or property insurance received by the creditor in excess of the amount to which the creditor is entitled within ten days after receipt by the creditor of the proceeds.

**§ 4.106. [Unconscionability]**

(1) In applying the provisions of this Act on unconscionability (Sections 5.108 and 6.111) to a separate charge for insurance, consideration shall be given, among other factors, to:

(a) potential benefits to the consumer including the satisfaction of his obligations;

(b) the creditor's need for the protection provided by the insurance; and

(c) the relation between the amount and terms of credit granted and the insurance benefits provided.

(2) If consumer credit insurance otherwise complies with this Article and other applicable law, neither the amount nor the term of the insurance nor the amount of a charge therefor is in itself unconscionable.

**COMMENT**

It may be shown that an agreement about insurance, like other terms of a consumer credit contract, is unconscionable, and the effects are those specified in Sections 5.108 and 6.111. However, it is the intent of this section that the issue be judged in relation to the particular risks insured. The section lists only some of the factors to be considered, and indicates that a balancing of benefits, needs, and costs is required. In general, the creditor's need for insurance protection and the consumer's potential benefit are more patent in connection with extensions of credit that are substantial as to amounts and periods; the expense of providing exceptional coverage is suspect in relation to relatively small extensions of credit. The relation between the credit terms and the insurance terms must be taken into account in applying this section.

**§ 4.107. [Maximum Charge by Creditor for Insurance]**

(1) Except as provided in subsection (2), if a creditor contracts for or receives a separate charge for insurance, the amount charged to the consumer for the insurance may not exceed the premium to be charged by the insurer, as computed at the time the charge to the consumer is determined, conforming to any rate filings required by law and made by the insurer with the [Commissioner] of Insurance.

(2) A creditor who provides consumer credit insurance in relation to open-end credit may calculate the charge to the consumer in each billing cycle by applying the current premium rate to the balance in the manner permitted with respect to finance charges by the provisions on finance charge for consumer credit sales pursuant to open-end credit (Section 2.202).

**COMMENT**

Subsection (1) generally limits the creditor's charge to the consumer for insurance to the premiums to be charged by the insurer. Subsection (2), applying to both open-end sales and loan credit, authorizes convenient methods of calculating charges that might not be permitted if subsection (1) were applied inflexibly.

**§ 4.108. [Refund Required; Amount]**

(1) Upon prepayment in full of a consumer credit transaction other than a consumer lease by the proceeds of consumer credit insurance, the consumer or his estate is entitled to a refund of any portion of a separate charge for insurance which by reason of prepayment is retained by the creditor or returned to him by the insurer, unless the charge was computed from time to time on the basis of the balances of the consumer's account.

(2) This Article does not require a creditor to grant a refund to the consumer if all refunds due to him under this Article amount to less than $1 and, except as provided in subsection (1), does not require the creditor to account to the consumer for any portion of a separate charge for

insurance because:

(a) the insurance is terminated by performance of the insurer's obligation;

(b) the creditor pays or accounts for premiums to the insurer in amounts and at times determined by the agreement between them; or

(c) the creditor receives directly or indirectly under any policy of insurance a gain or advantage not prohibited by law.

(3) Except as provided in subsection (2), the creditor shall promptly make or cause to be made an appropriate refund to the consumer with respect to any separate charge made to him for insurance if:

(a) the insurance is not provided or is provided for a shorter term than that for which the charge to the consumer for insurance was computed; or

(b) the insurance terminates before the end of the term for which it was written because of prepayment in full or otherwise.

(4) A refund required by subsection (3) is appropriate as to amount if it is computed according to a method prescribed or approved by the [Commissioner] of Insurance or a formula filed by the insurer with the [Commissioner] of Insurance at least 30 days before the consumer's right to a refund becomes determinable, unless the method or formula is employed after the [Commissioner] of Insurance notifies the insurer that he disapproves it.

**COMMENT**

1. Subsection (1) concerns a premium for consumer credit insurance, or any part of it, that is not treated by the insurer as earned, even though the insurer has paid benefits for which the premium charge was made. If the premium was the subject of a separate charge to the consumer, a refund must be made. Making the refund is not practicable, however, and is not required, if the charge has been computed on the consumer's outstanding balances. Subsection (2)(a) recognizes that the insurer may, upon performance of its obligation properly treat the premium as earned.

2. Subsection (2)(c) permits a creditor to derive from consumer credit insurance gains and advantages not prohibited by law such as dividends and refunds resulting from favorable mortality or morbidity experience with respect to insured consumers, and is predicated on the following conclusions: (1) although the gains and advantages may be large to the creditor, they are relatively insignificant to each insured consumer and the calculating, clerical, and mailing costs of returning them to insured consumers would be unreasonably disproportionate to the amounts involved, and (2) the requirement of Article 4 that premiums for consumer credit insurance be reasonable in relation to benefits (Section 4.203), if properly enforced by the State Insurance [Commissioner], will preclude the possibility of the use of consumer credit insurance as a device by creditors for concealing hidden charges from consumers.

3. Subsection (4) commits to the State Insurance [Commissioner] the responsibility for approval of methods and formulas for computing refunds that are required by the circumstances stated in subsection (3).

4. A consumer is entitled to a refund rather than a credit in the event of a required rebate of any separate charge for insurance. This precludes a creditor from holding a rebate until the contract is sufficiently paid down to have it constitute a prepayment in full which, particularly in long term contracts such as to finance a mobile home, gives the creditor free use of the consumer's money for a substantial period of time.

**§ 4.109. [Existing Insurance; Choice of Insurer]**

If a creditor requires insurance, upon notice to him the consumer has the option of providing the required insurance through an existing policy of insurance owned or controlled by the consumer, or through a policy to be obtained and paid for by the consumer, but the creditor for reasonable cause may decline the insurance provided by the consumer.

**COMMENT**

This section is directed against the practice of "tying" the grant of credit to the purchase of insurance from a particular insurer, through a particular agent, or the like, a practice prohibited by many existing statutes including the NAIC Model Act.

**§ 4.110. [Charge for Insurance in Connection with a Deferral, Refinancing, or Consolidation; Duplicate Charges]**

(1) A creditor may not contract for or receive a separate charge for insurance in connection with a deferral (Section 2.503), a refinancing (Section 2.504), or a consolidation

(Section 2.505), unless:

(a) the consumer agrees at or before the time of the deferral, refinancing, or consolidation that the charge may be made;

(b) the consumer is or is to be provided with insurance for an amount or a term, or insurance of a kind, in addition to that to which he would have been entitled had there been no deferral, refinancing, or consolidation;

(c) the consumer receives a refund or credit on account of any unexpired term of existing insurance in the amount required if the insurance were terminated (Section 4.108); and

(d) the charge does not exceed the amount permitted by this Article (Section 4.107).

(2) A creditor may not contract for or receive a separate charge for insurance which duplicates insurance with respect to which the creditor has previously contracted for or received a separate charge.

**COMMENT**

A separate charge for insurance in connection with a deferral, a refinancing, or a consolidation, is permitted only if it has been agreed to by the consumer and bears an appropriate relation to the premium. Section 4.107. No new charge may be made for a coverage to which the consumer is already entitled. Actual termination of existing insurance is not required. Subsection (1)(b) recognizes that augmenting existing insurance coverage for a new separate charge is appropriate, but that "pyramiding" charges is not. Subsection (2) explicitly prohibits pyramiding.

### § 4.111. [Cooperation Between Administrator and [Commissioner] of Insurance]

The Administrator and the [Commissioner] of Insurance shall consult and assist one another in maintaining compliance with this Article. They may jointly pursue investigations, prosecute suits, and take other official action they deem appropriate if either of them is otherwise empowered to take the action. If the Administrator is informed of a violation or suspected

violation by an insurer of this Article, or of the insurance laws, rules, and regulations of this State, he shall inform the [Commissioner] of Insurance of the circumstances.

**COMMENT**

Coordination of activities of creditors and insurers is essential to the provision of insurance related to consumer credit transactions. Accordingly, the public interest requires that the officials charged with supervising credit practices and those concerned with related insurance practices coordinate their efforts. This section encourages and empowers them to consult and work together in promoting compliance with this Article with efficiency and economy.

**§ 4.112. [Administrative Action of [Commissioner] of Insurance]**

[(1) To the extent that his responsibility under this Article requires, the [Commissioner] of Insurance shall adopt rules with respect to insurers, and with respect to refunds (Section 4.108), forms, schedules of premium rates and charges (Section 4.203), and his approval or disapproval thereof and, in case of violation, may make an order for compliance.

(2)] [The State administrative procedure act] [Each provision of the Part on Administrative Procedure and Judicial Review (Part 4) of the Article on Administration (Article 6) that applies to and governs administrative action taken by the Administrator also] applies to and governs all administrative action taken by the [Commissioner] of Insurance pursuant to this section.

**COMMENT**

1. Subsection (1) may be omitted in an enacting State in which the NAIC Model Act or a statute giving the [Commissioner] of Insurance the powers and duties provided for in subsection (1) is in force. If subsection (1) is omitted "(2)" at the beginning of subsection (2) should also be omitted.

2. If the enacting State has an adequate State administrative procedure act applying to and governing administrative action taken by the [Commissioner] of Insurance, reference should be made to it in subsection (2), otherwise Part 4 of Article 6 [Section 6.401 et seq.] should be enacted and referred to in subsection (2). The bracketed language in subsection (2) should be retained or deleted dependent upon which course is followed. See Comment to Section 6.401.

PART 2

## CONSUMER CREDIT INSURANCE

### § 4.201. [Term of Insurance]

(1) Consumer credit insurance provided by a creditor may be subject to the furnishing of evidence of insurability satisfactory to the insurer. Whether or not the evidence is required, the term of the insurance shall commence no later than when the consumer becomes obligated to the creditor or when the consumer applies for the insurance, whichever is later, except as follows:

(a) if any required evidence of insurability is not furnished until more than 30 days after the term otherwise would commence, the term may commence on the date the insurer determines the evidence to be satisfactory; or

(b) if the creditor provides insurance not previously provided covering debts previously created, the term may commence on the effective date of the policy.

(2) The originally scheduled term of consumer credit insurance shall extend at least until the due date of the last scheduled payment of the debt, except as follows:

(a) if the insurance relates to an open-end credit account, the term need extend only until payment of the debt under the account and may be sooner terminated after at least 30 days' notice to the consumer; or

(b) if the consumer is informed in writing that the insurance will be written for a specified shorter time, the term need extend only until the end of the specified time.

(3) The term of consumer credit insurance may not extend more than 15 days after the originally scheduled due date of the last scheduled payment of the debt, unless it is extended without additional cost to the consumer or as an incident to a deferral, refinancing, or

consolidation.

**COMMENT**

1. Normally, the term of consumer credit insurance provided by a creditor should be the same as the term of the debt.

2. Subsection (1) permits postponement of the effective date of consumer credit insurance coverage until after the debt is incurred:

(1) under the preamble to subsection (1), when the consumer delays his application for the insurance-coverage does not become effective at least until the consumer applies for the insurance,

(2) under subsection (1)(a), when the insurer requires the consumer to furnish evidence of insurability satisfactory to the insurer and the consumer does not furnish the evidence "until more than 30 days after the term otherwise would commence"-coverage does not become effective until the insurer determines the evidence of insurability to be satisfactory;

(3) under subsection (1)(b), when the creditor newly provides insurance with respect to debt previously created-coverage does not become effective at least until the effective date of the policy.

3. However, under subsection (1), if evidence of insurability satisfactory to the insurer is required, and is furnished within "30 days after the term otherwise would commence," coverage becomes effective when the term of the insurance otherwise would commence, e.g., the life of a consumer who less than 30 days after becoming obligated to a creditor furnishes evidence of insurability satisfactory to the insurer under a group policy insuring the lives of the creditor's consumers furnishing such evidence and who then dies is insured under the policy.

4. Subsection (2) specifies the circumstances when the term of consumer credit insurance need not extend to the due date of the last scheduled instalment of the debt.

5. Subsection (3) limits, subject to stated exceptions, the term of consumer credit insurance to 15 days after the scheduled due date of the last instalment of the debt.

**§ 4.202. [Amount of Insurance]**

(1) Except as provided in subsection (2):

(a) in the case of consumer credit insurance providing life coverage, the amount of insurance may not initially exceed the debt and, if the debt is payable in instalments, may not exceed at any time the greater of the scheduled or actual amount of the debt; or

(b) in the case of any other consumer credit insurance, the total amount of periodic benefits payable may not exceed the total of scheduled unpaid instalments of the debt, and the amount of any periodic benefit may not exceed the original amount of debt divided by the number of periodic instalments in which it is payable.

(2) If consumer credit insurance is provided in connection with an open-end credit account, the amounts payable as insurance benefits may be reasonably commensurate with the amount of debt as it exists from time to time. If consumer credit insurance is provided in connection with a commitment to grant credit in the future, the amounts payable as insurance benefits may be reasonably commensurate with the total from time to time of the amount of debt and the amount of the commitment. If the debt or the commitment is primarily for an agricultural purpose and there is no regular schedule of payments, the amounts payable as insurance benefits may equal the total of the initial amount of debt and the amount of the commitment.

**COMMENT**

1. Subsection (1) provides generally applicable limitations on the amounts of consumer credit insurance and benefits.

2. Subsection (2) provides necessarily more flexible limitations on the amounts of consumer credit insurance benefits in connection with open-end credit accounts, credit commitments, and debt and credit commitments for an agricultural purpose.

3. Experience has demonstrated that limitations of these kinds are essential to the effectiveness of the requirement of Section 4.203(2) that premium rates be not unreasonable in relation to the benefits provided by consumer credit insurance.

**§ 4.203. [Filing and Approval of Rates and Forms]**

(1) A creditor may not use a form or a schedule of premium rates or charges, the filing of which is required by this section, if the [Commissioner] of Insurance has disapproved the form or schedule and has notified the insurer of his disapproval. A creditor may not use a form or

schedule unless:

(a) the form or schedule has been on file with the [Commissioner] of Insurance for 30 days, or has earlier been approved by him; and

(b) the insurer has complied with this section with respect to the insurance.

(2) Except as provided in subsection (3), all policies, certificates of insurance, notices of proposed insurance, applications for insurance, endorsements, and riders relating to consumer credit insurance delivered or issued for delivery in this State, and the schedules of premium rates or charges pertaining thereto, shall be filed by the insurer with the [Commissioner] of Insurance. Within 30 days after the filing of any form or schedule, he shall disapprove it if the premium rates or charges are unreasonable in relation to the benefits provided under the form, or if the form contains provisions which are unjust, unfair, inequitable, or deceptive, encourage misrepresentation of the coverage, or are contrary to any provision of the [Insurance Code] or of any rule or regulation promulgated thereunder.

(3) If a group policy of consumer credit insurance has been delivered in another state, the forms to be filed by the insurer with the [Commissioner] of Insurance are the group certificates and notices of proposed insurance. He shall approve them if:

(a) they provide the information that would be required if the group policy were delivered in this State; and

(b) the applicable premium rates or charges do not exceed those established by his rules or regulations.

**COMMENT**

1. Subsections (1) and (2) reaffirm and broaden the powers of the [Commissioner] of Insurance under the NAIC Model Act as to forms and schedules of premium rates or charges relating to consumer credit insurance. Unlike the NAIC Model Act which is directed primarily to insurers, this section is directed to both creditors and insurers. Moreover, in its formulation as

to the relationship of premium rates and charges to the benefits provided, subsection (2) follows New York Insurance Law Section 154.7. That provision, as construed by the New York Court of Appeals in Old Republic Life Insurance Company v. Wikler, 9 N.Y.2d 524, 215 N.Y.S.2d 481, 175 N.E.2d 147 (1961), gives the New York Superintendent of Insurance ample power as to premium rates for credit life and accident and health insurance. Doubt, whether reasonable or not, has been expressed whether equivalent power is conferred by the corresponding formulation of Section 7B of the NAIC Model Act.

2. Subsection (3) facilitates insuring, as a group, the consumers of a creditor operating across state lines.

## PART 3

## PROPERTY AND LIABILITY INSURANCE

### § 4.301. [Property Insurance]

(1) A creditor may not contract for or receive a separate charge for insurance against loss of or damage to property, unless:

(a) the insurance covers a substantial risk of loss of or damage to property related to the credit transaction;

(b) the amount, terms, and conditions of the insurance are reasonable in relation to the character and value of the property insured or to be insured; and

(c) the term of the insurance is reasonable in relation to the terms of credit.

(2) The term of the insurance is reasonable if it is customary and does not extend substantially beyond a scheduled maturity.

(3) With respect to a transaction, except pursuant to open-end credit, a creditor may not contract for or receive a separate charge for insurance against loss of or damage to property, unless the amount financed exclusive of charges for the insurance is $300 or more and the value of the property is $300 or more.

(4) With respect to a transaction pursuant to open-end credit, the Administrator may adopt

rules consistent with the principles set out in subsections (1) and (2) prescribing whether, and the conditions under which, a creditor may contract for or receive a separate charge for insurance against loss of or damage to property.

