



Case Western Reserve Law Review

Volume 20 | Issue 3

1969

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Recommended Citation

Gilbert M. Manchester, *Consumer Credit: The Ohio Retail Installment Sales Act and Its Abuses*, 20 Case W. Res. L. Rev. 621 (1969)
Available at: <https://scholarlycommons.law.case.edu/caselrev/vol20/iss3/7>

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*Consumer Credit: The Ohio Retail Installment Sales Act and Its Abuses**

THE CURRENT SOCIETAL interest¹ in consumer credit transactions is one of the major fronts in the war on poverty. One tenacious enemy in the Ohio theatre of that conflict is the retail installment sale and the armor of confusion and ignorance which surrounds it. Numerous weapons have recently been designed to eradicate this confusion, notably the Truth in Lending Act² and the proposed Uniform Consumer Credit Code. Before resorting to such sophisticated weaponry, however, more intelligent use should be made of existing conventional weapons, mainly the Ohio Retail Installment Sales Act (RISA).³ Retail merchants and financial institutions daily effect a substantial number of practices which violate the letter and the spirit of the RISA.

The purpose of this Note is to examine the RISA and to present for clarification the innovations, gimmicks, and abuses⁴ of the RISA practiced by retail sellers and their companion financial institutions. Such treatment should acquaint both the legal profession and those in the commercial community who unknowingly are violating the law with the substance and the consequences of those violations.

I. THE RETAIL INSTALLMENT SALES ACT

In general, installment sales acts were passed to relieve economic burdens on low-income, high-risk consumers.⁵ The high credit risk involved in selling to needy consumers prohibited retail merchants from installment selling at regular interest rates, and usury

* The writer gratefully acknowledges the help of Marvin A. Sicherman, who was counsel for the trustee in bankruptcy in the *Sloan* case, discussed in text accompanying note 13 *infra*.

¹ Former President Johnson was perhaps the most prestigious proponent of increased consumer protection when he called upon Congress in his 1968 State of the Union Message to become the "consumer-conscious Congress."

² Consumer Credit Protection Act, Pub. L. 90-321, 1968 U.S. CODE CONG. & AD. NEWS 1232. Because the Truth in Lending Act is primarily thrust at the disclosure of relevant rates and charges in consumer credit transactions, an extended discussion of that recent act will be of little value for the purposes of this Note. The Ohio Retail Installment Sales Act (RISA) is *regulation* oriented as well as *disclosure* oriented, and this Note will be more concerned with the regulatory phase of that Act.

³ OHIO REV. CODE ANN. §§ 1317.01-99 (Page 1953) [hereinafter cited as CODE].

⁴ The abuses examined in this Note are not intended to be exhaustive of those commonly practiced by the so-called commercial establishment. It is hoped that the abuses here presented will enlighten the reader so that he will be able to recognize related abuses and deal with them effectively.

⁵ B. CURRAN, TRENDS IN CONSUMER CREDIT LEGISLATION 1-5 (1966).

statutes prohibited the interest rates required to make such installment selling safe and profitable. The result was that the installment sale was a rarity, and this type of consumer was forced to delay his purchase until he had saved the full purchase price on his own. Retail installment sales acts generally alleviate this problem by permitting a higher rate of interest to cover the risk while at the same time setting up strict requirements for the form and substance of installment contracts in order to protect the consumer.⁶

The Ohio Retail Installment Sales Act became effective on August 10, 1949.⁷ The two major thrusts of the Act are its requirements for the form of the contract and for the maximum interest rates which can be charged for a retail sale on time. The retail installment sales contract (RISK) must be in writing,⁸ and every RISK must recite the following: (1) the cash price of the specific good to be sold; (2) the amount of the down payment or trade-in value; (3) the unpaid balance (the difference between (1) and (2)); (4) the amount of the finance charge; and (5) the time balance (the total indebtedness owed by the buyer to the seller).⁹

Each RISK contains a finance charge, and the Ohio Act provides specific regulations prescribing the amount and incidence of those charges. The finance charge is severable into two distinct entities — the base finance charge and the service charge. Section 1317.06 allows a base finance charge not to exceed \$8 per \$100 a year.¹⁰ This base finance charge is regarded as simple interest. In addition to the finance charge, section 1317.06 also allows a service charge of 50 cents per month for the first \$50 unit and 25 cents per month for each of the next five \$50 units. The service charge can never amount to more than \$21 per year.¹¹

When the above regulatory rates are violated, the results to both the installment seller and anyone purchasing his chattel paper can truly be disastrous. Section 1317.08 provides that if a RISK charges more than the act allows or that if a RISK evidences a debt greater than that allowed by the Act, both the RISK and the secur-

⁶ *Id.*

⁷ See 23 OHIO BAR J. 357 (1950).