(5) The amounts of $300 in subsection (3) are subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

**COMMENT**

1. Subsection (1) imposes restrictions on property insurance similar to those provided by a number of retail instalment sales acts.

2. Subsection (2) permits reasonable flexibility so that the expiration of the term of property insurance need not coincide exactly with the scheduled maturity of the debt.

3. With respect to transactions other than pursuant to open-end credit, subsection (3) prohibits a separate charge for property insurance when either the amount of debt or the value of the property to be insured is relatively small.

4. With respect to transactions pursuant to open-end credit, fixed restrictions are not uniformly workable, *e.g.*, in the case of loans pursuant to open-end credit the value of the collateral could be much greater than the balance of the account while in the case of sales pursuant to open-end credit the balance of the account could include debt owing for services or consumables and be much larger than the value of the property securing the debt. However, neither is it desirable to exclude such transactions from restriction. Subsection (4) permits the Administrator to adopt rules consistent with the basic protective provisions of subsections (1) and (2) that will allow insurance charges to be made in appropriate circumstances in open-end credit transactions.

**§ 4.302. [Insurance on Creditor's Interest Only]**

If a creditor contracts for or receives a separate charge for insurance against loss of or damage to property, the risk of loss or damage not willfully caused by the consumer is on the consumer only to the extent of any deficiency in the effective coverage of the insurance, even though the insurance covers only the interest of the creditor.

**COMMENT**

This section prohibits a separate charge to the consumer for property insurance covering

the creditor's interest in property unless the consumer also receives the benefit of the insurance to the extent he does not willfully cause the loss or damage, risk of which is insured. "Single interest" property insurance for which the creditor makes a separate charge to the consumer may not provide for subrogation of the insurer to the rights of the creditor as to any loss or damage not willfully caused by the consumer. See also Section 2.501(2).

**§ 4.303. [Liability Insurance]**

A creditor may not contract for or receive a separate charge for insurance against liability unless the insurance covers a substantial risk of liability arising out of the ownership or use of property related to the credit transaction.

**COMMENT**

This section imposes restrictions with respect to liability insurance comparable to those imposed with respect to property insurance by subsection (1) of Section 4.301.

**§ 4.304. [Cancellation by Creditor]**

This section does not apply to an insurance premium loan. A creditor may request cancellation of a policy of property or liability insurance only after the consumer's default or in accordance with a written authorization by the consumer. In either case the cancellation does not take effect until written notice is delivered to the consumer or mailed to him at his address as stated by him. The notice shall state that the policy may be cancelled on a date not less than ten days after the notice is delivered, or, if the notice is mailed, not less than 13 days after it is mailed. A cancellation may not take effect until those times.

**COMMENT**

This section requires advance written notice, by either the creditor or the insurer of the prospective cancellation of property or liability insurance provided in connection with a consumer credit transaction. It is not applicable to lenders engaged in insurance premium financing. See Sections 5.110 and 5.111.

ARTICLE 5

## REMEDIES AND PENALTIES

Part 1

## LIMITATIONS ON CREDITORS' REMEDIES

Section


Part 2

## CONSUMERS' REMEDIES



Part 3

## CRIMINAL PENALTIES



PART 1

## LIMITATIONS ON CREDITORS' REMEDIES

### § 5.101. [Short Title]

This Article shall be known and may be cited as Uniform Consumer Credit Code-Remedies and Penalties.

### § 5.102. [Scope]

This Part applies to actions or other proceedings to enforce rights arising from consumer credit transactions, to extortionate extensions of credit (Section 5.107), and to unconscionability (Section 5.108).

### COMMENT

Section 1.201 states the territorial applicability of this Act. Section 1.109 provides for the applicability of this Act by written agreement.

### § 5.103. [Restrictions on Deficiency Judgments]

(1) This section applies to a deficiency on a consumer credit sale of goods or services and on a consumer loan in which the lender is subject to claims and defenses arising from sales and leases (Section 3.405). A consumer is not liable for a deficiency unless the creditor had disposed of the goods in good faith and in a commercially reasonable manner.

(2) If the seller repossesses or voluntarily accepts surrender of goods that were the subject of the sale and in which he has a security interest, the consumer is not personally liable to the seller for the unpaid balance of the debt arising from the sale of a commercial unit of goods of which the cash sale price was $1,750 or less, and the seller is not obligated to resell the collateral unless the consumer has paid 60 per cent or more of the cash price and has not signed after default a statement renouncing his rights in the collateral.

(3) If the seller repossesses or voluntarily accepts surrender of goods that were not the

subject of the sale but in which he has a security interest to secure a debt arising from a sale of goods or services or a combined sale of goods and services and the cash price of the sale was $1,750 or less, the consumer is not personally liable to the seller for the unpaid balance of the debt arising from the sale, and the seller's duty to dispose of the collateral is governed by the provisions on disposition of collateral (Part 5 of Article 9) of the Uniform Commercial Code.

(4) If the lender takes possession or voluntarily accepts surrender of goods in which he has a purchase money security interest to secure a debt arising from a consumer loan in which the lender is subject to claims and defenses arising from sales and leases (Section 3.405) and the net proceeds of the loan paid to or for the benefit of the consumer were $1,750 or less, the consumer is not personally liable to the lender for the unpaid balance of the debt arising from that loan and the lender's duty to dispose of the collateral is governed by the provisions on disposition of collateral (Part 5 of Article 9) of the Uniform Commercial Code.

(5) For the purpose of determining the unpaid balance of consolidated debts or debts pursuant to open-end credit, the allocation of payments to a debt shall be determined in the same manner as provided for determining the amount of debt secured by various security interests (Section 3.303).

(6) The consumer may be held liable in damages to the creditor if the consumer has wrongfully damaged the collateral or if, after default and demand, the consumer has wrongfully failed to make the collateral available to the creditor.

(7) If the creditor elects to bring an action against the consumer for a debt arising from a consumer credit sale of goods or services or from a consumer loan in which the lender is subject to claims and defenses arising from sales and leases (Section 3.405), when under this section he would not be entitled to a deficiency judgment if he took possession of the collateral, and obtains

judgment:

(a) he may not take possession of the collateral, and

(b) the collateral is not subject to levy or sale on execution or similar proceedings pursuant to the judgment.

(8) The amounts of $1,750 in subsections (2), (3) and (4) are subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

## COMMENT

1. Where there has been a default with respect to a secured consumer credit transaction, the rights of the creditor and consumer are controlled by Part 5 (Default) of UCC Article 9 [U.C.C. § 9-501 et seq.], except to the extent that such rights are changed by this Act. Under the UCC the creditor has the right to take possession of the collateral on default subject to applicable constitutional limitations (compare Fuentes v. Shevin, 407 U.S. 67, 32 L.Ed.2d 556 (1972) and Mitchell v. W.T. Grant Co., 94 S.Ct. 1895, 416 U.S. 600, 40 L.Ed.2d 406 (1974) with Adams v. Egley, 338 F.Supp. 614 (S.D.Cal.1972), rev'd sub nom. Adams v. Southern California First National Bank, 492 F.2d 324 (9th Cir.1974)), and may proceed without judicial process. UCC Section 9-503. The creditor may sell, lease or otherwise dispose of the collateral in public or private proceedings, and may buy at his own sale. The consumer is entitled to reasonable notification of the time and place of any public sale and reasonable notification of the time after which the collateral will be disposed of privately. UCC Section 9-504(1) and (3). Proceeds are applied first to the expenses of repossession and disposition and then to satisfaction of the indebtedness. Any excess is paid to the consumer and the consumer is liable for any deficiency. UCC Section 9-504(1) and (2). If the consumer has paid 60 per cent of the cash price in the case of a sale or 60 per cent of the principal in the case of a loan, and has not signed after default a statement renouncing his rights, the creditor must dispose of the collateral. If the creditor fails to dispose of the collateral within 90 days after repossession the consumer may recover in conversion or alternatively under UCC Section 9-507(1). In all other cases the creditor may retain the collateral in satisfaction of the debt, if the consumer does not object after receipt of notification. UCC Section 9-505. The consumer has a right to redeem the collateral at any time before disposition of the collateral or satisfaction of the obligation, by tendering fulfillment of all obligations secured by the collateral as well as expenses of the creditor. UCC Section 9-506.

2. The provisions of the UCC outlined above are modified to some extent by this section with respect to proceedings to enforce rights arising from consumer credit sales and consumer loans in which the lender is subject to claims and defenses arising from sales and leases (Section 3.405). For both types of transactions, this section adopts the position of that line of cases under the UCC that directly or indirectly deny the creditor a deficiency if the creditor has not disposed of the collateral in good faith and in a commercially reasonable manner. See, *e.g.,* Atlas Thrift Co. v. Horan, 27 Cal.App.3d 999, 104 Cal.Rptr. 315 (Cal.Ct.App.3d Dist.1972).

3. With respect to a consumer credit sale of a commercial unit of goods of which the cash price is $1750 or less, a seller who repossesses or voluntarily accepts surrender of the goods sold in which he has a security interest may not obtain a deficiency judgment against the consumer if the proceeds on disposition of the goods are insufficient to pay the indebtedness and the expenses of the seller. The seller need not resell the goods unless the consumer has paid 60 per cent or more of the cash price and has not signed after default a statement renouncing his rights in the collateral. In cases of sales of $1750 or less, this section gives to the seller the option of either suing for the unpaid balance or repossessing, but he may not do both. The amount of $1750 in all subsections of this section in which it appears is derived from the Report of the National Commission on Consumer Finance. The concept of "commercial unit" is borrowed from UCC Section 2-105(6) and is employed to preclude the argument that subsection (2) is inapplicable to a consumer credit sale of a stove, a refrigerator, a washer, a dryer and a TV set for a total cash price of more than $1750 when each of these "commercial units" does not separately cost more than $1750.

4. The seller may have a security interest in collateral other than goods sold in the consumer credit sale. The Act allows the seller to take a security interest in collateral other than goods sold in some sales of services, in consumer credit sales primarily for agricultural purposes, and in cross-collateral transactions in which a seller makes more than one sale to one consumer and takes a security interest in goods sold in one sale to secure debt arising from other sales. Sections 3.301 and 3.302. In these cases, if the cash price of the sale is $1750 or less, the seller who repossesses or voluntarily accepts surrender of collateral may not obtain a deficiency judgment against the consumer. The rights of the consumer with respect to compulsory disposition of collateral which was not the subject of the sale and recovery of any surplus on disposition are defined in UCC Sections 9-504 and 9-505.

5. If a lender makes a consumer loan in which the net proceeds paid to or for the benefit of the consumer are $1750 or less to enable the consumer to purchase goods under circumstances where the lender is subject to claims and defenses arising from the sale of the goods (Section 3.405) and pursuant to a security interest acquired in the goods repossesses or voluntarily accepts surrender of the goods, the lender may not obtain a deficiency judgment against the consumer if the proceeds on disposition of the goods are insufficient to pay the indebtedness and the expenses of the lender with respect to that loan. Subsection (4) is limited to the described type of transaction as only this type of transaction is an alternative to a consumer credit sale in which the seller in financing the purchase would be limited by this section. The rights of the consumer with respect to compulsory disposition of the collateral and recovery of any surplus on disposition are defined in UCC Sections 9-504 and 9-505.

6. Subsection (6) is designed to protect creditors against consumers who wrongfully damage collateral or who wrongfully refuse to surrender collateral. In addition to the right of the creditor to repossess the collateral, the subsection gives to the creditor a right of action for damages for the loss of value of the collateral resulting from wrongful injury to the goods or, in the case of wrongful refusal to surrender the collateral, for any loss suffered by the creditor because of his inability to repossess.

7. Subsection (7) prohibits a creditor not entitled to a deficiency judgment under this section from achieving substantially the same result by first obtaining judgment for the debt and then levying on the collateral on execution.

**§ 5.104. [No Garnishment Before Judgment]**

Before entry of judgment in an action against a consumer for debt arising from a consumer credit transaction, the creditor may not attach unpaid earnings of the consumer by garnishment or like proceedings.

**COMMENT**

This section, within the scope of this Act, carries out the mandate of the Supreme Court in the landmark decision of Sniadach v. Family Finance Corp., 89 S.Ct. 1820, 395 U.S. 337, 23 L.Ed.2d 349 (1969) and further adopts the recommendation of the Report of the National Commission on Consumer Finance that prejudgment garnishment, even of nonresident consumers, should be abolished.

**§ 5.105. [Limitation on Garnishment]**

(1) For purposes of this Part:

(a) "disposable earnings" means that part of the earnings of an individual remaining after the deduction from those earnings of amounts required by law to be withheld; and

(b) "garnishment" means any legal or equitable procedure through which earnings of an individual are required to be withheld for payment of a debt.

(2) The maximum part of the aggregate disposable earnings of an individual for any workweek which is subjected to garnishment to enforce payment of a judgment arising from a consumer credit transaction may not exceed the lesser of:

(a) 25 per cent of his disposable earnings for that week, or

(b) the amount by which his disposable earnings for that week exceed 40 times the Federal minimum hourly wage prescribed by Section 6(a)(1) of the Fair Labor Standards Act of

1938, U.S.C. tit. 29, § 206(a)(1), in effect at the time the earnings are payable.

In case of earnings for a pay period other than a week, the Administrator shall prescribe by rule a multiple of the Federal minimum hourly wage equivalent in effect to that set forth in paragraph (b).

(3) No court may make, execute, or enforce an order or process in violation of this section.

(4) At any time after entry of a judgment in favor of a creditor in an action against a consumer for debt arising from a consumer credit transaction, the consumer may file with the court his verified application for an order exempting from garnishment pursuant to that judgment, for an appropriate period of time, a greater portion or all of his aggregate disposable earnings for a workweek or other applicable pay period than is provided for in subsection (2). He shall designate in the application the portion of his earnings not exempt from garnishment under this section and other law, the period of time for which the additional exemption is sought, describe the judgment with respect to which the application is made, and state that the designated portion as well as his earnings that are exempt by law are necessary for the maintenance of him or a family supported wholly or partly by the earnings. Upon filing a sufficient application under this subsection, the court may issue any temporary order necessary under the circumstances to stay enforcement of the judgment by garnishment, shall set a hearing on the application not less than [five] nor more than [ten] days after the date of filing of the application, and shall cause notice of the application and the hearing date to be served on the judgment creditor or his attorney of record. At the hearing, if it appears to the court that all or any portion of the earnings sought to be additionally exempt are necessary for the maintenance of the consumer or a family supported wholly or partly by the earnings of the consumer for all or any part of the time requested in the application, the court shall issue an order granting the application to that extent; otherwise it shall

deny the application. The order is subject to modification or vacation upon further application of any party to it upon a showing of changed circumstances after a hearing upon notice to all interested parties.

**COMMENT**

1. This section is derived from the CCPA (15 U.S.C. § 1601 et seq., specifically §§ 1672, 1673). The exemption has been increased from thirty times the minimum hourly wage to forty in the belief that the higher figure is justified in consumer credit transactions, a belief substantiated by the recommendation of the Report of the National Commission on Consumer Finance.

2. Section 5.104 prohibits all garnishment before judgment for collection of consumer debt. This section limits the use of garnishment after judgment for collection of consumer debt. It complements rather than displaces local garnishment laws and applies only to garnishment and like proceedings directed toward one other than the consumer, *e.g.*, an employer. The consumer's interests are adequately protected in proceedings supplementary to judgment in which the consumer is personally before the court and the court is therefore able to take his and his dependents' needs into consideration in granting an order against him for payment of a judgment on a consumer debt.

3. Subsection (2) is designed to assure the consumer that under normal circumstances he will retain enough of his earnings to be able to support himself and his dependents by exempting a portion of his earnings from garnishment to enforce judgments for consumer debts. The exemption is based on the concept of "disposable earnings" rather than gross earnings. Disposable earnings are defined to include only those earnings which the consumer can spend after deductions required by law. If the law requires a portion of the consumer's wages to be withheld from him, the consumer has no power of disposition with respect to that portion, and that portion is therefore not included in disposable wages. Thus, amounts required to be withheld for social security or income taxes, amounts withheld pursuant to compulsory retirement, health insurance or similar plans imposed by law and amounts withheld because of a garnishment or levy by another creditor are excluded from "disposable earnings." However, if amounts are withheld from the consumer's earnings by the employer pursuant to a request by the employee or pursuant to a contract made by the employee or on his behalf by a labor union or similar organization, the amounts withheld are included in "disposable earnings" since the deduction is not required by law.

4. Subsection (2) sets limits on the maximum amount of disposable earnings that a creditor in a consumer credit transaction may reach by garnishment. There is a double test. The creditor may not garnish more than (a) 25 per cent of disposable earnings for any workweek or (b) the amount by which disposable earnings exceed 40 times the Federal minimum hourly wage, whichever is less.