⁸ CODE § 1317.02.

⁹ CODE § 1317.04.

¹⁰ For a comparison of all states' RISA rates and charges in chart form, see B. CURRAN, *supra* note 5, at 270.

¹¹ Suppose, for example, that the unpaid balance was \$300. Fifty cents per month for the first \$50 unit would amount to \$6 for a year. Twenty-five cents per month for each of the next five \$50 units would amount to \$15. Thus the maximum service charge per year would be \$21 (\$15 plus \$6).

ity interest created by the RISK shall be *unenforceable*.¹² Thus, the buyer is left with the good for which he has paid little if anything, and the seller is left with an unenforceable evidence of indebtedness.

The wronged buyer under section 1317.08 must prove that the seller was notified of the overcharge and failed to give full credit, or he must prove that the overcharge was willful. If the buyer meets the burden of proof, Ohio's civil penalties are unusually strict in that, given the proper circumstances, a seller violating RISA will lose both the principal, the interest, and the security interest in the good. The buyer may keep the good without paying for it, and any amounts already paid by the buyer are recoverable from the seller.

On its face, the Ohio RISA seems fairly clear cut: its formal requirement provisions call for a certain listing of items purchased in the contract; the finance and service charges are fair and easily understood; and its civil and criminal penalty provisions are seemingly strict enough to deter any deviation on the part of the retail merchant. However, so long as the retail seller is profit motivated, he will forever tap the resources of his ingenuity to come up with a variation or deviation of the law, put it in the form of a RISK, and thereby violate both the letter and spirit of the statute.

II. ABUSES AND INNOVATIONS

A. *Negative Equity*: In re *Sloan*¹³

Recently, the United States District Court for the Northern

¹² CODE § 1317.08 reads in part:

No retail installment contract which evidences an indebtedness greater than that allowed by section 1317.06 or 1317.07 of the Revised Code and no retail installment contract in connection with which any charge prohibited by sections 1317.01 to 1317.11, inclusive, of the Revised Code, has been contracted for or received *shall be enforceable* against any retail buyer, or any other person . . . liable on the obligation created by any retail buyer . . . and *no security interest* created by any such retail installment contract . . . *shall be enforceable* against any retail buyer . . . (Emphasis added.)

The Ohio RISA also provides criminal penalties for willful violations. CODE § 1317.99 (A) provides that "[W]hoever willfully violates sections 1317.01 to 1317.11, inclusive, of the *Revised Code*, shall be fined not more than one thousand dollars or imprisoned not more than one year, or both."

Whether or not an *informed* buyer can take advantage of the RISA penalties by intentionally drawing the seller into an unenforceable contract and relying on the fact that the seller will not change the rates after he has received notification is open to question. In that situation, the buyer should be estopped by his own bad conduct to call upon the aid of the RISA. The fraud of the buyer should be a defense to the harsh penalties of section 1317.08, and the parties should then be returned to status quo.

¹³ 285 F. Supp. 1 (N.D. Ohio 1968). For a criticism of the *Sloan* decision, see Note, 30 OHIO ST. L.J. 144 (1969).

District of Ohio was called upon to construe the Ohio RISA for the first time in a federal court. In 1966 Dewie Sloan approached Commerce Ford, Inc. to buy a new Ford. Mr. Sloan wished to trade his 1965 Ford for the new car. Commerce would allow only \$1600 trade-in value for the 1965 Ford, for which a prior loan balance of \$2143.64 was still owing to a third party. In order to make the sale of the new Ford and in order to allow Mr. Sloan to buy the new car, Commerce inserted under the trade-in item of the RISK the figure "(-\$543.64)," the difference between Commerce's appraisal of the 1965 Ford and the amount which Sloan still owed on the previous RISK. Thus the unpaid balance of the cash price on the new RISK was an amount \$543.64 greater than the actual cash price. The finance charge was based upon that greater figure. The inclusion of such a negative amount in the trade-in item of the RISK has been termed "negative equity" by counsel for the trustee.

Upon execution, Commerce assigned the RISK to a finance company. Unfortunately Mr. Sloan was adjudicated a bankrupt before any payments were made on the contract, and the finance company then repossessed the new Ford pursuant to the security agreement. The trustee in bankruptcy filed an application for turnover order,¹⁴ alleging that the inclusion of negative equity made the contract unenforceable. The referee, allowing the turnover, determined that the inclusion of the \$543.64 in the contract and the finance charges which were based on the addition amounted to a willful overcharge in violation of section 1317.08 and that consequently the lien created by the security agreement was void and wholly unenforceable.¹⁵

When the finance company appealed the referee's decision, District Judge Green determined that "when the retail seller included the 'negative equity' within the retail installment sales contract it was engaging in the small loan business."¹⁶ Because chapter 1317 contains no provisions allowing small loans, and since the licensing and control of small loan companies is governed by chapter 1321,¹⁷

¹⁴ An application for a turnover order is a bankruptcy proceeding whereby the trustee asserts his right of possession of an asset which is in possession of one other than the trustee.