*Example:* Assume that the Federal minimum hourly wage is $2.00. An unmarried consumer who has no dependents and therefore claims one withholding exemption earns $3.10

an hour. Wages are paid for a weekly pay period. During that period the consumer worked 38 hours. His gross wages were $117.80. His employer withholds Federal income taxes of $16.60, social security taxes of $6.89, union dues of $1.25 pursuant to a contract with the union, and $5.00 for a Christmas savings plan of which the consumer is a member. Net wages paid to the employee are $88.06. "Disposable earnings" are $94.31; 25 per cent of disposable earnings is $23.57; 40 times the minimum hourly wage of $2.00 is $80.00; the excess of disposable earnings over $80.00 is $14.31. Under subsection (2), the creditor may garnish no more than $14.31, the lesser of $23.57 and $14.31.

5. Under unusual circumstances such as illness, an abnormally large number of dependents, or similar conditions, some or all of the amount of disposable earnings subject to garnishment by subsection (2) may be necessary for the support of the consumer or his family for a brief or an extended period of time. Subsection (4) affords the consumer in that instance an opportunity to be heard and introduce evidence, and in the event undue hardship is proved to the satisfaction of the court, the amount of the garnishment may be reduced or the garnishment removed. In this respect, subsection (4) follows a recommendation of the Report of the National Commission on Consumer Finance.

6. This section is not meant to displace other provisions of state law which may provide additional protection to the consumer. For example, if state law exempts 90 per cent of earnings, only $11.78 or 10 per cent of earnings of $117.80 may be collected under the garnishment in the example above.

7. There is no private right of action for monetary relief vested by this Act in the consumer for violation of this section; enforcement is expected to come primarily through the restriction imposed on the court in subsection (3) and appropriate action by the Administrator (Article 6, Part 1). However, this should not be construed as precluding an individual consumer from obtaining appropriate injunctive or other non-monetary relief for violation of the section, or from obtaining monetary relief consistent with Section 1.103 against a creditor for wrongful seizure of exempt earnings. See, *e.g.*, Albrecht v. Treitschke, 17 Neb. 205, 22 N.W. 418 (1885).

**§ 5.106. [No Discharge From Employment for Garnishment]**

An employer may not discharge an employee for the reason that a creditor of the employee has subjected or attempted to subject unpaid earnings of the employee to garnishment or like proceedings directed to the employer for the purpose of paying a judgment arising from a consumer credit transaction.

**COMMENT**

1. The employee's remedy for violation of this section is found in Section 5.201(5).

2. This section is derived from the CCPA (15 U.S.C., § 1601 et seq., specifically § 1674),

but it prohibits an employer from discharging an employee by reason of any garnishment (whether one or more) under a judgment arising from a consumer credit transaction.

**§ 5.107. [Extortionate Extensions of Credit]**

(1) If it is the understanding of the creditor and the consumer at the time an extension of credit is made that delay in making repayment or failure to make repayment could result in the use of violence or other criminal means to cause harm to the person, reputation, or property of any person, the repayment of the extension of credit is unenforceable through civil judicial processes against the consumer.

(2) If it is shown that an extension of credit was made at an annual rate exceeding 45 per cent calculated according to the actuarial method and that the creditor then had a reputation for the use or threat of use of violence or other criminal means to cause harm to the person, reputation, or property of any person to collect extensions of credit or to punish the non-repayment thereof, there is prima facie evidence that the extension of credit was unenforceable under subsection (1).

**COMMENT**

1. This section is derived from 18 U.S.C. § 892, as added by Title II of the CCPA.

2. This section is intended to facilitate federal prosecutions with respect to making extortionate extensions of credit by providing one of the elements required for a prima facie case under the CCPA provision referred to above, viz., that the repayment of the extension of credit would be unenforceable through civil judicial processes against the consumer.

**§ 5.108. [Unconscionability; Inducement by Unconscionable Conduct; Unconscionable Debt Collection]**

(1) With respect to a transaction that is, gives rise to, or leads the debtor to believe will give rise to, a consumer credit transaction, if the court as a matter of law finds:

(a) the agreement or transaction to have been unconscionable at the time it was

made, or to have been induced by unconscionable conduct, the court may refuse to enforce the agreement; or

(b) any term or part of the agreement or transaction to have been unconscionable at the time it was made, the court may refuse to enforce the agreement, enforce the remainder of the agreement without the unconscionable term or part, or so limit the application of any unconscionable term or part as to avoid any unconscionable result.

(2) With respect to a consumer credit transaction, if the court as a matter of law finds that a person has engaged in, is engaging in, or is likely to engage in unconscionable conduct in collecting a debt arising from that transaction, the court may grant an injunction and award the consumer any actual damages he has sustained.

(3) If it is claimed or appears to the court that the agreement or transaction or any term or part thereof may be unconscionable, or that a person has engaged in, is engaging in, or is likely to engage in unconscionable conduct in collecting a debt, the parties shall be afforded a reasonable opportunity to present evidence as to the setting, purpose, and effect of the agreement or transaction or term or part thereof, or of the conduct, to aid the court in making the determination.

(4) In applying subsection (1), consideration shall be given to each of the following factors, among others, as applicable:

(a) belief by the seller, lessor, or lender at the time a transaction is entered into that there is no reasonable probability of payment in full of the obligation by the consumer or debtor;

(b) in the case of a consumer credit sale or consumer lease, knowledge by the seller or lessor at the time of the sale or lease of the inability of the consumer to receive substantial benefits from the property or services sold or leased;

(c) in the case of a consumer credit sale or consumer lease, gross disparity between

the price of the property or services sold or leased and the value of the property or services measured by the price at which similar property or services are readily obtainable in credit transactions by like consumers;

(d) the fact that the creditor contracted for or received separate charges for insurance with respect to a consumer credit sale or consumer loan with the effect of making the sale or loan, considered as a whole, unconscionable; and

(e) the fact that the seller, lessor, or lender has knowingly taken advantage of the inability of the consumer or debtor reasonably to protect his interests by reason of physical or mental infirmities, ignorance, illiteracy, inability to understand the language of the agreement, or similar factors.

(5) In applying subsection (2), consideration shall be given to each of the following factors, among others, as applicable:

(a) using or threatening to use force, violence, or criminal prosecution against the consumer or members of his family;

(b) communicating with the consumer or a member of his family at frequent intervals or at unusual hours or under other circumstances so that it is a reasonable inference that the primary purpose of the communication was to harass the consumer;

(c) using fraudulent, deceptive, or misleading representations such as a communication which simulates legal process or which gives the appearance of being authorized, issued, or approved by a government, governmental agency, or attorney at law when it is not, or threatening or attempting to enforce a right with knowledge or reason to know that the right does not exist;

(d) causing or threatening to cause injury to the consumer's reputation or economic

status by disclosing information affecting the consumer's reputation for credit-worthiness with knowledge or reason to know that the information is false; communicating with the consumer's employer before obtaining a final judgment against the consumer, except as permitted by statute or to verify the consumer's employment; disclosing to a person, with knowledge or reason to know that the person does not have a legitimate business need for the information, or in any way prohibited by statute, information affecting the consumer's credit or other reputation; or disclosing information concerning the existence of a debt known to be disputed by the consumer without disclosing that fact; and

(e) engaging in conduct with knowledge that like conduct has been restrained or enjoined by a court in a civil action by the Administrator against any person pursuant to the provisions on injunctions against fraudulent or unconscionable agreements or conduct (Section 6.111).

(6) If in an action in which unconscionability is claimed the court finds unconscionability pursuant to subsection (1) or (2), the court shall award reasonable fees to the attorney for the consumer or debtor. If the court does not find unconscionability and the consumer or debtor claiming unconscionability has brought or maintained an action he knew to be groundless, the court shall award reasonable fees to the attorney for the party against whom the claim is made. In determining attorney's fees, the amount of the recovery on behalf of the consumer is not controlling.

(7) The remedies of this section are in addition to remedies otherwise available for the same conduct under law other than this Act, but double recovery of actual damages may not be had.

(8) For the purpose of this section, a charge or practice expressly permitted by this Act is

not in itself unconscionable.

## COMMENT

1. Subsections (1) and (3) are derived in significant part from UCC Section 2-302. Subsection (1), as does UCC Section 2-302, provides that a court can refuse to enforce or can adjust an agreement or part of an agreement that was unconscionable on its face at the time it was made. However, many agreements are not in and of themselves unconscionable according to their terms, but they would never have been entered into by a consumer if unconscionable means had not been employed to induce the consumer to agree to the contract. It would be a frustration of the policy against unconscionable contracts for a creditor to be able to utilize unconscionable acts or practices to obtain an agreement. Consequently subsection (1) also gives to the court the power to refuse to enforce an agreement if it finds as a matter of law that it was induced by unconscionable conduct. Finally, subsection (1) includes provisions for court determination of unconscionability in a transaction that a consumer is led to believe will give rise to a consumer credit transaction so that, for example, a seller cannot bind the consumer to a short term sale contract payable in a lump sum on the assurance the seller will secure financing for the consumer, and then inform the consumer financing is unavailable and keep the downpayment or goods traded in as a penalty for non-payment.

In subsection (3) the omission of the adjective "commercial" found in UCC Section 2-302 from the provision concerning the presentation of evidence as to the conduct's or contract's "setting, purpose, and effect" is deliberate. Unlike the UCC, this section is concerned only with transactions involving consumers, and the relevant standard of conduct for purposes of this section is not that which might be acceptable as between knowledgeable merchants but rather that which measures acceptable conduct on the part of a businessman toward a consumer.

2. Subsection (2) provides a consumer remedy for unconscionable conduct in the collection of consumer credit debts. In recent years, there has been much legislative activity in this area. In subjecting this type of creditor conduct to the concept of unconscionability, this section provides a more flexible device for halting multifarious activities than the specific and somewhat rigid treatment contained in other legislation, and follows the lead of Section 6.111 of this Act which affords the Administrator the means to deal with this type of practice. Indeed this section considered as a whole confers on the consumer the ability to obtain relief in basically the same situations the Administrator is authorized to seek relief under Section 6.111, although not necessarily under the same conditions, *e.g.*, no course of conduct is required. The section is not exclusive, however; subsection (7) stipulates that the remedies of this section are in addition to remedies otherwise available for the same conduct under law other than this Act so as to preserve, for example, the developing remedy for abusive debt collection in tort.

3. This section is intended to make it possible for the courts to police conduct which is, and contracts or clauses which are found to be unconscionable. The basic test is whether, in the light of the background and setting of the market, the needs of the particular trade or case, and the condition of the particular parties to the conduct or contract, the conduct involved is, or the contract or clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time the conduct occurs or is threatened or at the time of the making of the

contract. The principle is one of the prevention of oppression and unfair surprise and not the disturbance of reasonable allocation of risks or reasonable advantage because of superior bargaining power or position. The particular facts involved in each case are of utmost importance since certain conduct, contracts or contractual provisions may be unconscionable in some situations but not in others. The following cases illustrate prior application of the doctrine of unconscionability: Williams v. Walker-Thomas Furn. Co., 350 F.2d 445, 121 U.S.App.D.C. 315 (1965); American Home Improvement, Inc. v. MacIver, 105 N.H. 435, 201 A.2d 886 (1964); Ellsworth Dobbs, Inc. v. Johnson, 50 N.J. 528, 236 A.2d 843 (1967); Unico v. Owen, 50 N.J. 101, 232 A.2d 405 (1967); Henningsen v. Bloomfield Motors, Inc., 32 N.J. 358, 161 A.2d 69 (1960); Frostifresh Corp. v. Reynoso, 54 Misc.2d 119, 281 N.Y.S.2d 964 (Sup.Ct., App.Term, 2d Dept.1967), rev'g in part 52 Misc.2d 26, 274 N.Y.S.2d 757 (Nassau Co.1966).

4. Subsections (4) and (5) list a number of specific factors to be considered on the issue of unconscionability. It is impossible to anticipate all of the factors and considerations which may support a conclusion of unconscionability in a given instance so the listing is not exclusive. The following are illustrative of individual transactions which would entitle a consumer to relief under this section:

Under subsection (4)(a), a sale of goods to a low income consumer without expectation of payment but with the expectation of repossessing the goods sold and reselling them at a profit;

Under subsection (4)(b), a sale to a Spanish speaking laborer-bachelor of an English language encyclopedia set, or the sale of two expensive vacuum cleaners to two poor families sharing the same apartment and one rug;

Under subsection (4)(c), a home solicitation sale of a set of cookware or flatware to a housewife for $375 in an area where a set of comparable quality is readily available on credit in stores for $125 or less;

Under subsection (4)(e), a sale of goods on terms known by the seller to be disadvantageous to the consumer where the written agreement is in English, the consumer is literate only in Spanish, the transaction was negotiated orally in Spanish by the seller's salesman, and the written agreement was neither translated nor explained to the consumer, but the mere fact a consumer has little education and cannot read or write and must sign with an "X" is not itself determinative of unconscionability;

Under subsection (5)(a) and (c), threatening that the creditor will have the consumer thrown in jail and her welfare checks stopped if the debt is not paid.

5. Since the remedies of this section are non-monetary in nature except for the ability to recover actual damages for unconscionable debt collection, subsection (6) authorizes an award of reasonable attorneys fees to the successful consumer or debtor. However, to discourage litigation seeking exculpation from merely bad bargains, provision is also made for recovery by a creditor if the court does not find unconscionability and the consumer's or debtor's action was known by the consumer or debtor to be groundless.

6. Subsection (8) prohibits a finding that a charge or practice expressly permitted by this Act is in itself unconscionable. However, even though a practice or charge is authorized by this Act, the totality of a particular creditor's conduct may show that the practice or charge is part of unconscionable conduct. Therefore, in determining unconscionability, the creditor's total conduct, including that part of his conduct which is in accordance with the provisions of this Act, may be considered.

**§ 5.109. [Default]**

An agreement of the parties to a consumer credit transaction with respect to default on the part of the consumer is enforceable only to the extent that:

(1) the consumer fails to make a payment as required by agreement; or

(2) the prospect of payment, performance, or realization of collateral is significantly impaired; the burden of establishing the prospect of significant impairment is on the creditor.

**COMMENT**

1. One of the vital terms of every consumer credit agreement is that which sets forth the criteria which will constitute default. By its nature it is not a term that is agreed to by the parties but rather one that is dictated by the creditor. It is appropriate, therefore, that its content and implications be confined by the law so as to prevent abuse. This section is intended to accomplish that.

2. The section recognizes that there are two entirely distinct sets of circumstances which might constitute default on an instalment obligation. First and most common is the failure to pay an instalment as required. A default of this type is susceptible of being cured by the consumer without impairing a continuing contractual relationship. See Section 5.110. A second type of default relates to behavior of the consumer which endangers the prospect of a continuing relationship. It may be insolvency, illegal activity, or an impending removal of assets from the jurisdiction. There must, however, be circumstances present which significantly impair the relationship. The burden of proof is on the creditor to justify his action on a claim of default of this type.

**§ 5.110. [Notice of Consumer's Right to Cure]**

(1) With respect to a consumer credit transaction, after a consumer has been in default for ten days for failure to make a required payment and has not voluntarily surrendered possession of goods that are collateral, a creditor may give the consumer the notice described in this section. A

creditor gives notice to the consumer under this section when he delivers the notice to the consumer or mails the notice to him at his residence (subsection (6) of Section 1.201).

(2) Except as provided in subsection (3), the notice shall be in writing and conspicuously state: the name, address, and telephone number of the creditor to whom payment is to be made, a brief identification of the credit transaction, the consumer's right to cure the default, and the amount of payment and date by which payment must be made to cure the default. A notice in substantially the following form complies with this subsection:

(name, address, and telephone number of creditor) _____.

(account number, if any) _____.

(brief identification of credit transaction) _____.

(date) _____ is the LAST DAY FOR PAYMENT

(amount) _____ is the AMOUNT NOW DUE

You are late in making your payment(s). If you pay the AMOUNT NOW DUE (above) by the LAST DAY FOR PAYMENT (above), you may continue with the contract as though you were not late. If you do not pay by that date, we may exercise our rights under the law.

If you are late again in making your payments, we may exercise our rights without sending you another notice like this one. If you have questions, write or telephone the creditor promptly.

(3) If the consumer credit transaction is an insurance premium loan, the notice shall conform to the requirements of subsection (2) and a notice in substantially the form specified in that subsection complies with this subsection, except for the following:

(a) in lieu of a brief identification of the credit transaction, the notice shall identify

the transaction as an insurance premium loan and each insurance policy or contract that may be cancelled;

(b) in lieu of the statement in the form of notice specified in subsection (2) that the creditor may exercise his rights under the law, the statement that each policy or contract identified in the notice may be cancelled; and

(c) the last paragraph of the form of notice specified in subsection (2) shall be omitted.