¹⁵ By agreement of the parties, the finance company had sold the car and had turned the proceeds of the sale as a fund over to the court.

¹⁶ 285 F. Supp. at 4. The *Sloan* decision at first seems ambiguous because the negative equity was held to have been in reality a small loan. The illegality of the contract, however, is not determined in regard to the Small Loan Act, but rather solely under the Ohio RISA, which was construed to preclude the making of a small loan in the form of a RISK.

¹⁷ CODE §§ 1321.01-99.

the court ruled that when Commerce granted the small loan, it violated sections 1317.04, 1317.06, and 1317.07 of the *Ohio Revised Code*¹⁸ because the loan was made in the form of a RISK.

Having determined that the RISK was violative of the Ohio RISA, the court was forced to construe the penalty provided in section 1317.08. Because that section makes unenforceable both the RISK and the security interest, the final result to the finance company is that it has lost *all* its rights derived from the transaction. In dictum, the court stated that under section 1317.08, if a retail buyer had paid in full a RISK which had included excessive finance charges or which had evidenced indebtedness not authorized by the RISA, "he could recover every cent paid to the retail seller"¹⁹ and he could keep the chattel. The *Sloan* decision should strike terror into the hearts of every financial institution which buys RISK paper and should send installment buyers running to reexamine their agreements. The *Sloan* decision should also be a major weapon of Legal Aid offices and the neighborhood law offices in the ghetto areas, where the negative equity situation is most likely to occur.²⁰

The negative equity concept is necessarily limited to the facts of *Sloan*, or at least to a situation in which the seller is willing to give the buyer less on trade-in than the buyer already owes for the goods which he wishes to trade-in. It is arguable that such a harsh penalty is undeserved for an act which was essentially "intended for the benefit of the retail buyer."²¹ Were it not for the inclusion of negative equity, Sloan probably could not have purchased the car. The penalty is undeniably harsh, but it may be justified. Whether such transactions are motivated for the benefit of the buyers or for the benefit of sellers who sell on a high pressure, high volume basis is at least open to question. What is not open to question is the fact that Dewie Sloan was adjudged a bankrupt, and the inability to pay the obligation of the litigated RISK was one of the factors that put him in that position.

¹⁸The three sections must be construed together to find the illegality: Section 1317.04 sets out the specific items includible in a RISK. See text accompanying notes 10 & 11 *supra*. Section 1317.07 ties the two previous sections together and prohibits RISK's which "evidence any indebtedness in excess of the time balance fixed in the written instrument in compliance with section 1317.04 . . ."

¹⁹285 F. Supp. at 8.

²⁰The negative equity situation is more likely to occur where the need for credit is greatest and where the buyer is most likely to be unable to provide a *bona fide* down payment.

²¹285 F. Supp. at 6.

Statutorily, the negative equity violation is fairly clear cut. By way of example, suppose Buyer purchases a \$600 washer-dryer from Awful Appliance, Inc., with payments to run over a 3-year period. The finance charge would amount to \$144 (8 percent of \$600 x 3), and the service charge would be \$63 (\$21 x 3), giving a total time charge of \$207. The total indebtedness is \$807. Thirty-six equal installments would amount to approximately \$22.42 per month. After one full year, Buyer and his wife, having paid \$269.04 and still owing \$537.96, become very dissatisfied with the washer-dryer which had never worked correctly in the first place. They approach Acrid Appliance Co. to purchase another \$600 washer-dryer which Buyer's wife had been admiring since they had purchased the first one. Buyer and Acrid agree that he should purchase the new washer-dryer through a 3-year RISK since Buyer does not have any ready cash. Buyer wants to trade in the unsatisfactory washer-dryer, and tells Acrid that he still owes \$537.96 on a previous RISK. Taking note of the amount still owing, Acrid appraises the old washer-dryer and tells Buyer that normally they don't take Awful Appliances on trade-in, but since Buyer is in a bind, Acrid will make an exception; the most he can give him on trade-in, however, is \$337.96. Buyer is severely dismayed by the low trade-in value, but Acrid quickly reminds him that Awful Appliances' products are poorly made and that with one year's depreciation this particular unit will probably need a new motor, new wiring, and much labor to make it resaleable by Acrid. Buyer agrees.

Acrid's salesman brings out Acrid's standard form for installment sales. Under the item entitled "Cash Sale Price," he inserts \$600. Under "Trade-in," he inserts (-\$200),^{21a} the difference between the \$537.96 owed by Buyer and the \$337.96 trade-in value. Under "Unpaid Principal Balance," he inserts \$800 (\$600 plus \$200). Under "Time Price Differential," he inserts \$255, the aggregate of the 8 percent per hundred per year (\$192) plus the standard service charge for a 3-year contract (\$63). Under the last item, "Time Balance," he inserts \$1055. The RISK then recites that Buyer agrees to pay the Time Balance in 36 consecutive monthly installments, each installment to be in the amount of \$29.30 except the final installment which shall be \$29.50. Buyer and Acrid both sign the form and Buyer receives his copy.

^{21a} The (-\$200) figure is technically incorrect since it does not take into account the abatement of the unearned interest. At the end of 1 year of a 3-year contract, 55 percent of the interest is earned. A technically correct figure would be, in this case, (-\$93.20); however, for purposes of clarity in this example, the (-\$200) figure is used.

One week later, Buyer is injured on the job and cannot even meet the first monthly installment. Ten days after the first payment was due, three men, apparently from Acrid, appear at Buyer's house — two to cart off the washer-dryer, and one to demand immediate payment of the impending deficiency and cost of removal, approximately \$500. Buyer calls a lawyer.

The lawyer at first tells Buyer that Acrid has every right to proceed in the manner taken; but because Buyer is an old school-mate, he will at least look at Buyer's copy of the contract. The lawyer spots the (-\$200) under the trade-in item and wonders what it is. Buyer then explains the whole transaction from the beginning. In the seclusion of his law library, the lawyer begins to read chapter 1317 of the *Ohio Revised Code*. He finds that section 1317.04 lists the only items includible in a RISK. Section 1317.04 (A) provides for the cash price of the specific good. Section 1317.04 (B) provides for the down payment which can be in either money or goods. Section 1317.04 (C) provides for the unpaid balance, "which is *the difference between divisions (A) and (B)*."²² In Buyer's contract, there really was no down payment. Quite the contrary, whatever it was, the unpaid balance of Buyer's RISK certainly did not reflect *the difference between* the cash price and the trade-in value.²³ The lawyer determines that the RISK was not executed in compliance with section 1317.04, as is specifically required by section 1317.07 in order to make the installment contract valid under the statutory law of Ohio.

Because the trade-in arrangement amounted to a loan prohibited by section 1317.04²⁴ and because the maximum finance rate was applied to that loan as well as to the specific price of the good, the RISK showed an indebtedness greater than that allowed by sections 1317.06 and 1317.07. As such, the RISK is unenforceable and void by the terms of section 1317.08.²⁵ Not only does Buyer have a right to keep the washer-dryer but he also need not pay anything to Acrid. The lawyer's first act should be to notify Acrid

²² CODE § 1317.04(c).

²³ One can argue for a finding of illegality by noting that if the legislature had intended to allow the use of negative equity, it would not have used the phrase "the difference between," for that phrase suggests a subtraction, not an addition. Because it used that phrase, it must have intended to *exclude* negative equity from valid RISK's. In reality, however, the legislature probably never even thought of the possible inclusion of negative equity.

²⁴ See note 18 *supra* & accompanying text.

²⁵ See note 12 *supra*.

of the overcharge.²⁶ If Acrid fails to restore full credit for the overcharge within 10 days after notice, Buyer can reclaim the repossessed washer-dryer and avoid the contractual obligation altogether. Because both the underlying obligation *and* the security agreement are void according to RISA, the seller does not even have the status of an unsecured creditor.

It should be noted that finance companies which purchase RISK paper or which indirectly sponsor such RISK paper will fare no better than the hapless Acrid of the previous example. They enjoy no standard or status of holder in due course,²⁷ at least not under chapter 1317. The civil penalties in section 1317.08 apply to "the seller, his agent, assignee, or successor in interest. . . ."²⁸

*In re Sloan*²⁹ brought to light one practice which was heretofore thought to be acceptable in retail commercial circles. While the seller's wisdom of granting a loan via negative equity may be challenged since the good sold will never provide enough security to cover the debt in case of default, the negative equity situation has been and will remain prevalent in installment sales, particularly among automobile dealers who have a heavy trade-in volume.³⁰ The impact of the *Sloan* decision depends upon its communication to those who stand to benefit most from it — installment con-

²⁶ CODE § 1317.08 provides in part:

In order for a retail buyer, or any of the aforementioned persons liable on his obligation, to avail himself of this section, he must prove that the retail seller or the holder of the retail installment contract has been notified in writing of the overcharge and has failed within ten days of such notification to advise the retail buyer of a full credit, or he must prove that the overcharge has been willful. (Emphasis added.)