**COMMENT**

1. This section must be read in conjunction with the preceding section (Section 5.109-Default) and the following section (Section 5.111-Cure of Default). Section 5.109 delineates the legal criteria for default and recognizes that a default consisting of the failure to make a payment as required by the agreement is susceptible of being cured by the consumer without impairing a continuing contractual relationship. This section then provides for a notice which may be sent to the consumer in the case of a failure in payment. The notice may be given at any time after the payment is more than ten days late. This is the same point at which the creditor may be entitled to assess a delinquency charge under Section 2.502. The notice is calculated to give the consumer enough information to understand his predicament and to encourage him to take appropriate steps to alleviate it. However, if the default is coupled with a voluntary surrender of possession of goods that are collateral for the debt, it is considered that the consumer regards a continuing relationship at an end, and no notice is provided for.

2. With respect to an insurance premium loan, the consumer should be adequately forewarned of cancellation of his insurance by the creditor. Subsection (3) of this section provides for a particularized notice in this type of transaction.

3. The forms of notice specified in this section are not mandatory. However, Section 5.111 provides that a default consisting of a failure to make a required payment may be cured by the consumer if he makes that payment before the expiration of the minimum period prescribed after written notice of his default and that prior to this time the creditor may not proceed against goods that are collateral or accelerate the maturity of the unpaid debt. This provision prevents the practice of some unscrupulous creditors who repossess collateral when a payment is only a day or two late. It also gives the average consumer the opportunity to rehabilitate his account, bring a billing error to the attention of or present a breach of warranty claim to the creditor, or negotiate a refinancing or deferral arrangement that may be required by a change in his financial circumstances.

4. Section 5.111 imposes no limitation on the creditor's right to proceed against a consumer or goods that are collateral with respect to successive defaults on the same obligation

other than an insurance premium loan or if the consumer has voluntarily surrendered possession, and particularly deals with the somewhat different nature of an insurance premium loan transaction.

**§ 5.111. [Cure of Default]**

(1) With respect to a consumer credit transaction, except as provided in subsection (2), after a default consisting only of the consumer's failure to make a required payment, a creditor, because of that default, may neither accelerate maturity of the unpaid balance of the obligation, nor take possession of or otherwise enforce a security interest in goods that are collateral until 20 days after a notice of the consumer's right to cure (Section 5.110) is given, nor, with respect to an insurance premium loan, give notice of cancellation as provided in subsection (4) until 13 days after a notice of the consumer's right to cure (Section 5.110) is given. Until expiration of the minimum applicable period after the notice is given, the consumer may cure all defaults consisting of a failure to make the required payment by tendering the amount of all unpaid sums due at the time of the tender, without acceleration, plus any unpaid delinquency or deferral charges. Cure restores the consumer to his rights under the agreement as though the defaults had not occurred.

(2) With respect to defaults on the same obligation other than an insurance premium loan and subject to subsection (1), after a creditor has once given a notice of consumer's right to cure (Section 5.110), this section gives the consumer no right to cure and imposes no limitation on the creditor's right to proceed against the consumer or goods that are collateral. For the purpose of this section, in open-end credit, the obligation is the unpaid balance of the account and there is no right to cure and no limitation on the creditor's rights with respect to a default that occurs within 12 months after an earlier default as to which a creditor has given a notice of consumer's right to cure (Section 5.110).

(3) This section and the provisions on waiver, agreements to forego rights, and settlement of claims (Section 1.107) do not prohibit a consumer from voluntarily surrendering possession of goods which are collateral and the creditor from thereafter accelerating maturity of the obligation and enforcing the obligation and his security interest in the goods at any time after default.

(4) If a default on an insurance premium loan is not cured, the lender may give notice of cancellation of each insurance policy or contract to be cancelled. If given, the notice of cancellation shall be in writing and given to the insurer who issued the policy or contract and to the insured. The insurer, within two business days after receipt of the notice of cancellation together with a copy of the insurance premium loan agreement if not previously given to him, shall give any notice of cancellation required by the policy, contract, or law and, within ten business days after the effective date of the cancellation, pay to the lender any premium unearned on the policy or contract as of that effective date. Within ten business days after receipt of the unearned premium, the lender shall pay to the consumer indebted upon the insurance premium loan any excess of the unearned premium received over the amount owing by the consumer upon the insurance premium loan.

**COMMENT**

See Comment to Section 5.110. Note subsection (2) of this section answers the question of what constitutes the obligation in open-end credit and specifies the applicable period in open-end credit with respect to notice of the consumer's right to cure under Section 5.110.

**§ 5.112. [Creditor's Right to Take Possession After Default]**

Upon default by a consumer with respect to a consumer credit transaction, unless the consumer voluntarily surrenders possession of the collateral to the creditor, the creditor may take possession of the collateral without judicial process only if possession can be taken without entry into a dwelling and without the use of force or other breach of the peace.

## COMMENT

1. Under Section 9-503 of the UCC a secured creditor has the right to take possession of collateral without resorting to legal process if he can do so without a breach of the peace. This raises delicate problems when it comes to repossessing furniture or other property that is within a home or apartment. The disputes that result from such a situation are rarely the type that get to the appellate courts for resolution. It is necessary, therefore, to make it clear that dwellings cannot be entered absent the consent of the occupants except under the supervision of the court. This section is subject to the limitations imposed by preceding sections (Sections 5.109, 5.110 and 5.111).

2. There are currently several disputed issues pertaining to the proper procedures to be utilized by a creditor in proceeding against collateral. Whether a creditor, absent consent of the consumer, is entitled to use self-help at all is under question. And, when possession is sought by legal process, the issues remain as to whether a hearing is to be held prior to the issuance of process in only some cases, what type of hearing is required to meet constitutional requirements, and whether the right to a hearing can be waived. See Comment 1 to Section 5.103. These issues seem best resolved in the courts and therefore no attempt to resolve them in this Act is made.

### § 5.113. [Venue]

An action by a creditor against a consumer arising from a consumer credit transaction shall be brought in the [county] of the consumer's residence (subsection (6) of Section 1.201), unless an action is brought to enforce an interest in land securing the consumer's obligation, in which case the action may be brought in the [county] in which the land or a part thereof is located. If the [county] of the consumer's residence has changed the consumer upon motion may have the action removed to the [county] of his current residence. If the residence of the consumer is not within this State, the action may be brought in the [county] in which the sale, lease, or loan was made. If the initial papers offered for filing in the action on their face show noncompliance with this section, the [clerk] shall not accept them.

## COMMENT

One of the common abuses in consumer credit is the bringing of an action against the consumer in a county or district other than that of his residence. Although courts universally

condemn this practice, general venue provisions that allow an action to be brought where either the plaintiff or the defendant resides facilitate it. This section requires an action by a creditor arising from a consumer credit transaction to be brought where the consumer resides except in a case involving an interest in land. This is a venue provision only and does not disturb existing requirements for service of legal process.

**§ 5.114. [Complaint; Proof]**

(1) In an action brought by a creditor against a consumer arising from a consumer credit transaction, the complaint shall allege the facts of the consumer's default, the amount to which the creditor is entitled, and an indication of how that amount was determined.

(2) A default judgment may not be entered in the action in favor of the creditor unless the complaint is verified by the creditor or sworn testimony, by affidavit or otherwise, is adduced showing that the creditor is entitled to the relief demanded.

**COMMENT**

Studies that have been performed of consumers who have legal action brought against them show a high rate of judgments taken by default, in excess of 90 per cent in some urban areas. Modern rules of procedure that require a complaint to contain only the barest of facts contemplate contested litigation. In the event judgment is taken by default there is not enough information in the pleadings to enable the court to enter an accurate award. This section provides that the minimum amount of information necessary to compute the award shall be brought to the attention of the court.

**§ 5.115. [Stay of Enforcement of or Relief from Default Judgment]**

At any time after entry of a default judgment in favor of a creditor and against a consumer in an action arising from a consumer credit transaction, the court which rendered the judgment, for cause including lack of jurisdiction to render the judgment, and upon motion of a party or its own motion, with notice as the court may direct, may stay enforcement of or relieve the consumer from the judgment by order upon just and equitable conditions.

**COMMENT**

The high rate of judgments by default arising out of consumer credit transactions suggests

a need for broad judicial discretion to open or void such judgments and re-examine the claims upon which they were rendered in appropriate cases where cause exists. Particularly, the systematic practice by some process servers (usually private process servers) of filing an affidavit of service on the consumer when, in fact, the summons has never been served but stuffed in a "sewer" or elsewhere, cannot furnish the basis for a judgment. However, such discretion is generally associated with courts of general jurisdiction and most actions arising from consumer credit transactions fall within the purview of limited jurisdiction courts. This section is intended to confer that discretion upon any court with jurisdiction to entertain actions arising from consumer credit transactions.

**§ 5.116. [Limitation on Enforcement of Security for Supervised Loan]**

(1) Except as to a purchase money security interest, this section applies to a security interest in an item of goods other than a motor vehicle which (a) is possessed by a consumer, (b) is being used by him or a member of a family wholly or partly supported by him, (c) is or may be claimed to be exempt from execution on a money judgment under the laws of this State, and (d) is collateral for a supervised loan.

(2) Unless the consumer, after written notice to him of his rights under this section, voluntarily surrenders to the lender possession of any item of goods to which this section applies, the lender, without an order or process of the [ ] court, may not take possession of the items or otherwise enforce the security interest according to its terms. The notice to the consumer shall conform to any rule adopted by the Administrator.

(3) The court may order or authorize process respecting an item of goods to which this section applies only after a hearing upon notice to the consumer of the hearing and his rights at it. The notice shall be as directed by the court. The order or authorization may prescribe appropriate conditions as to payments upon the debt secured or otherwise. The court may not order or authorize process respecting the item if it finds upon the hearing both that the consumer lacks the means to pay all or part of the debt secured and that continued possession and use of the item is necessary to avoid undue hardship for the consumer or a member of a family wholly or partly

supported by him.

(4) The court, upon application of the lender or the consumer and notice to the other, and after a hearing and a finding of changed circumstances, may vacate or modify an order or authorization pursuant to this section.

**COMMENT**

1. This section responds to the recommendation of the National Commission on Consumer Finance that security interests in household goods should not be allowed in any loan or consolidation transaction if the goods were not acquired by the use of that credit because in the event of default the right to repossess or threat to repossess these goods have far too disruptive an impact on the family life of the debtor to be in the public interest. However, since the section more appropriately directs itself to a limitation on the right to enforce a security interest rather than to the right to contract for one, the purview of it extends beyond household goods to goods that this State has determined are entitled to exemption in accordance with the policy that a debtor should not be deprived of the necessities of life by his creditors if he is unable to pay his debts.

2. For the safeguards contemplated by this section to function, the consumer must be aware of his rights. Subsection (2) requires a notice to him and authorizes the Administrator to determine by rule what sort of notice should be given of those rights, when it should be given, and how the consumer should be able to waive his rights or claim the exemption. Subsection (3) provides for additional notice of rights to the consumer in the notice of the hearing and vests in the court the necessary discretion to fashion its order in conformity with the particular circumstances brought out at the hearing.

PART 2

## CONSUMERS' REMEDIES

### § 5.201. [Effect of Violations on Rights of Parties]

(1) If a creditor has violated any provision of this Act applying to collection of an excess charge or amount or enforcement of rights (subsections (2) and (4) of Section 1.201), authority to make supervised loans (Section 2.301), restrictions on interests in land as security (Section 2.307), limitations on the schedule of payments on loan terms for supervised loans (Section 2.308), attorney's fees (Section 2.507), charges for other credit transactions (Section 2.601),

disclosure with respect to consumer leases (Section 3.202), notice to consumers (Section 3.203), receipts, statements of account, and evidences of payment (Section 3.206), form of insurance premium loan agreement (Section 3.207), notice to co-signers and similar parties (Section 3.208), security in sales and leases (Section 3.301), no assignments of earnings (Section 3.305), authorizations to confess judgment (Section 3.306), certain negotiable instruments prohibited (Section 3.307), referral sales and leases (Section 3.309), limitations on default charges (Section 3.402), card issuer subject to claims and defenses (subsection (5) of Section 3.403), assignees subject to claims and defenses (subsection (4) of Section 3.404), lenders subject to claims and defenses arising from sales and leases (subsection (4) of Section 3.405), limitation on enforcement of security for supervised loan (Section 5.116), or assurance of discontinuance (Section 6.109), the consumer has a [claim for relief] [cause of action] to recover actual damages and also a right in an action other than a class action, to recover from the person violating this Act a penalty in an amount determined by the court not less than $100 nor more than $1,000. With respect to violations arising from sales or loans made pursuant to open-end credit, no action pursuant to this subsection may be brought more than two years after the violations occurred. With respect to violations arising from other consumer credit transactions, no action pursuant to this subsection may be brought more than one year after the scheduled or accelerated maturity of the debt.

(2) A consumer is not obligated to pay a charge in excess of that allowed by this Act and has a right of refund of any excess charge paid. A refund may not be made by reducing the consumer's obligation by the amount of the excess charge, unless the creditor has notified the consumer that the consumer may request a refund and the consumer has not so requested within 30 days thereafter. If the consumer has paid an amount in excess of the lawful obligation under

the agreement, the consumer may recover the excess amount from the person who made the excess charge or from an assignee of that person's rights who undertakes direct collection of payments from or enforcement of rights against consumers arising from the debt.

(3) If a creditor has contracted for or received a charge in excess of that allowed by this Act, or if a consumer is entitled to a refund and a person liable to the consumer refuses to make a refund within a reasonable time after demand, the consumer may recover from the creditor or the person liable in an action other than a class action a penalty in an amount determined by the court not less than $100 nor more than $1,000. With respect to excess charges arising from sales or loans made pursuant to open-end credit, no action pursuant to this subsection may be brought more than two years after the violation or passage of a reasonable time for refund occurs. With respect to excess charges arising from other consumer credit transactions no action pursuant to this subsection may be brought more than one year after the scheduled or accelerated maturity of the debt. For purposes of this subsection, a reasonable time is presumed to be 30 days.

(4) Except as otherwise provided, a violation of this Act does not impair rights on a debt.

(5) If an employer discharges an employee in violation of the provisions prohibiting discharge (Section 5.106), the employee within [ ] days may bring a civil action for recovery of wages lost as a result of the violation and for an order requiring reinstatement of the employee. Damages recoverable shall not exceed lost wages for six weeks.

(6) A creditor is not liable for a penalty under subsection (1) or (3) if he notifies the consumer of a violation before the creditor receives from the consumer written notice of the violation or the consumer has brought an action under this section, and the creditor corrects the violation within 45 days after notifying the consumer. If the violation consists of a prohibited agreement, giving the consumer a corrected copy of the writing containing the violation is

sufficient notification and correction. If the violation consists of an excess charge, correction shall be made by an adjustment or refund. The Administrator and any official or agency of this State having supervisory authority over a supervised financial organization shall give prompt notice to a creditor of any violation discovered pursuant to an examination or investigation of the transactions, business, records, and acts of the creditor (Sections 2.305, 6.105 and 6.106).

(7) A creditor may not be held liable in an action brought under this section for a violation of this Act if the creditor shows by a preponderance of evidence that the violation was not intentional and resulted from a bona fide error notwithstanding the maintenance of procedures reasonably adapted to avoid the error.

(8) In an action in which it is found that a creditor has violated this Act, the court shall award to the consumer the costs of the action and to his attorneys their reasonable fees. In determining attorney's fees, the amount of the recovery on behalf of the consumer is not controlling.

**COMMENT**

1. Rights that are accompanied by inadequate remedies or no remedy at all and limitations on agreements and practices that do not provide for sufficient penalties or for any penalty at all are generally ineffective to accomplish the desired result. They become little more than exhortatory, easily ignored, and meaningless proclamations. In order to protect rights created and to deter provisions of agreements and practices proscribed by legislation, suitable remedies and penalties must exist. Since an aggrieved party is one of the persons best able to enforce violations of rights and limitations, this section sets forth a right of action in the consumer in the event of violation by the creditor of each section of this Act that does not include its own provision for infraction and better to deter such practices, even of some that do, as in the case of referral sales and leases (Section 3.309).

2. Subsection (1) lists 22 provisions of this Act for the contravention of which actual damages and a penalty could be recovered. The formula used for the penalty is derived from the CCPA (15 U.S.C. § 1601 et seq.) with a minimum and a maximum recovery. Within this range a court may apportion penalties according to the seriousness of the offense and the overall circumstances of each violation. The penalty is designed not only to provide a deterrent to potential violators but also an incentive to a consumer to bring an action when a violation has occurred. Consequently, penalties may not be recovered in a class action, although actual

damages may be if the enacting State's rules of civil procedure permits.

3. Subsections (2) and (3) set forth the rights of the consumer with respect to excess charges by the creditor. A refund rather than a credit of an excess charge must be made if requested by the consumer to prevent the creditor from holding a refund due until the contract is sufficiently paid down to have it credited as a prepayment in full. Subsection (3) imposes the same penalty on those who make excess charges or refuse to make refunds to which a consumer is entitled as that for violators of provisions listed in subsection (1). This provision is necessary because if the only rights the consumer had were those provided in subsection (2), it would be worth the creditor's gamble to make excess charges. The only thing that could be lost would be the illegal charge itself, and even that would be unlikely in view of the small percentage of consumers who would seek recovery.