²⁷ Ordinarily transactions such as are discussed here would fall within the *Uniform Commercial Code*. Section 1303.31(A) defines a holder in due course to be "a holder who takes the instrument: (1) for value; and (2) in good faith; and (3) without notice that it is overdue or has been dishonored or of any defense against or claim to it on the part of any person." Thus the finance companies which buy RISK paper would generally qualify under the above definition as holders in due course and would thereby be secured parties under *Commercial Code* article 9. Section 1309.12, however, states: "Nothing in sections 1309.01 to 1309.50, inclusive . . . validates any charge or practise illegal under any statute or regulation thereunder governing . . . retail installment sales . . ." Similarly section 1309.14 (B) gives absolute priority to chapter 1317 when it conflicts with chapter 1309. Because section 1317.08 applies the penalties to assignees in addition to sellers, the benefits of holder in due course status are lost. See Note, 114 U. PA. L. REV. 395, 414 (1966).

²⁸ See note 26 *supra*.

²⁹ 285 F. Supp. 1 (N.D. Ohio 1968).

³⁰ Automobile dealers are naturally more inclined to commit the negative equity error because of the nature of the industry. Because of the high price of automobiles, they are the most likely of all the durable goods to be bought on a time basis. In addition, the used automobile industry has made the trade-in commonplace with the purchase of a new car.

sumers and the lawyers who are called upon to help them when their RISK transactions go astray.

B. The use of two RISK's

One gimmick that occurs mainly in low income consumer transactions arises when the buyer has little or no cash and nothing of value to trade in, yet desires to purchase a good which the seller is equally desirous to sell to him. Such sales are generally the result of heavy television advertising campaigns which offer expensive luxury items at seemingly low prices and at favorable terms of time payment.³¹ Typically, the buyer first communicates his lack of liquidity to the seller. The seller then contacts the finance company who is presently buying seller's RISK paper and asks to be told the amount of paper the finance company will be willing to buy from the seller for this particular buyer. The finance company replies that it will buy the buyer's RISK from the seller only if the buyer can make a down payment of a certain amount.³² Both the seller and the finance company know the buyer cannot make such a down payment. The answer is in two RISKS: one for the difference between the suggested down payment and the cash price of the good which the finance company will buy, and the other is for the amount of the suggested down payment which the seller retains *as* the down payment, thereby satisfying the finance company's admonishment that the buyer have a down payment of a certain amount. It should be noted that the maximum rates and charges permitted under chapter 1317 are typically included in the retained RISK so that upon the retained RISK the buyer ends up

³¹ See generally Note, *supra* note 27.

³² The strictness with which a particular finance company oversees a particular seller's installment sale varies, depending upon the lending policies of the finance company and the general reputation for prudence of the seller. Generally a finance company will set up a reserve account for the seller, whereby the finance company holds in reserve a portion of the purchase price of the RISK paper it buys from the seller. The reserve account builds up rapidly according to the volume of RISK paper which is sold to the finance company, and if any of the paper is not collected or goes in default, the finance company reimburses itself from the reserve account. As the RISK paper is collected by the finance company over a period of time, part of the reserve account is released to the seller. The reserve account is continuously being increased by new RISK paper at the same time that it is being decreased by the release of old RISK paper and therefore remains at about the same amount. The finance companies can gauge their success with a particular seller by watching the activity within the reserve account, and if there is too much activity, that is, a frequent necessity to reimburse the finance company from the reserve account, the finance company will usually terminate its business with that seller. A particular seller's prudence in installment sales can therefore be gauged by noting the frequency with which he changes financial companions.

owing much more than just the finance company's suggested down payment.³³ The other RISK covers the same good as the retained RISK and recites the amount suggested by the finance company as the down payment, leaving an unpaid balance of the same amount as stated in the down payment of the retained RISK. The two RISK's together, therefore, act as the down payments for each other. In reality, both RISK's are somewhat fictional in that it is actually a loan of the suggested down payment and has no relation to the transaction other than the tentative manufacture of a down payment;³⁴ the second RISK is fictional in the sense that it has recited a down payment which has never taken place.³⁵ The illegality of the two RISK's occurs because the rates and charges of the two together exceeds the statutory limit. The buyer will be paying service charges of \$21 per year on two contracts when he should be paying that amount on only one. The two RISK's must be considered one contract since each is invalid on its own terms because of the fictitious nature of the down payments recited in each.³⁶ When the RISK's are construed together, the service charges are excessive, and both would be void and unenforceable under section 1317.08.

If the rare situation occurs in which the seller charges only simple interest in the first RISK, without the service charge, the transaction is nevertheless assailable under the *Sloan* rationale.³⁷ No matter what the buyer and seller wish to call the first RISK, it is in reality an outright loan of money. Since the seller is undoubtedly not a licensed small loan company, he has no business making this loan. He is more in error for making the loan in the form of a RISK because the purpose of the Ohio RISA was to provide a means to purchase a specific good on an extended time basis.³⁸ The mak-

³³ The total amount owing for the *down payment alone* would include: the amount of the down payment; the base finance charge; and the service charge.