4. Subsection (5) describes the rights of an employee who has been discharged in violation of Section 5.106.

5. Violations may occur for a variety of reasons, not all of them necessarily pernicious. Subsection (6) provides that if the creditor becomes aware of a violation, voluntarily notifies the consumer of the violation, and corrects the violation within 45 days after notification, he is not subject to a penalty. Such a provision encourages the autonomous correction of errors and violations. Voluntariness is considered to cease, however, either upon the commencement of an action against the creditor or upon his receipt of written notification from the consumer of the violation. Consistent with the idea that many errors and violations will be rectified upon knowledge without resort to sanctions, subsection (6) also provides that violations discovered pursuant to administrative examination or investigation shall promptly be brought to the attention of the creditor. Probably the most common type of creditor violation results from clerical mistake. No policy would be served in imposing liability for violations due to unintentional bona fide errors which occur notwithstanding the maintenance of procedures reasonably adapted to avoid them, and subsection (7) provides a creditor with an affirmative defense in such cases. Moreover, acts done or omitted in conformity with a rule, interpretation or declaratory ruling of the Administrator ought to result in no liability under this Act, except for refund of an excess charge. This Act so provides, as well as affording ample opportunity for creditor and consumer participation in the formulation and correction of rules. See Sections 6.104(4) and 6.107.

6. Subsection (8) directs the court to award to the consumer the costs of the action and to his attorney his reasonable fees in any action where it is found that a creditor has violated this Act. The direction to award attorney's fees should enable consumers to find attorneys to prosecute their cases, an essential element if the consumers' rights provided by this section are to be enforced, as an attorney is assured of adequate compensation. This is so whether or not the case goes to trial since any settlement offer will have to take the attorney's compensation into account.

7. This Act provides for other remedies in addition to those set forth in this section. For example, the consumer has a defense to the enforcement of a transaction which violates Section 5.107 on extortionate extensions of credit. Section 5.108 gives a consumer or debtor a remedy in certain cases of unconscionability. [Optional Section 5.203, if enacted, sets forth the rights of a

person with respect to transactions in which the creditor has violated the provisions on compliance with the Federal Truth in Lending Act. Section 3.201.] The consumer also has a right to cancel a home solicitation sale. Part 5 of Article 3 (Sections 3.501 et seq.).

In addition to the foregoing individual consumers' remedies the Act provides for actions by the Administrator for the benefit of consumers. The Administrator may issue cease and desist orders with respect to violations of the Act or may bring civil actions to restrain violations of the Act. Sections 6.108 and 6.110. The Administrator may also bring a civil action against a creditor to recover actual damages sustained and excess charges paid by one or more consumers who have a right to recover explicitly granted by this Act, but not for penalties, and amounts recovered shall be paid to each consumer or set off against his obligation. Section 6.113. Section 6.111 provides for civil actions by the Administrator for injunctions against a course of making unconscionable agreements or of fraudulent or unconscionable conduct.

Finally, in addition to the individual consumers' remedies and remedies of the Administrator described above, the consumer may have other remedies based on general principles of law or equity, or based on the provisions of other applicable law. See Sections 1.103 and 6.115. Also, damages or penalties to which a consumer is entitled may be set off against the consumer's obligation, and may be raised as a defense to an action on the obligation without regard to the time limitations prescribed by this section. See Section 5.202.

**§ 5.202. [Damages or Penalties as Set-Off to Obligation]**

Damages or penalties to which a consumer is entitled pursuant to this Part may be set off against the consumer's obligation, and may be raised as a defense to an action on the obligation without regard to the time limitations prescribed by this Part.

**[§ 5.203. [Civil Liability for Violation of Disclosure Provisions]**

(1) Except as otherwise provided in this section, a creditor who, in violation of the provisions of the Federal Truth in Lending Act other than its provisions concerning advertising of credit terms, fails to disclose information to a person entitled to it under this Act is liable to that person in an amount equal to the sum of:

(a) twice the amount of the finance charge in connection with the transaction, but the liability under this paragraph shall be not less than $100 or exceed $1,000; and

(b) in the case of a successful action to enforce the liability under paragraph (a),

the costs of the action together with reasonable attorney's fees as determined by the court.

(2) A creditor has no liability under this section, if within 15 days after discovering an error, and before the institution of an action under this section or the receipt of written notice of the error, the creditor notifies the person concerned of the error and makes adjustments in the appropriate account as necessary to assure that the person will not be required to pay a finance charge in excess of the amount or percentage rate actually disclosed. The Administrator and any official or agency of this State having supervisory authority over a supervised financial organization shall give prompt notice to a creditor of any error discovered pursuant to an examination or investigation of the transactions, business, records, and acts of the creditor (Sections 2.305, 6.105 and 6.106).

(3) A creditor may not be held liable in any action brought under this section for a violation of this Act if the creditor shows by a preponderance of evidence that the violation was not intentional and resulted from a bona fide error notwithstanding the maintenance of procedures reasonably adapted to avoid the error.

(4) Any action which may be brought under this section against the original creditor in a credit transaction involving a security interest in land may be maintained against any subsequent assignee of the original creditor, if the assignee, its subsidiaries, or affiliates were in a continuing business relationship with the original creditor at the time the credit was extended or at the time of the assignment, unless the assignment was involuntary, or the assignee shows by a preponderance of evidence that it did not have reasonable grounds to believe that the original creditor was engaged in violations of this Act and that it maintained procedures reasonably adapted to apprise it of the existence of the violations.

(5) An obligor or consumer has all rights under this Act that he has under the Federal

Truth in Lending Act concerning a right of rescission as to certain transactions. A creditor or other person has all liabilities and defenses under this section that he has under the Federal Truth in Lending Act.

(6) In this section, creditor includes a person who in the ordinary course of business regularly extends or arranges for the extension of credit, or offers to arrange for the extension of credit, and the seller of an interest in land and the lender who makes a loan secured by an interest in land if, but for the rate of the finance charge made in the transaction, the sale or loan would be a consumer credit sale or consumer loan.

(7) An action may not be brought under this section more than one year after the date of the occurrence of the violation.

(8) The liability of a creditor under this section is in lieu of and not in addition to his liability under the Federal Truth in Lending Act. An action by a person with respect to a violation may not be maintained pursuant to this section if a final judgment has been rendered for or against that person with respect to the same violation pursuant to the Federal Truth in Lending Act. If a final judgment has been rendered in favor of a person pursuant to this section and thereafter a final judgment with respect to the same violation is rendered in favor of the same person pursuant to the Federal Truth in Lending Act, a creditor liable under both judgments has a [claim for relief] [cause of action] against that person for appropriate relief to the extent necessary to avoid double liability with respect to the same violation.

(9) The Administrator shall adopt rules to keep this section in harmony with the Federal Truth in Lending Act. These rules supersede any provisions of this section which are inconsistent with the Federal Truth in Lending Act.]

**COMMENT**

1. This section is derived from the CCPA (15 U.S.C. § 1601 et seq., specifically, § 1640). It is intended to allow fulfillment of the demand of that statute that under state law classes of credit transactions be subject to requirements substantially similar to those imposed by the CCPA and that adequate provision for enforcement exist if the state enacting this Act wishes to apply for an exemption from the CCPA.

2. Subsections (1) through (4), consequently, are modeled exactly on the Federal provisions, except for the additional requirement of administrative notification to creditors of errors discovered through examinations or investigations, and subsection (9) directs the Administrator by rule to conform this section to any modifications from time to time of the Federal statute. If the Federal provisions on which this section is modeled are amended before enactment of this Act, this section should be conformed.

3. Subsection (5) is similar to subsection (9) in that it seeks to allow conformity of rights and liabilities under this section with those under the Federal Act, including the provision on a right of rescission as to certain transactions, as they may be formulated by case law interpretation.

4. Subsection (6) broadens the definition of "creditor" for purposes of this section beyond that applicable elsewhere in this Act (subsection (18) of Section 1.301) to again assure conformity.

5. Finally, subsection (8) mitigates against double creditor liability if a creditor is sued both under this section and under the CCPA.

6. If the enacting State wishes to apply for an exemption from the Federal Truth in Lending Act, the brackets before and after Sections 5.203 and 5.302 should be deleted and those sections enacted, the brackets before and after those sections in the Table of Articles, Parts, and Sections should be deleted, and the brackets in subsection (5) of Section 1.202 preceding and following the references to Sections 5.203 and 5.302 deleted.

Otherwise,

a. Omit Sections 5.203 and 5.302 and the references to them in the Table of Articles, Parts, and Sections, and

b. In subsection (5) of Section 1.202, delete the brackets and the language enclosed within them.

## PART 3

## CRIMINAL PENALTIES

### § 5.301. [Willful and Knowing Violations]

(1) A supervised lender who willfully and knowingly makes charges in excess of those permitted by the Article on Finance Charges and Related Provisions (Article 2) applying to supervised loans (Part 4) is guilty of a misdemeanor and upon conviction may be [sentenced to pay a fine not exceeding $[ ], or to imprisonment not exceeding one year, or both].

(2) A person who, in violation of the provisions of this Act applying to authority to make supervised loans (Section 2.301), willfully and knowingly engages without a license in the business of making supervised loans, or of taking assignments of and undertaking direct collection of payments from and enforcement of rights against consumers arising from supervised loans, is guilty of a misdemeanor and upon conviction may be [sentenced to pay a fine not exceeding $[ ], or to imprisonment not exceeding one year, or both].

(3) A person who willfully and knowingly engages in the business of entering into consumer credit transactions, or of taking assignments of rights against consumers arising therefrom and undertaking direct collection of payments or enforcement of these rights, without complying with the provisions of this Act concerning notification (Section 6.202) or payment of fees (Section 6.203), is guilty of a misdemeanor and upon conviction may be [sentenced to pay a fine not exceeding $100].

**[§ 5.302. [Disclosure Violations]**

(1) A person is guilty of a [misdemeanor] and upon conviction may be sentenced to pay a fine not exceeding $5,000, or to imprisonment not exceeding one year, or both, if he willfully and knowingly:

(a) gives false or inaccurate information or fails to provide information which he is required to disclose under the Federal Truth in Lending Act;

(b) uses any rate table or chart, the use of which is authorized by the provisions of

the Federal Truth in Lending Act, in a manner which consistently understates the annual percentage rate determined according to those provisions; or

(c) otherwise fails to comply with any requirement of the provisions on disclosure of the Federal Truth in Lending Act.

(2) The criminal liability of a person under this section is in lieu of and not in addition to his criminal liability under the Federal Truth in Lending Act; no prosecution of a person with respect to the same violation may be maintained pursuant to both this section and the Federal Truth in Lending Act.]

**COMMENT**

This section is derived from the CCPA (15 U.S.C. § 1601 et seq., specifically, § 1611). See Comment to Section 5.203.

ARTICLE 6

**ADMINISTRATION**

Part 1

**POWERS AND FUNCTIONS OF ADMINISTRATOR**

Section

Part 2

## NOTIFICATION AND FEES



Part 3

## COUNCIL OF ADVISORS ON CONSUMER CREDIT



[Part 4]

## [ADMINISTRATIVE PROCEDURE AND JUDICIAL REVIEW]

[6.415. Appeals.]

PART 1

## POWERS AND FUNCTIONS OF ADMINISTRATOR

### § 6.101. [Short Title]

This Article shall be known and may be cited as Uniform Consumer Credit Code-Administration.

### § 6.102. [Applicability and Scope]

This Part applies to persons who in this State:

(a) enter into, solicit, or participate in consumer credit transactions; or lead a debtor to believe that a transaction will give rise to a consumer credit transaction;

(b) directly collect payments from or enforce rights against consumers arising from consumer credit transactions, wherever they are entered into; or

(c) enter into a sale of an interest in land or a loan secured by an interest in land if, but for the rate of the finance charge, the sale or loan would be a consumer credit sale or consumer loan, but only for the purpose of authorizing the Administrator to enforce the provisions on compliance with the Federal Truth in Lending Act (Section 3.201).

#### COMMENT

Except for this Part and Part 2 of this Article, Section 1.201 states the territorial application of this Act. This Part has a broader territorial application than some other provisions, but this section is not intended to extend the territorial application of other provisions beyond the limits specified in Section 1.201. The scope of this Part is also broader than that of some other provisions. Compare, *e.g.*, subsection (3) of this section and Section 1.301(12)(b)(ii) and (15)(b)(ii).

### § 6.103. [Administrator]

"Administrator" means [ ].

**COMMENT**

In order to obtain the administration essential to the effectiveness of this Act, the National Conference recommends centralizing all powers of administration in a single official or agency. In recognition of the fact that in some States a single official or agency either is not constitutionally possible or may not be politically feasible, the Act does not attempt to identify the Administrator. The Administrator may be a single State official or department, two or more State officials or departments, or a Commission. For example in a State in which a single official (*e.g.*, Superintendent or Commissioner of Banks, Banking or Financial Institutions) or a single department (*e.g.*, Banking Department, Commerce Department or Department of Financial Institutions) presently supervises both banks and other financial institutions such as consumer finance companies and sales finance companies, it may be desirable to designate that official or department as the single Administrator. If two or more State officials or departments are to share the powers of the Administrator, the National Conference recommends that a Commission including those officials or departments be designated as Administrator, and that, unless a statutory division of areas of power and authority is provided for, the Commission be given power to prescribe the areas in which the officials or departments who are members of the Commission shall exercise the power and authority of the Administrator.

**§ 6.104. [Powers of Administrator; Reliance on Rules; Duty to Report**

(1) In addition to other powers granted by this Act, the Administrator within the limitations provided by law may:

(a) receive and act on complaints, take action designed to obtain voluntary compliance with this Act, or commence proceedings on his own initiative;

(b) counsel persons and groups on their rights and duties under this Act;

(c) establish programs for the education of consumers with respect to credit practices and problems;

(d) make studies appropriate to effectuate the purposes and policies of this Act and make the results available to the public; [and]

(e) adopt, amend, and repeal rules to carry out the specific provisions of this Act, but not with respect to unconscionable agreements or fraudulent or unconscionable conduct [;

(f) maintain offices within this State; and]

[ (g) appoint any necessary attorneys, hearing examiners, clerks, and other employees and agents and fix their compensation, and authorize attorneys appointed under this section to appear for and represent the Administrator in court].

(2) In addition to other powers granted by this Act, the Administrator shall enforce the Federal Truth in Lending Act, except to the extent otherwise provided by law.

(3) To keep the Administrator's rules in harmony with the rules of administrators in other jurisdictions that enact substantially the Uniform Consumer Credit Code, the Administrator, so far as is consistent with the purposes, policies, and provisions of this Act, shall:

(a) before adopting, amending, and repealing rules, advise and consult with administrators in other jurisdictions that enact substantially the Uniform Consumer Credit Code; and

(b) in adopting, amending, and repealing rules, take into consideration the rules of administrators in other jurisdictions that enact substantially the Uniform Consumer Credit Code.

(4) Except for refund of an excess charge, no liability is imposed under this Act for an act done or omitted in conformity with a rule, interpretation, or declaratory ruling of the Administrator, notwithstanding that after the act or omission the rule, interpretation, or ruling is amended or repealed or is determined by judicial or other authority to be invalid for any reason.

(5) The Administrator shall report [annually on or before January 1] to the [Governor and Legislature] on the operation of his office, the use of consumer credit in this State, and the problems of persons of small means obtaining credit from persons regularly engaged in extending sales or loan credit. For the purpose of making the report, the Administrator may conduct research and make appropriate studies. The report shall include a description of the examination

and investigation procedures and policies of his office, a statement of policies followed in deciding whether to investigate or examine the offices of credit suppliers subject to this Act, a statement of the number and percentages of offices which are periodically investigated or examined, a statement of the types of consumer credit problems of both creditors and consumers which have come to his attention through his examinations and investigations and the disposition of them under existing law, a statement of the extent to which rules of the Administrator pursuant to this Act are not in harmony with the rules of administrators in other jurisdictions that enact substantially the Uniform Consumer Credit Code and the reasons for these variations, and a general statement of the activities of his office and of others to promote the purposes of this Act. The report may not identify the creditors against whom action is taken by the Administrator.

**COMMENT**

1. The Administrator is given broad power to make studies relative to the proper working of this Act, to provide educational services for consumers, and to advise persons and groups as to their rights and obligations under this Act. The various disclosure rules, rate limitations, and other provisions of the Act designed to protect the consumer cannot be fully effective unless consumers are aware of and understand their rights under the Act. Therefore, an essential part of the Administrator's total responsibility is providing consumer education.