³⁴ CODE § 1317.04(B) reads: "The amount in cash of the retail buyer's down payment, if any, whether made in money or goods or partly in money or partly in goods." A negotiable instrument, while having some of the qualities of both money and goods, is neither in itself.

³⁵ The fact that the seller might be able to convert the first RISK into cash will not satisfy section 1317.04(B), because the subsequent sale of the seller's RISK is no part of the original transaction. Most typically the seller simply holds on to the first RISK, knowing that in case of default, the finance company will repossess on the strength of the second RISK. The profit on those transactions in which default never occurs is great enough to offset the seller's loss on those few first RISK's which are not paid off.

³⁶ The proof of the down payment for each RISK would necessitate the production of the other since they each represent the other's down payment.

³⁷ See notes 16-18 *supra* & accompanying text.

³⁸ The only other case to construe chapter 1317 was *Teegardin v. Foley*, 166 Ohio St. 449, 143 N.E.2d 824 (1957), in which the court stated:

ing of small loans is governed by the Small Loan Act,³⁹ and the two types of transactions should not be commingled.

The two-RISK situation is particularly debilitating to the low income consumer because his payment terms are usually extended over a longer period of time,⁴⁰ thereby increasing both the finance charge (interest rate) and the service charge. When he is faced with two payments per month where in reality he should be paying only one, his chances of being driven into bankruptcy are increased to a degree proportionate to the overcharge resulting from the two RISK's.

C. *Increasing the Cash Selling Price*

To the seller who is aware of the difficulties of negative equity and the two-RISK situation, another innovation is available for him to reach the same contractual result: he merely increases the cash selling price by the amount he wishes to loan the buyer in order to consummate the sale. For example, assume that Buyer approaches Seller wishing to trade in a good for which he still owes \$1000. Seller is willing to allow only \$500 for the used good on trade-in, but in order to avoid the negative equity situation,⁴¹ the seller recites on the RISK a trade-in value of \$1000 while simultaneously increasing the cash selling price of the new good which the buyer is purchasing by \$500. Such an increase in the cash price is clearly prohibited under the Ohio RISA. Section 1317.01(K) defines "cash price" to mean the price at which the subject matter of the contract would be sold if the sale were an immediate cash sale instead of a time sale.⁴² Because the inflated cash price in the above example is clearly inconsistent with the de-

The General Assembly, however, in enacting legislation requiring retail automobile dealers and financial institutions to be licensed under separate laws and answerable to separate state agencies, has, without being arbitrary, clearly considered each of said businesses as being in a separate class for certain purposes. *Id.* at 464, 143 N.E.2d at 834 (emphasis added).

³⁹ CODE §§ 1321.01-99.

⁴⁰ See generally D. CAPLOVITZ, *THE POOR PAY MORE* (paperback ed. 1967); Note, 76 YALE L.J. 745 (1967), which contain discussions of related problems of low-income consumers.

⁴¹ Depending upon how *Sloan* is interpreted, negative equity could be construed to include any transaction which is in reality the making of a loan through the use of a RISK.

⁴² CODE § 1317.01(K) states:

"Cash Price" means the price measured in dollars, agreed upon in good faith by the parties as the price at which the specific goods which are the subject matter of any retail installment sale would be sold if such sale were a sale for cash to be paid upon delivery instead of a retail installment sale.

defined cash price of the statute, the RISK will not have been executed in compliance with section 1317.04. Because the rates and charges covering that portion of the RISK which was a prohibited loan are excessive, the RISK is unenforceable under section 1317.08 in the same manner as was the negative equity RISK and the two-RISK situation.⁴³ The enforcement of the Ohio RISA in the inflated cash price situation, therefore, should not be too difficult under the terminology of the Act.

However, totally prohibiting the inflated cash price will be extremely difficult. Retail merchants are typically outspoken concerning their rights to sell what they please, to whom they please, and at whatever price they please. Any effort to establish a standard cash price of a specific good for the purposes of comparing it to an alleged inflated cash price will probably be met with a fervent outcry of "governmental price control!"⁴⁴ The seller will argue that he has a right to charge "whatever the traffic will bear," while he also conjures up notions of old style capitalistic enterprise. Such an argument can be overcome by noting that in establishing the standard cash price as defined in section 1317.01(K) the test is one of good faith by the parties to the transaction.⁴⁵ With the help of the buyer who now wants to avoid the obligations created by the prohibited RISK, proof of the actual loan in the form of an inflated cash price can be accomplished.⁴⁶ The process will be strenuous, however, since the actual abuse of the Ohio RISA does not appear on the face of the RISK as it does in the previously discussed abuses.⁴⁷

It should be noted at this point that the above three abuses — negative equity, the use of two RISK's, and the inflated cash price — all result from the desire of the seller to make a loan to the buyer. Although assumedly the buyer also desires the loan, he is

⁴³ See note 12 *supra* & accompanying text.