The Administrator also is given the power to receive and act on complaints. Consumer complaints can be expected to be an important basis for the invocation of the Administrator's investigatory powers (Section 6.106). The ability to file a complaint in addition may be a significant adjunct to the consumer's private right of action for violations (Section 5.201) or for unconscionability (Section 5.108) and, in appropriate cases, even an alternative to it. Appropriate cases might involve situations where, in the context of a single case, a violation will be difficult to establish, where the complaint involves an untested provision of the Act, or where the amount at stake individually is not sufficient under the circumstances to prompt private action to cure a violation. Since the Administrator is not under a duty to act in any particular instance, he may act only in those cases where he believes it desirable to do so pursuant to policy considerations established by him. In acting, the Administrator may seek voluntary compliance or invoke the remedies provided in this Part.

This Act in numerous places specifically directs the Administrator to adopt rules as a more reasonable approach than providing long and complex statutory provisions that are likely to prove too inflexible in practice. However, little foresight is required to recognize that the need will arise for rules to carry out many other specific provisions of the Act. For example, this Act

contains a provision restricting a separate charge for property insurance where the value of the property is less than $300 (subsection (3) of Section 4.301). To make this provision workable, the Administrator should adopt a rule specifying reasonable means for establishing an appropriate standard of value consistent with operational needs of creditors and the policy of the provision. Almost any provision also may need to be the subject of an interpretive rule, and procedural rules will be required in many instances to satisfy the requirements of administrative procedure statutes. Subsection (1)(e) grants the Administrator authority to adopt, amend, and repeal rules in these circumstances.

2. Subsection (2) requires the Administrator to enforce the Federal Truth in Lending Act, including, as defined in Section 1.302, regulations pursuant to that Act made part of this Act by Section 3.201.

3. The direction to the Administrator in subsection (3) to keep his rules in harmony with the rules of administrators in other jurisdictions that enact substantially the Uniform Consumer Credit Code is derived from the Uniform Narcotic Drug Act Section 1(14) (Alt.).

4. Under subsection (4), a person who acts in accordance with rules, interpretations, or declaratory rulings of the Administrator incurs no liability with respect to such conduct even if the rules, interpretations, or declaratory rulings are later amended, repealed or declared to be invalid, except that if a rule, interpretation, or ruling relating to charges is declared invalid, any excess charge made under the supposed authority of the invalid rule, interpretation or ruling may be covered by the consumers affected or by the Administrator for the consumers.

**§ 6.105. [Administrative Powers with Respect to Supervised Financial Organizations]**

(1) With respect to supervised financial organizations, the powers of examination and investigation (Sections 2.305 and 6.106) and administrative enforcement (Section 6.108) shall be exercised by the official or agency to whose supervision the organization is subject. All other powers of the Administrator under this Act may be exercised by him with respect to a supervised financial organization.

(2) If the Administrator receives a complaint or other information concerning noncompliance with this Act by a supervised financial organization, he shall inform the official or agency having supervisory authority over the organization concerned. The Administrator may request information about supervised financial organizations from the officials or agencies supervising them.

(3) The Administrator and any official or agency of this State having supervisory authority over a supervised financial organization shall consult and assist one another in maintaining compliance with this Act. They may jointly pursue investigations, prosecute actions, and take other official action, as they deem appropriate, if either of them otherwise is empowered to take the action.

**COMMENT**

1. "Supervised financial organizations" are by definition subject to supervision by an official or agency of this State or the United States. Section 1.301(41). The powers of administration and investigation and administrative enforcement under this Act are delegated to that official or agency rather than to the Administrator, unless he is also the supervising official or agency. All other powers of the Administrator, including rule making and initiation of judicial action, may be exercised by him with respect to supervised financial organizations.

2. Subsections (2) and (3) provide for exchange of information and for cooperation between the Administrator under this Act and the supervisory authorities of supervised financial institutions. Subsection (3) goes further and requires the Administrator and the State agency having supervision over supervised financial organizations to consult with and assist each other in carrying out their duties under this Act.

**§ 6.106. [Investigatory Powers]**

(1) If the Administrator has cause to believe that a person has engaged in conduct or committed an act that is subject to action by the Administrator, he may make an investigation to determine whether the person has engaged in the conduct or committed the act. To the extent necessary for this purpose, he may administer oaths or affirmations, and, upon his own motion or upon request of any party, subpoena witnesses, compel their attendance, adduce evidence, and require the production of, or testimony as to, any matter relevant to the investigation, including the existence, description, nature, custody, condition, and location of any books, documents, or other tangible things and the identity and location of persons having knowledge of relevant facts, or any other matter reasonably calculated to lead to the discovery of admissible evidence.

(2) If the person's records are located outside this State, the person at his option shall

make them available to the Administrator at a convenient location within this State or pay the reasonable and necessary expenses for the Administrator or his representative to examine them where they are located. The Administrator may designate representatives, including comparable officials of the State in which the records are located, to inspect them on his behalf.

(3) Upon application by the Administrator showing failure without lawful excuse to obey a subpoena or to give testimony, and upon reasonable notice to all persons affected thereby, the [ ] court shall grant an order compelling compliance.

(4) The Administrator may not make public the name or identity of a person whose acts or conduct he investigates under this section or the facts disclosed in the investigation, but this subsection does not apply to disclosures in actions or enforcement proceedings pursuant to this Act.

**COMMENT**

1. Administrator under this section includes the official or agency referred to in Section 6.105(1).

2. The Administrator may commence an investigation under this section if he has cause to believe that a violation of law or regulations or other act or conduct has occurred which would subject the person committing or engaging in it to action by the Administrator. The Administrator, therefore, may commence an investigation when he has met the usual administrative standards; political, judicial and other governmental processes provide ample protection against arbitrary use of the power. Action by the Administrator includes both administrative enforcement and enforcement by civil action.

**§ 6.107. [Application of [Administrative Procedure Act] [Part on Administrative Procedure and Judicial Review]]**

Except as otherwise provided, the [State Administrative Procedure Act] [Part on Administrative Procedure and Judicial Review (Part 4) of this Article] applies to and governs all administrative action taken by the Administrator pursuant to this Article.

## COMMENT

If the enacting State has an adequate State administrative procedure act reference should be made to it in this section. Otherwise Part 4 of Article 6 [Section 6.401 et seq.] should be enacted and referred to here. Brackets and bracketed language in this section and its caption should be retained or deleted dependent upon which course is followed. See Comment to Section 6.401.

### § 6.108. [Administrative Enforcement Orders]

(1) After notice and hearing the Administrator may order a creditor or a person acting in his behalf to cease and desist from violating this Act. A respondent aggrieved by an order of the Administrator may obtain judicial review of the order and the Administrator may obtain an order of the court for enforcement of his order in the [ ] court. The proceeding for review or enforcement is initiated by filing a petition in the court. Copies of the petition shall be served upon all parties of record.

(2) Within 30 days after service of the petition for review upon the Administrator, or within any further time the court allows, the Administrator shall transmit to the court the original or a certified copy of the entire record upon which the order is based, including any transcript of testimony, which need not be printed. By stipulation of all parties to the review proceeding, the record may be shortened. After hearing, the court may (a) reverse or modify the order if the findings of fact of the Administrator are clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record, (b) grant any temporary relief or restraining order it deems just, and (c) enter an order enforcing, modifying, and enforcing as modified, or setting aside in whole or in part the order of the Administrator, or remanding the case to the Administrator for further proceedings.

(3) An objection not urged at the hearing shall not be considered by the court unless the failure to urge the objection is excused for good cause shown. A party may move the court to

remand the case to the Administrator in the interest of justice for the purpose of adducing additional specified and material evidence and seeking findings thereon upon good cause shown for the failure to adduce this evidence before the Administrator.

(4) The jurisdiction of the court shall be exclusive and its final judgment or decree is subject to review by the [ ] court in the same manner and form and with the same effect as in appeals from a final judgment or decree in a [special proceeding]. The Administrator's copy of the testimony shall be available at reasonable times to all parties for examination without cost.

(5) A proceeding for review under this section shall be initiated within 30 days after a copy of the order of the Administrator is received. If no proceeding is so initiated, the Administrator may obtain an order of the court for enforcement of his order upon showing that his order was issued in compliance with this section, that no proceeding for review was initiated within 30 days after a copy of the order was received, and that the respondent is subject to the jurisdiction of the court.

(6) With respect to unconscionable agreements or fraudulent or unconscionable conduct by the respondent, the Administrator may not issue an order pursuant to this section but may bring a civil action for an injunction. (Section 6.111).

**COMMENT**

1. A cease and desist order issued under this section is not enforceable against the respondent until a judicial enforcement order is secured by the Administrator. However, unless the respondent files a petition for judicial review of the cease and desist order within 30 days after he receives a copy of the order, it becomes final and the Administrator may obtain enforcement of it without having to support his findings with substantial evidence. The Administrator in such a case need show only issuance of the order in compliance with this section, failure of the respondent to seek review within 30 days, and jurisdiction of the court. Any issues other than those mentioned above must be raised by the filing of a petition for review within the proper time.

2. The Administrator may not issue cease and desist orders under this section as to

conduct which violates only the unconscionability or fraudulent conduct rules set out in Section 6.111.

**§ 6.109. [Assurance of Discontinuance]**

If it is claimed that a person has engaged in conduct which could be subject to an order by the Administrator (Sections 2.303 and 6.108) or by a court (Sections 6.110, 6.111, and 6.112), the Administrator may accept an assurance in writing that the person will not engage in the same or similar conduct in the future. The assurance may include any of the following: stipulations for the voluntary payment by the creditor of the costs of investigation or of an amount to be held in escrow as restitution to debtors aggrieved by past or future conduct of the creditor or to cover costs of future investigation, or admissions of past specific acts by the creditor or that those acts violated this Act or other statutes. A violation of an assurance of discontinuance is a violation of this Act.

**COMMENT**

This section provides a method for resolving controversies without formal proceedings that involve conduct which is alleged to contravene the provisions of this Act. Considerable flexibility is granted to the Administrator in formulating the terms of any assurance entered into. If a creditor violates an assurance concluded with the Administrator, that itself constitutes a violation of this Act, for which the Administrator may invoke the remedies given him in this Part and an affected consumer may have a private right of action (Section 5.201).

**§ 6.110. [Injunctions Against Violations of Act]**

The Administrator may bring a civil action to restrain any person from violating this Act and for other appropriate relief including but not limited to the following: to prevent a person from using or employing practices prohibited by this Act, to reform contracts to conform to this Act and to rescind contracts into which a creditor has induced a consumer to enter by conduct violating this Act, even though a consumer is not a party to the action. An action under this section may be joined with an action under the provisions on civil actions by Administrator

(Section 6.113).

**COMMENT**

The Administrator has an option of proceeding either under this section or under Section 6.108. In an action under this section the Administrator, in addition to relief appropriate under other law of this State, may seek relief under Sections 6.112 and 6.113.

**§ 6.111. [Injunctions Against Unconscionable Agreements and Fraudulent or Unconscionable Conduct Including Debt Collection]**

(1) The Administrator may bring a civil action to restrain a person to whom this Part applies from engaging in a course of:

(a) making or enforcing unconscionable terms or provisions of consumer credit transactions;

(b) fraudulent or unconscionable conduct in inducing consumers to enter into consumer credit transactions;

(c) conduct of any of the types specified in paragraph (a) or (b) with respect to transactions that give rise to or that lead persons to believe will give rise to consumer credit transactions; or

(d) fraudulent or unconscionable conduct in the collection of debts arising from consumer credit transactions.

(2) In an action brought pursuant to this section the court may grant relief only if it finds:

(a) that the respondent has made unconscionable agreements or has engaged or is likely to engage in a course of fraudulent or unconscionable conduct;

(b) that the respondent's agreements have caused or are likely to cause or the conduct of the respondent has caused or is likely to cause injury to consumers or debtors; and

(c) that the respondent has been able to cause or will be able to cause the injury

primarily because the transactions involved are credit transactions.

(3) In applying subsection (1)(a), (b), and (c), consideration shall be given to each of the factors specified in the provisions on unconscionability with respect to a transaction that is, gives rise to, or that a person leads the debtor to believe will give rise to, a consumer credit transaction (subsection (4) of Section 5.108), among others.

(4) In applying subsection (1)(d), consideration shall be given to each of the factors specified on the provisions on unconscionability with respect to the collection of debts arising from consumer credit transactions (subsection (5) of Section 5.108), among others.

(5) In an action brought pursuant to this section, a charge or practice expressly permitted by this Act is not in itself unconscionable.

**COMMENT**

1. Section 5.108 provides a private remedy for unconscionable conduct. This section, in addition, permits the Administrator to bring suit to enjoin a person to whom this Part applies from engaging in a course of conduct specified in subsection (1)(a), (b), (c), or (d). These subsections cover three different areas of unconscionable conduct: (1) unconscionable contract terms, (2) fraudulent or unconscionable conduct in inducing persons to enter into transactions, and (3) fraudulent or unconscionable conduct in the collection of consumer credit debts.

2. One purpose of this section is to afford the Administrator a means of dealing with new patterns of fraudulent or unconscionable conduct unforeseen and, perhaps, unforeseeable at the writing of this Act. Another is to give him a more flexible remedy for halting reprehensible creditor practices that have been specifically and somewhat rigidly treated in previous consumer credit legislation. For instance, this Act has no specific prohibition against the creditor's allowing the consumer to sign a credit agreement containing blanks. In some situations there may be legitimate reasons for a contract to contain blanks at the time of signing. However, if the creditor deliberately leaves blanks to be filled in after the consumer's signature and without his consent, the Administrator may seek to restrain the practice as fraudulent or unconscionable conduct under this section.

3. Subsections (3) and (4) refer to a number of specific factors to be considered on the issue of unconscionability which are listed in Section 5.108. The illustrative individual transactions described in the Comment to Section 5.108, if engaged in by a person to whom this Part applies as a course of conduct, would entitle the Administrator to injunctive relief under this section.

4. Subsection (5) prohibits a finding that a charge or practice expressly permitted by this Act is in itself unconscionable. However, even though a practice or charge is authorized by this Act, the totality of a particular creditor's conduct may show that the practice or charge is part of an unconscionable course of conduct. Therefore, in determining unconscionability, the creditor's total conduct, including that part of his conduct which is in accordance with the provisions of this Act, may be considered.

5. For cases illustrating the prior application of the doctrine of unconscionability in private actions, see Comment to Section 5.108. This doctrine was applied in an action by a public official in State by Lefkowitz v. ITM, Inc., 52 Misc.2d 39, 275 N.Y.S.2d 303 (Sup.Ct.1966).

**§ 6.112. [Temporary Relief]**

With respect to an action brought to enjoin violations of the Act (Section 6.110) or unconscionable agreements or fraudulent or unconscionable conduct (Section 6.111), the Administrator may apply to the court for appropriate temporary relief against a defendant, pending final determination of the action. The court may grant appropriate temporary relief.

**COMMENT**

This section permits the Administrator to seek appropriate temporary relief in connection with actions brought pursuant to Sections 6.110 and 6.111, but leaves to other State law the determination of the circumstances in which it will be granted.

**§ 6.113. [Civil Actions by Administrator]**

(1) After demand, the Administrator may bring a civil action against a creditor to recover actual damages sustained and excess charges paid by one or more consumers who have a right to recover explicitly granted by this Act. In a civil action under this subsection, penalties may not be recovered by the Administrator. The court shall order amounts recovered under this subsection to be paid to each consumer or set off against his obligation. A consumer's action, except a class action, takes precedence over a prior or subsequent action by the Administrator with respect to the claim of that consumer. A consumer's class action takes precedence over a subsequent action by the Administrator with respect to claims common to both actions, but the

Administrator may intervene. An Administrator's action on behalf of a class of consumers takes precedence over a consumer's subsequent class action with respect to claims common to both actions. Whenever an action takes precedence over another action under this subsection, the latter action may be stayed to the extent appropriate while the precedent action is pending and dismissed if the precedent action is dismissed with prejudice or results in a final judgment granting or denying the claim asserted in the precedent action. A defense available to a creditor in a civil action brought by a consumer is available to him in a civil action brought under this subsection.

(2) The Administrator may bring a civil action against a creditor or a person acting in his behalf to recover a civil penalty of no more than $5,000 for repeatedly and intentionally violating this Act. A civil penalty pursuant to this subsection may not be imposed for a violation of this Act occurring more than two years before the action is brought or for making unconscionable agreements or engaging in a course of fraudulent or unconscionable conduct.

(3) The Administrator may bring a civil action against a creditor for failure to file notification in accordance with the provisions on notification (Section 6.202) or to pay fees in accordance with the provisions on fees (Section 6.203) to recover the fees the defendant has failed to pay and a civil penalty in an amount determined by the court not exceeding the greater of three times the amount of fees the defendant has failed to pay or $1,000.