⁴⁴ This argument misses the issue entirely, for the test is not what is the seller's price of the good for *all* buyers — only what would have been his price to this particular buyer if this buyer had been paying the full cash price.

⁴⁵ See note 42 *supra*.

⁴⁶ The buyer, of course, will now be willing to offer his version of how the cash price was reached since the buyer has so much to gain under section 1317.08 by showing the RISK to contain an unauthorized loan.

⁴⁷ In the inflated cash price situation, proof of the violation must go *beyond* a mere showing of the RISK, since the price cannot be deemed to be *inflated* merely by looking at it. Negative equity, however, can be spotted merely by noting the presence of a negative or minus figure under the trade-in item of the RISK. The two-RISK situation is similarly obvious on the face of the RISK because there are two corresponding RISK's.

probably unaware⁴⁸ of the long term harm it causes him by way of excessive rates and charges. Certainly the buyer is unaware of the illegality of such transactions under the Ohio RISA, as are most retail sellers and finance companies.

If the seller genuinely wishes the buyer to get a loan so that he can afford to purchase the good, he should send the buyer to a bona fide independent small loan company or a bank.⁴⁹ He should not try to consummate the loan himself under the guise of a RISK. What is basically wrong with a loan incorporated into a RISK, aside from the excessive charges, statutory violations, and the harm to the buyer, is that in each case the seller is arranging the financing for *more* than he is selling. The security interest in the chattel which is created by the RISK will simply not cover the total indebtedness in case of a default. A question arises as to why sellers would be willing to take the chance of creating a partially unsecured debt on such a wide scale. Perhaps the reason is that the risk of default is not so great as merchants and financial institutions would have the public believe.⁵⁰ The aggregate loss from defaults is probably much less than the revenue derived from the excessive charges to those buyers who actually pay.

D. *The Direct Loan Concept*

One recent innovation sponsored by the banking industry is the concept of a direct loan. Instead of having the seller execute a RISK with the buyer and then having the bank purchase the RISK from the seller, the buyer takes a direct loan from the bank, on the bank's form, executed at the seller's place of business. The buyer never goes to the bank, and the seller never signs the contract and is not a party to the paper. The seller delivers the security agreement to the bank for the bank's approval, and the seller takes the proceeds of the loan from the bank and gives the purchased good to the buyer. The end result to the buyer is the same as if he and the seller had executed a RISK which the seller then assigned to

⁴⁸ See sources cited in note 40 *supra*.

⁴⁹ While such a procedure is more time-consuming and certainly more difficult for the consumer, he avoids the negative equity problem. In addition, the ordeal of having to go through two or more security-oriented transactions in order to purchase the desired good will have a two-fold effect: first, the buyer will be exposed to the intricacies and pitfalls of retail finance arrangements *twice*, thereby possibly *informing* him of the actual rates in each more so than if the entire purchase were consummated on one RISK; second, the *bother* of obtaining a separate loan and the time involved would serve to minimize any spur-of-the-moment, unwise buying.

⁵⁰ See text accompanying note 6 *supra*.

the bank. In each case, the buyer makes his payments to the bank. The legality of the direct loan concept hinges in part upon whether RISA formalities are observed or whether the loan is executed on a standard bank loan form.⁵¹ The rate of interest charged is also relevant.

If RISA formalities are observed and if RISA rates are applied to the loan, the transaction begins to look like a standard RISK, minus the retail merchant. The banking industry and retail merchants, primarily automobile dealers, have been cooperating in the use of the direct loan. On the strength of an Ohio Attorney General's Opinion,⁵² banks have been proceeding under the assumption that the direct loan does not involve a retail installment sale. However, under section 1317.01(A), "Retail installment sale" is defined to include "every retail sale of specific goods to any person in which the cash price may be paid in installments over a period of time." The direct loan as now practiced would seem to fit that definition. Section 1317.01(I) defines "Retail seller" to mean "a seller who is a party to a retail installment sale." In a direct loan, the retailer is not a party to the paper. Who, then, is the seller? Perhaps, since the bank is the only party to the paper other than the buyer, the bank is the "seller," acting as the agent for the seller in fact.⁵³ If the bank is the seller, it is probably transacting business not included in the purpose clause of its articles of incorporation. While the making of loans is clearly a function incidental to banking, the assumption of the status of a retail installment seller clearly is not such a function.