**COMMENT**

1. This Act explicitly grants a right of action to a consumer to recover actual damages and a penalty for the violation of numerous of its provisions. See Section 5.201. In addition, subsection (1) of this section allows the Administrator, after demand, to bring a civil action on behalf of one or more individual consumers in such cases, except for the recovery of penalties, in contemplation that in some number of these cases the Administrator may be the only person with the necessary informational or monetary resources properly to prosecute an action, may be the only person who can adequately represent a group of consumers, or for other reasons may be an appropriate person to litigate the question involved. If a consumer brings an action on behalf of

himself, his action takes precedence, whether prior or subsequent to the action of the Administrator. If the consumer brings a class action (the ability to do so depends on other law of this State), it takes precedence if it is brought before an action by the Administrator with respect to claims common to both actions, but the Administrator is given the authority to intervene. If the Administrator's action on behalf of a class of consumers is brought prior to that of the consumer, the Administrator's action takes precedence with respect to claims common to both actions.

2. Whether the Administrator's action is on behalf of a single consumer or a class of consumers, it is subject to the same limitations as if brought by the consumer or consumers. For example, if a defense of the running of the statute of limitations would be available to a creditor in an action brought pursuant to Section 5.201 it is available to the creditor to the same extent in an action brought under subsection (1) by the Administrator, and under this subsection the Administrator may recover excess charges from an assignee only where the assignee has under taken direct collection or enforcement. See Section 5.201(1) and (2).

3. An action for a civil penalty under subsection (2) of this section may be in lieu of or in addition to an action under subsection (1). The civil penalty under subsection (2) may be recovered for any violation of the Act, but not for unconscionable or fraudulent conduct subject to action under Section 5.108 or under Section 6.111. The amount of the penalty to be imposed under subsection (2) is in the discretion of the court, but a penalty may be imposed only if it is found that the defendant has engaged in a course of repeated and intentional violations of the Act. Since this subsection confers a right of recovery on the Administrator in his own behalf, it prescribes its own statute of limitations. An unintentional and bona fide error defense is inapplicable since recovery can only be had for repeated and intentional violations, and if a creditor voluntarily notifies consumers of and corrects violations, his conduct should be taken into account with respect to whether an action under this subsection is appropriate or in connection with the penalty imposed.

4. Failure to file notification or to pay fees in accordance with the provisions of Sections 6.202 and 6.203 is a violation of this Act. However, the remedy of subsection (2) is inappropriate for a variety of reasons among which is it does not permit recovery of the unpaid fees as well as a penalty for the violation. Subsection (3) creates a more specific remedy for this type of violation. The amount of the penalty to be imposed is in the discretion of the court subject to a basic limitation of three times the unpaid fees. Since this amount of penalty may be of little consequence where small amounts are owed, the court may impose a penalty in excess of three times the unpaid fees up to $1,000.

**§ 6.114. [Jury Trial]**

The Administrator has no right to trial by jury in an action brought by him under this Act.

**§ 6.115. [Consumer's Remedies Not Affected]**

The grant of powers to the Administrator in this Article does not affect remedies available to consumers under this Act or under other principles of law or equity.

**COMMENT**

1. It is not the intention of the grant of powers to the Administrator or of any of the other provisions of this Act dealing with consumers' remedies to diminish in any way the availability of consumers' remedies under other principles of law or equity or to impede the development of judicially created law in this area. For example, the individual consumer has a cause of action under Section 5.201(2) and (3) to recover any charges in excess of those permitted in the Act and to recover a penalty in certain cases, and the Administrator may also bring an action under Section 6.113 to recover excess charges on behalf of consumers. Whether or not an action to recover excess charges by a class of private parties would lie depends upon the State law with respect to class actions. This Act does not specifically authorize such class actions nor does it preclude them. See also Section 5.105, Comment 7.

2. Various other consumers' remedies provided by other applicable law are not affected by this Act. Examples include the UCC provisions concerning the buyer's revocation of acceptance of goods delivered (UCC Section 2-608), the buyer's right to cancel the contract and to take a security interest in the goods delivered (UCC Section 2-711), the buyer's right to incidental and consequential damages (UCC Section 2-715), and the buyer's remedies for fraud (UCC Section 2-721). So, too, the limitations on contract provided for in the UCC in regard to penalties, liquidated damages, and limitation of remedies (UCC Sections 2-718 and 2-719) continue to apply to transactions governed by this Act.

**[§ 6.116. [Venue]**

The Administrator may bring actions or proceedings in a court in a [county] in which an act on which the action or proceeding is based occurred or in a [county] in which respondent resides or transacts business.]

**COMMENT**

This section is bracketed since it may be unnecessary in some States because of adequate venue rules in those States.

PART 2

## NOTIFICATION AND FEES

### § 6.201. [Applicability]

This Part applies to a creditor engaged in entering into consumer credit transactions in this State and to a creditor having an office or place of business in this State who takes assignments and undertakes direct collection of payments from or enforcement of rights against consumers arising from these transactions.

#### COMMENT

1. All creditors engaged in entering into consumer credit transactions in this State must file notification under Section 6.202. As to when a creditor enters into a consumer credit transaction in this State see Section 1.201 on territorial application.

2. Assignees of consumer obligations must file notification under Section 6.202 only if all of the three following elements are present: (1) the assigned obligations arose out of consumer credit transactions entered into in this State, (2) the assignee has an office or place of business in this State, and (3) the assignee undertakes direct collection of payments from the consumers or direct enforcement of obligations against consumers. An assignee having no office or place of business within this State is not required to file notification even though he is engaged in direct collection or direct enforcement of consumer accounts in this State.

3. The direct collection provision excludes from the notification requirements the assignee "in bulk" or "for security" who leaves the collection of the obligation to the assignor and so has no relationship with the consumers with whom this Act is primarily concerned. If an assignee for some reason, such as the default or bankruptcy of the assignor, takes over the direct collection or direct enforcement of obligations against consumers, he must at that time file notification.

4. Under Sections 1.301(12)(b)(i) and (14)(a)(iv) a transaction pursuant to a lender credit card is excluded from the definitions of consumer credit sale and consumer lease and is classified as a loan made by the issuer of the card. Section 1.301(25). However, a transaction pursuant to a seller credit card may be a consumer credit sale or consumer lease. Consequently, a seller or lessor engaged in such transactions must file notification under Section 6.202.

### § 6.202. [Notification]

(1) Persons subject to this Part shall file notification with the Administrator within 30 days

after commencing business in this State, and, thereafter, on or before January 31 of each year. The notification shall state:

(a) name of the person;

(b) name in which business is transacted if different from (a);

(c) address of principal office, which may be outside this State;

(d) address of all offices or retail stores, if any, in this State at which consumer credit transactions are entered into, or in case of a person taking assignments of obligations, the offices or places of business within this State at which business is transacted;

(e) if consumer credit transactions are entered into otherwise than at an office or retail store in this State, a brief description of the manner in which they are entered into;

(f) address of designated agent upon whom service of process may be made in this State; and

(g) whether supervised loans are made.

(2) If information in a notification becomes inaccurate after filing, no further notification is required until the following January 31.

**COMMENT**

1. The basic rule is that notification must be filed within 30 days after commencing in this State business which is subject to this Act. In the case of an assignee who did not take the assignment with the intention of engaging in direct collection or enforcement but who at some later time finds it necessary to do so, notification is required 30 days after undertaking direct collection or enforcement.

2. Subsection (1)(e) requires a brief description of the manner of selling, leasing, or lending under which the creditor receives the consumer's offer at a place other than at an office or retail store, e.g., door to door selling, product parties.

3. Once a person has filed notification, he need file only once a year even though he changes his business name or opens additional places of business or makes other changes during the year.

**§ 6.203. [Fees]**

(1) A person required to file notification shall pay to the [Administrator] and annual fee of $10. The fee shall be paid with the filing of the first notification and on or before January 31 of each year thereafter.

(2) Except as provided in subsection (4), a person required to file notification who is a seller, lessor, or lender shall pay at the time and in the manner stated in subsection (1) an additional fee of [$10] for each $100,000 or part thereof exceeding [$10,000], of the average unpaid balances, including unpaid scheduled periodic payments under consumer leases, of obligations arising from consumer credit transactions entered into by him in this State and held on the last day of each calendar month during the preceding calendar year and held either by the seller, lessor, or lender or by his immediate or remote assignee who has not filed notification. The unpaid balances of assigned obligations held by an assignee who has not filed notification are presumed to be the unpaid balances of the assigned obligations at the time of their assignment by the seller, lessor, or lender.

(3) Except as provided in subsection (4), a person required to file notification who is an assignee shall pay at the time and in the manner stated in subsection (1) an additional fee of [$10] for each $100,000, or part thereof exceeding [$10,000], of the average unpaid balances, including unpaid scheduled periodic payments payable by lessees, of obligations arising from consumer credit transactions entered into in this State taken by him by assignment and held by him by assignment and held by him on the last day of each calendar month during the preceding calendar year.

(4) A supervised financial organization is exempt from 50 per cent of the fees prescribed by subsections (2) and (3) to take account of its obligation to pay other fees or charges to officials

or agencies to whose supervision it is also subject.

(5) To the extent that a seller, lessor, or lender, or his immediate or remote assignee is obligated to pay and pays fees to another state or official thereof pursuant to provisions similar but not necessarily identical to subsections (2) and (3), he is entitled to an exemption from the fees prescribed by subsections (2) and (3).

(6) The [Administrator] may collect a charge not exceeding [$25] from each person required to pay fees under this section with respect to fees not paid in full within 90 days after they are due.

**COMMENT**

1. Any person required to file notification under this Part must pay an annual fee of $10. Subsection (1) provides for payment of an annual fee with the first filing of a notification, to assure income for the first year of operations under this Act, and thereafter on or before January 31 of each year.

2. In addition, except as otherwise provided in this section, such a person who is a seller, lessor, or lender must pay an additional fee of [$10] for each $100,000, or part thereof exceeding [$10,000], of the average unpaid balances, including unpaid scheduled periodic payments under consumer leases, of obligations arising from consumer credit transactions entered into by him in his State and held on the last day of each calendar month during the preceding calendar year and held by him. An assignee must pay an additional fee of [$10] for each $100,000, or part thereof exceeding [$10,000], of the average unpaid balances of obligations arising from consumer credit transactions entered into in this State taken by him by assignment and held by him by assignment and held by him on the last day of each calendar month during the preceding calendar year. The exclusion of the first [$10,000] of consumer credit receivables is designed to enable a merchant who sells most of his closed-end paper to ordinarily avoid paying additional fees and the similar exclusion with respect to assignees is to maintain consistency. Average outstandings on the last day of each month during the year has been chosen as a convenient basis for calculating additional fees since creditors normally maintain records of these figures and they are easily audited by the Administrator. The additional fee per $100,000 or part thereof of receivables should be set by the enacting State at that figure which will produce for it, under its particular circumstances, funds sufficient for the adequate administration of this Act.

3. To illustrate the operation of this section and using a $10 additional fee and a $10,000 exclusion assume that a seller had average consumer credit sale unpaid balances during the preceding year of $975,000 of which he assigned immediately after the sales involved $325,000 to a sales finance company which had filed notification. The sum on which the seller must compute the additional fee in excess of the $10 annual fee is $975,000 less $325,000, or

$650,000. Therefore, the seller's total fee will be an annual fee of $10 plus $70 of additional fee, or $80. The sales finance company's fee in addition to the $10 annual fee will be based on the average unpaid balances of the assigned accounts. Therefore, the sales finance company's total fee will be a $10 annual fee plus $40, or $50.

4. A seller, lessor or lender entering into consumer credit transactions in this State cannot escape liability for the fees imposed by subsection (2) by assigning the resulting obligations to an out-of-state assignee who has not filed notification. Subsection (2) imposes a liability for the fees on the seller, lessor or lender if his immediate or remote assignee has not filed notification, and a presumption is created on the basis of which the fees can be computed.

5. All creditors extending consumer credit in a state enacting this Act are governed by it and should share in financing the cost of its administration. However, since supervised financial organizations are subject to examination, investigation, and administrative enforcement by officials or agencies to whose supervision they are subject other than the Administrator (Section 6.105) and pay fees or charges to those officials or agencies, subsection (4) creates an exemption from 50 per cent of the additional fees otherwise payable by such creditors.

6. It is conceivable that an obligation can exist to pay additional fees under this Act on consumer credit paper and also to pay similar fees to another state on the same consumer credit paper. To the extent of the obligation to pay and payment of fees to the other state or official thereof, subsection (5) permits an exemption from the additional fees payable under this section.

## PART 3

## COUNCIL OF ADVISORS ON CONSUMER CREDIT

### § 6.301. [Council of Advisors on Consumer Credit]

(1) The Council of Advisors on Consumer Credit is created consisting of [sixteen] members appointed by the Governor. The Governor shall designate one of the Advisors as Chairman. In appointing members of the Council, the Governor shall seek to achieve a fair representation from the various segments of the consumer credit industry and the public.

(2) The term of office of each member of the Council is [four] years. Of those members first appointed, [four] shall be appointed for a term of [one] year, [four] for a term of [two] years, [four] for a term of [three] years, and [four] for a term of [four] years. A member chosen to fill a vacancy arising otherwise than by expiration of term shall be appointed for the unexpired term of

the member whom he is to succeed. A member of the Council is eligible for reappointment.

(3) Members of the Council shall serve without compensation, but are entitled to reimbursement of expenses reasonably incurred in the performance of their duties.

**§ 6.302. [Function of Council; Conflict of Interest]**

The Council shall advise and consult with the Administrator concerning the exercise of his powers under this Act and may make recommendations to him. Members of the Council may assist the Administrator in obtaining compliance with this Act. Since it is an objective of this Part to obtain competent representatives of creditors and the public to serve on the Council and to assist and cooperate with the Administrator in achieving the objectives of this Act, service on the council does not in itself constitute a conflict of interest regardless of the occupations or associations of the members.

**§ 6.303. [Meetings]**

The Council and the Administrator shall meet together at a time and place designated by the Chairman at least twice each year. The Council may hold additional meetings when called by the Chairman.

[PART 4]

**[ADMINISTRATIVE PROCEDURE AND JUDICIAL REVIEW]**

**§ 6.401. [Applicability and Scope]**

This Part applies to the Administrator, prescribes the procedures to be observed by him in exercising his powers under this Act, and supplements the provisions of the Part on Powers and

Functions of Administrator (Part 1) of this Article and of the Part on Supervised Lenders (Part 3) of the Article on Finance Charges and Related provisions (Article 2).]

**COMMENT**

This Part is patterned after the Uniform Law Commissioners' Revised Model State Administrative Procedure Act, hereinafter referred to as the Revised Model Act. It is intended for adoption only in those states which have not enacted an adequate administrative procedure act which would apply to the actions of the Administrator under this Act. States which have acts covering only a part of the matter dealt with in this Part may find it desirable to adopt portions of this Part. States which presently have administrative procedure acts which depart markedly from the Revised Model Act may find it desirable to adopt this Part or some of its sections to apply to actions of the Administrator. See Sections 2.306, 4.112, and 6.107.

**[§ 6.402. [Definitions in Part: "Contested Case"; "License"; "Licensing"; "Party"; "Rule"]**

In this Part:

(1) "Contested case" means a proceeding, including but not restricted to one pursuant to the provisions on administrative enforcement orders (subsection (1) of Section 6.108) and licensing, in which the legal rights, duties, or privileges of a party are required by law to be determined by the Administrator after an opportunity for hearing.

(2) "License" means a license authorizing a person to make supervised loans pursuant to the provisions on authority to make supervised loans (Section 2.301).

(3) "Licensing" includes the Administrator's process respecting the grant, denial, revocation, suspension, annulment, withdrawal, or amendment of a license.

(4) "Party" means the Administrator and each person named or admitted as a party, or who is aggrieved by action taken and seeks to be admitted as a party.

(5) "Rule" means each rule specifically authorized by this Act that applies generally and implements, interprets, or prescribes law or policy, or each statement by the Administrator that

applies generally and describes the Administrator's procedure or practice requirements or the organization of his office. The term includes the amendment or repeal of a prior rule but does not include:

(a) statements concerning only the internal management of the Administrator's office and not affecting private rights or procedures available to the public; [or]

(b) declaratory rulings issued pursuant to the provisions on declaratory rulings by Administrator (Section 6.409) [; or

(c) intra-office memoranda].]

**COMMENT**

These definitions are derived from Section 1 of the Revised Model Act.

**[§ 6.403. [Public Information; Adoption of Rules; Availability of Rules and Orders]**

(1) In addition to other rule-making requirements imposed by law, the Administrator shall:

(a) adopt as a rule a description of the organization of his office, stating the general course and method of the operations of his office and the methods whereby the public may obtain information or make submissions or requests;

(b) adopt rules of practice setting forth the nature and requirements of all formal and informal procedures available, including a description of all forms and instructions used by the Administrator or his office;

(c) make available for public inspection all rules and all other written statements of policy or interpretations formulated, adopted, or used by the Administrator in the discharge of his functions; and

(d) make available for public inspection all final orders, decisions, and opinions.

(2) A rule, order, or decision of the Administrator is not valid or effective against any

person or party, nor may it be invoked by the Administrator for any person, until it has been made available for public inspection as herein required. This provision does not apply in favor of any person or party who has actual knowledge thereof.]