In any case, it would seem that the direct loan as now practiced by banks is a violation of the branch banking laws.⁵⁴ The retail

⁵¹ If RISA formalities are observed, there is little question about the application of RISA regulation. The more difficult question arises when the transaction has none of the *formalities* of a RISK but nevertheless is, in substance, a RISK.

⁵² *OP. ATT'Y GEN. (OHIO) 65-58 (1965)* involved the question of whether the payment of a finder's fee to the seller by a bank in the direct loan situation violates section 1317.08. The Ohio Attorney General ruled that for purposes of the payment of the compensation for such a service, the direct loan was not a retail installment sale and that section 1317.08 did not apply. This is not to say, however, that the direct loan is not a retail installment sale for *any* purpose.

⁵³ This line of reasoning may at first appear to be absurd, for clearly the bank intends only to function in such a transaction as a lender of money, not as a seller of consumer goods. However, "seller" takes on a special meaning since there is a statutory definition, and it is not absurd to view the bank as the seller in light of that clear definition.

⁵⁴ CODE § 1101.01(D) defines "Branch" to be:
an office or other place at which a bank receives money or its equivalent from the public for deposit and conducts a *general banking business*, but does not

merchant is acting as an agent for the bank if he solicits a loan to the buyer on behalf of the bank. Since the seller typically does this solicitation at his own place of business, the bank is in effect setting up a limited purpose branch at a location other than its licensed banking location.⁵⁵ In order to properly proceed with the direct loan concept, ruling out RISA altogether, the bank might be forced to secure a branch license from the Ohio Superintendent of Banks⁵⁶ or the Comptroller if the bank is a national bank.⁵⁷

The direct loan concept, while a praiseworthy idea on the part of the banking industry's efforts to facilitate commercial transactions and increase the general flow of commerce, nevertheless should be subject to all the regulating of the Ohio RISA. When one looks behind the intricacies of the contractual arrangement, what appears is still a retail purchase of a consumer good on an installment-time basis. The primary concern should be the protection of the buyer. If the direct loan is held to be outside of the bounds of the RISA, the buyer is left with an installment sale without the protection which the legislature intended to give to that buyer.⁵⁸

III. CONCLUSION

The innovations and gimmicks set forth above are by no means exhaustive of the abuses presently practiced under the Ohio RISA.⁵⁹ Nor will the ingenious invention of similar abuses cease so long as

include a bank's principal place of business. The term "branch" does not include:

(1) Any place, such as a . . . commercial, retail, or manufacturing establishment, at which a person other than a bank carries on a business or conducts operations *and at which such bank only receives items for subsequent deposit* from such establishment (Emphasis added.)

Note that in the direct loan situation, the bank is doing much more than receiving items for subsequent deposit. It is soliciting and receiving and consummating loan business which, in the ordinary course, occurs only at the physical location of the bank.

⁵⁵ The question thus narrows to whether it is permissible and/or desirable for a bank to permeate into other areas of business, impose its practices upon transactions specifically regulated by statute in a manner inconsistent with banking regulation, and thus thwart the legislative intent as to the regulation of those other areas of business.

⁵⁶ The establishment of state branches is governed by chapter 1111 of the CODE.

⁵⁷ The establishment of national branches is governed by 12 U.S.C. § 36 (Supp. 1969).

⁵⁸ Cf. note 38 *supra*.

⁵⁹ Among some of the notorious abuses presently practiced but not covered in this Note are the wrongful imposition of delinquent payment charges in connection with revolving charge accounts and the widespread use of RISK formalities and rates in the home-improvement contract in which the essential benefit of the contract is the extensive labor involved in installing relatively few goods.

retail merchants are forced by a competitive commercial community to make the best of the marketplace supply and demand system. What has taken place in Ohio is that the Ohio RISA has been treated by sellers, financial institutions, and the legal community in general, as legislation which enables and protects only the retail installment contract. Chapter 1317's provisions seemingly are seen only as guidelines by which retail installment contracts are formed and as the official guideline for applying rates and charges to the RISK. What has gradually become disregarded is the other aspect of the Ohio RISA — perhaps its more important aspect — the built-in buyer protection.

*In re Sloan*⁶⁰ should be credited with the partial resuscitation of the buyer protection side of the Ohio RISA. Although the facts of *Sloan* are narrowed to the occurrence of negative equity, the decision opens a line of analysis which can be used to draw to the surface and assail some of the other abuses which are presently being practiced and also those future abuses which are as yet untried. Perhaps the best deterrent to the gimmicks which violate the Ohio RISA would be the wide spread communication of both the forms in which the abuses appear and the showing of their illegality under chapter 1317 of the *Ohio Revised Code*. When that communication is accomplished and the wholesale use of such innovations is slowed, the road to attacking the other problems of the urban poor will be made easier.

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⁶⁰ 285 F. Supp. 1 (N.D. Ohio 1968).