**COMMENT**

This section is derived from Section 2 of the Revised Model Act.

**[§ 6.404. [Procedure for Adoption of Rules]**

(1) Prior to the adoption, amendment, or repeal of any rule, the Administrator shall:

(a) give at least 30 days' notice of his intended action. The notice shall include a statement of either the terms or substance of the intended action or a description of the subjects and issues involved, and the time, place, and manner in which interested persons may present their views thereon. The notice shall be mailed to all persons who have made timely request of the Administrator for advance notice of his rule-making proceedings and be published in [here insert the medium of publication appropriate for the adopting State];

(b) afford all interested persons reasonable opportunity to submit data, views, or arguments, orally or in writing. In case of substantive rules, opportunity for oral hearing shall be granted if requested by 25 persons, a governmental subdivision or agency, or an association having not fewer than 25 members. The Administrator shall consider fully all written and oral submissions respecting the proposed rule. Upon adoption of a rule the Administrator, if requested to do so by an interested person before adoption or within 30 days thereafter, shall issue a concise statement of the principal reasons for and against its adoption, incorporating therein his reasons for overruling the considerations urged against its adoption.

(2) A rule is not valid unless adopted in substantial compliance with this section. A proceeding to contest any rule on the ground of non-compliance with the procedural requirements

of this section shall be commenced within two years from the effective date of the rule.]

**COMMENT**

This section is derived from Section 3 of the Revised Model Act.

**[§ 6.405. [Filing and Taking Effect of Rules]**

(1) The Administrator shall file in the office of the [Secretary of State] a certified copy of each rule adopted by him. The [Secretary of State] shall keep a permanent register of the rules open to public inspection.

(2) Each rule hereafter adopted is effective 20 days after filing, except that a later effective date may be specified in the rule.]

**COMMENT**

This section is derived from Section 4 of the Revised Model Act.

**[§ 6.406. [Publication of Rules]**

(1) The [Secretary of State] shall compile, index, and publish all effective rules adopted by the Administrator. Compilations shall be supplemented or revised as often as necessary.

(2) Compilations shall be made available upon request to [agencies and officials of this State] free of charge and to other persons at prices fixed by the [Secretary of State] to cover mailing and publication costs.]

**COMMENT**

This section is derived from Section 5 of the Revised Model Act.

**[§ 6.407. [Petition for Adoption of Rules]**

An interested person may petition the Administrator requesting the adoption, amendment, or repeal of a rule. The Administrator shall prescribe by rule the form for petitions and the

procedure for their submission, consideration, and disposition. Within 30 days after submission of a petition, the Administrator either shall deny the petition in writing (stating his reasons for the denials) or initiate rule-making proceedings in accordance with the provisions on procedure for adoption of rules (Section 6.404).]

**COMMENT**

This section is derived from Section 6 of the Revised Model Act.

**[§ 6.408. [Declaratory Judgment on Validity or Applicability of Rules]**

The validity or applicability of a rule may be determined in an action for declaratory judgment in the [ ] court if it is alleged that the rule, or its threatened application, interferes with or impairs, or threatens to interfere with or impair, the legal rights or privileges of the plaintiff. The Administrator shall be made a party to the action. A declaratory judgment may be rendered whether or not the plaintiff has requested the Administrator to pass upon the validity or applicability of the rule in question.]

**COMMENT**

This section is derived from Section 7 of the Revised Model Act.

**[§ 6.409. [Declaratory Rulings by Administrator]**

The Administrator shall provide by rule for the filing and prompt disposition of petitions for declaratory rulings as to the applicability of any statutory provision or of any rule of the Administrator. Rulings disposing of petitions have the same status as decisions or orders in contested cases.]

**COMMENT**

This section is derived from Section 8 of the Revised Model Act.

**[§ 6.410. [Contested Cases; Notice; Hearing; Records]**

(1) In a contested case, all parties shall be afforded an opportunity for hearing after reasonable notice.

(2) The notice shall include:

(a) a statement of the time, place, and nature of the hearing:

(b) a statement of the legal authority and jurisdiction under which the hearing is to be held;

(c) a reference to the particular provisions of the statutes and rules involved; and

(d) a short and plain statement of the matters asserted. If the Administrator or other party is unable to state the matters in detail at the time the notice is served, the initial notice may be limited to a statement of the issues involved. Thereafter upon application a more definite and detailed statement shall be furnished.

(3) Opportunity shall be afforded all parties to respond and present evidence and argument on all issues involved.

(4) Unless precluded by law, informal disposition may be made of a contested case by stipulation, agreed settlement, consent order, or default.

(5) The record in a contested case shall include:

(a) pleadings, motions, and intermediate rulings;

(b) evidence received or considered;

(c) a statement of matters officially noticed;

(d) questions and offers of proof, objections, and rulings thereon;

(e) proposed findings and exceptions;

(f) any decision, opinion, or report by the officer presiding at the hearing; and

(g) staff memoranda or data submitted to the hearing officer or members of the office of the Administrator in connection with their consideration of the case.

(6) Oral proceedings or any part thereof shall be transcribed on request of any party [, but at his expense].

(7) Findings of fact shall be based exclusively on the evidence and on matters officially noticed.]

**COMMENT**

This section is derived from Section 9 of the Revised Model Act.

**[§ 6.411. [Rules of Evidence; Official Notice]**

In contested cases:

(1) irrelevant, immaterial, or unduly repetitious evidence shall be excluded. The rules of evidence as applied in [nonjury] civil cases in the [ ] court of this State shall be followed. If necessary to ascertain facts not reasonably susceptible of proof under those rules, evidence not admissible there under may be admitted (except where precluded by statute) if it is of a type commonly relied upon by reasonably prudent men in the conduct of their affairs. The Administrator shall give effect to the rules of privilege recognized by law. Objections to evidentiary offers may be made and shall be noted in the record. Subject to these requirements, if a hearing will be expedited and the interests of the parties will not be prejudiced substantially, any part of the evidence may be received in written form;

[ (2) documentary evidence may be received in the form of copies or excerpts, if the original is not readily available. Upon request, parties shall be given an opportunity to compare the copy with the original;]

(3) a party may conduct cross-examinations required for a full and true disclosure of the facts;

(4) notice may be taken of judicially cognizable facts. In addition, notice may be taken of generally recognized technical or scientific facts within the Administrator's specialized knowledge. Parties shall be notified either before or during the hearing, or by reference in preliminary reports or otherwise, of the material noticed, including any staff memoranda or data, and they shall be afforded an opportunity to contest the material so noticed. The Administrator's experience, technical competence, and specialized knowledge may be utilized in the evaluation of the evidence.]

**COMMENT**

This section is derived from Section 10 of the Revised Model Act.

**[§ 6.412. [Decisions and Orders]**

A final decision or order adverse to a party in a contested case shall be in writing or stated in the record. A final decision shall include findings of fact and conclusions of law, separately stated. Findings of fact, if set forth in statutory language, shall be accompanied by a concise and explicit statement of the underlying facts supporting the findings. If, in accordance with rules of the Administrator, a party submitted proposed findings of fact, the decision shall include a ruling upon each proposed finding. Parties shall be notified either personally or by mail of any decision or order. Upon request a copy of the decision or order shall be delivered or mailed forthwith to each party and to his attorney of record.]

**COMMENT**

This section is derived from Section 12 of the Revised Model Act.

**[§ 6.413. [Licenses]**

(1) Whenever the grant or denial of a license is required to be preceded by notice and opportunity for hearing, the provisions of this Part concerning contested cases apply.

(2) A revocation, suspension, annulment, or withdrawal of a license is unlawful unless the Administrator, before instituting proceedings, gives notice by mail to the licensee of facts or conduct which warrant the intended action, and the licensee was afforded an opportunity to show compliance with all lawful requirements for retention of the license.]

**COMMENT**

This section is derived from Section 14 of the Revised Model Act.

**[§ 6.414. [Judicial Review of Contested Cases]**

(1) A person who has exhausted all administrative remedies available before the Administrator and is aggrieved by a final decision in a contested case is entitled to judicial review under this Part. This section does not limit utilization of or the scope of judicial review available under other means of review, redress, relief, or trial de novo provided by law. A preliminary, procedural, or intermediate action or ruling of the Administrator is immediately reviewable if review of the final decision of the Administrator would not provide an adequate remedy.

(2) Proceedings for review are instituted by filing a petition in the [ ] court within [30] days after [mailing notice of] the final decision of the Administrator or, if a rehearing is requested, within [30] days after the decision thereon. Copies of the petition shall be served upon the Administrator and all parties of record.

(3) The filing of the petition does not itself stay enforcement of the decision of the Administrator. The Administrator may grant, or the reviewing court may order, a stay upon appropriate terms.

(4) Within [30] days after service of the petition, or within further time allowed by the

court, the Administrator shall transmit to the reviewing court the original or a certified copy of the entire record of the proceeding under review. By stipulation of all parties to the review proceedings, the record may be shortened. A party unreasonably refusing to stipulate to limit the record may be taxed by the court for the additional costs. The court may require or permit subsequent corrections or additions to the record.

(5) If, before the date set for hearing, application is made to the court for leave to present additional evidence, and it is shown to the satisfaction of the court that the additional evidence is material and there were good reasons for failure to present it in the proceeding before the Administrator, the court may order that the additional evidence be taken before the Administrator upon conditions determined by the court. The Administrator may modify his findings and decision by reason of the additional evidence and shall file that evidence and any modifications, new findings, or decisions with the reviewing court.

(6) The review shall be confined to the record and be conducted by the court without a jury. In cases of alleged irregularities in procedure before the Administrator, not shown in the record, proof thereon may be taken in the court. The court, upon request, shall hear oral argument and receive written briefs.

(7) The court may not substitute its judgment for that of the Administrator as to the weight of the evidence on questions of fact. The court may affirm the decision of the Administrator or remand the case for further proceedings. The court may reverse or modify the decision if substantial rights of the appellant have been prejudiced because the administrative findings, inferences, conclusions, or decisions are:

(a) in violation of constitutional or statutory provisions;

(b) in excess of the statutory authority of the Administrator;

(c) made upon unlawful procedure;

(d) affected by other error of law;

(e) clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record; or

(f) arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion.]

**COMMENT**

This section is derived from Section 15 of the Revised Model Act.

**[§ 6.415. [Appeals]**

An aggrieved party may obtain a review of any final judgment of the [ ] court under this Part by appeal to the [ ] court. The appeal shall be taken as in other civil cases.]

**COMMENT**

This section is derived from Section 16 of the Revised Model Act.

## ARTICLE 7

## Reserved for Future Use

## ARTICLE 8

## Reserved for Future Use

## ARTICLE 9

## EFFECTIVE DATE AND REPEALER

Section
9.101. Time of Taking Effect; Provisions for Transition.
9.102. Continuation of Licensing.
9.103. Specific Repealer and Amendments.

**§ 9.101. [Time of Taking Effect; Provisions for Transition]**

(1) Except as otherwise provided in this section, this Act takes effect at 12:01 a.m. on [ ].

(2) To the extent appropriate to permit the Administrator to prepare for operation of this Act when it takes effect and to act on applications for licenses to make supervised loans under this Act (subsection (1) of Section 2.302), the Part on Supervised Lenders (Part 3) of the Article on Finance Charges and Related Provisions (Article 2), and the Article on Administration (Article 6) take effect [ ].

**Note:** Insert in lieu of brackets at the end of subsection (2) either "immediately" or the earliest time possible under the constitutional or statutory requirements of the enacting State.

(3) Transactions entered into before this Act takes effect and the rights, duties, and interests flowing from them thereafter may be terminated, completed, consummated, or enforced as required or permitted by any statute, rule of law, or other law amended, repealed, or modified by this Act as though the repeal, amendment, or modification had not occurred; but this Act applies to:

(a) refinancings, consolidations, and deferrals made after this Act takes effect as to sales, leases, and loans whenever entered into;

(b) sales or loans entered into after this Act takes effect pursuant to open-end credit entered into, arranged, or contracted for before this Act takes effect; and

(c) all credit transactions entered into before this Act takes effect insofar as the Article on Remedies and Penalties (Article 5) limits the remedies of creditors.

**§ 9.102. [Continuation of Licensing]**

All persons licensed or otherwise authorized under [list statutes] on the effective date of this Act are licensed to make supervised loans under this Act pursuant to the Part on Supervised Lenders (Part 3) of the Article on Finance Charges and Related Provisions (Article 2), and that Part applies to the persons so previously licensed or authorized. The Administrator may, but is not required to, deliver evidence of licensing to the persons so previously licensed or authorized.

**COMMENT**

This section provides automatic licensing under Article 2, Part 3 (Section 2.301 et seq.) for all lenders previously licensed under the State's licensed lender statutes prior to the effective date. No application or administrative action is required and the formal license under the prior statute, which will be repealed, will be a license under Part 3 of Article 2. The Administrator, at such time as his new duties under the Code permit him an opportunity, may substitute new licenses for those in the lenders' possession, but this is entirely a ministerial act.

**§ 9.103. [Specific Repealer and Amendments]**

(1) The following acts and parts of acts are repealed:

(a)

(b)

(c) [and so on]

(2) The following acts and parts of acts are amended:

(a)

(b)

(c) [and so on]

**Note re Repealer and Amendatory Provisions**

This Act is a comprehensive statute designed to regulate most aspects of consumer credit, maximum charges that may be made for consumer credit and rates of interest generally. Consumer credit covered includes sales credit related to the sale to consumers of goods or services, consumer loan credit, some credit related to the sale or financing of homes and some agricultural credit. All States have one or more acts regulating consumer credit and rates of interest and in many States additional provisions performing the same function appear in various

other acts. To accommodate existing law to this Act, each State enacting this Act will need to repeal one or more existing acts or particular provisions in acts and may have to amend one or more other acts. The purpose of this Note is to suggest to the statutory revisor or other person preparing this Act for introduction into a particular State Legislature the acts which should be repealed or amended. To produce the uniformity which the Commissioners believe desirable, acts should be repealed or amended as recommended in this Note.

**Acts to be Totally or Substantially Repealed**

Subject to other specific suggestions of this Note, certain existing acts devoted primarily to regulating consumer credit should be repealed in their entirety. The revisor or draftsman should insert in this section the appropriate statutes or provisions to be repealed. To help guide the search for these acts or provisions, a list of some of the common popular names of these acts follow, although there may be others in any particular jurisdiction:

Small loan acts, personal loan acts, consumer loan acts, acts licensing personal loan lenders, sales finance companies, consumer finance companies, and industrial loan acts.

Instalment loan laws.

Retail instalment sales acts, motor vehicle instalment sales acts, all goods acts.

Revolving sales credit acts, revolving loan acts.

Truth in Lending acts.

Home solicitation sales acts.

Home improvement sales and loan acts.

Insurance premium financing acts.

**Acts Permitting Maximum Charges for Credit and General Usury Acts**

Repeal of the above listed consumer credit regulatory acts will automatically repeal provisions in these acts permitting maximum charges for the types of credit dealt with in the acts. In addition, all general usury statutes and all other provisions in acts permitting maximum charges for loans, forbearance, or the extension of credit should be repealed, excepting only provisions, if any, for maximum charges to be made by pawnbrokers.

Statutes providing for a "legal rate" of interest, that is, the rate to be applied for judgments, notes and other cases where there is no agreed rate or no agreement is possible (as in a judgment) should not be repealed. If these statutes are so intertwined with maximum contract rates, e.g., usury provisions, that it is difficult to separate the two types of provisions, total repeal of the usury and legal rate statute plus the addition of the following provision in this Act or elsewhere in the State statutes may be in order:

"If there is no agreement or provision of law for a different rate, the interest of money shall be at the rate of [six] per cent per annum."

### Provisions of Existing Statutes Affecting Powers of Organizations

In some States provisions relating to rates of interest are intertwined with provisions relating to powers of particular types of organizations, *e.g.*, licensed lenders, consumer finance companies, commercial and industrial banks and trust companies, and thrift institutions such as credit unions, savings, banks, and savings and loan associations whether or not organized for profit. In these cases statutory provisions should be repealed, preserved or amended according to Section 1.108 of this Act. See Comment to Section 1.108.

### Uniform Commercial Code

The Official Text of Uniform Commercial Code Section 9-203 and the Note which follows it read in part as follows:

"A transaction, although subject to this Article, is also subject to . . . . .*, and in the case of conflict between the provisions of this Article and any such statute, the provisions of such statute control. Failure to comply with any applicable statute has only the effect which is specified therein.

> **Note:** At * . . . insert reference to any local statute regulating small loans, retail instalment sales and the like"

If a State which enacted the UCC followed the instructions in the Note and inserted at the asterisk in UCC Section 9-203 references to local statutes regulating small loans, retail instalment sales and the like, UCC Section 9-203 should be amended to substitute a reference to the Uniform Consumer Credit Code in lieu of those listed statutes. No other provisions of the UCC need be amended if it was enacted without variation from uniform language.