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A FUNCTIONAL ANALYSIS OF TRUTH IN LENDING

Jonathan M. Landers*
and Ralph J. Rohner**

INTRODUCTION

Lawmakers frequently have an imperfect view of the objectives and probable impact of legislative innovations when they spring into being. This shortcoming is truly reflected in efforts to provide meaningful disclosure to consumers in credit transactions. Ten years after the enactment of the federal Truth in Lending Act,¹ we find numerous symptoms of disquietude with the law:²

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Both authors have served as consultants on Truth in Lending to the Board of Governors of the Federal Reserve System. The views expressed herein are those of the authors and not necessarily the Board of Governors. The authors thank Professor Alan Schwartz of the University of Southern California, who read an earlier draft and made a number of insightful suggestions.

1. The Truth in Lending Act is subchapter I of the Consumer Credit Protection Act, 15 U.S.C. §§ 1601-1667 (1976). The Act is administered by the Federal Reserve Board, which has issued an interpretive regulation, popularly called "Regulation Z." 12 C.F.R. §§ 226.1-1503 (1978).

2. The multi-sided debate emerges clearly through several sets of Senate Banking Committee Hearings. See *Oversight on Consumer Protection Activities of Federal Banking Agencies: Hearings Before the Senate Comm. on Banking, Housing and Urban Affairs*, 94th Cong., 2d Sess. (1976); *Simplify and Reform the Truth in Lending Act: Hearings on S. 1312, S. 1501 and S. 1653, Before the Subcomm. on Consumer Affairs of the Senate Comm. on Banking, Housing and Urban Affairs*, 95th Cong., 1st Sess. (1977) [hereinafter cited as *Simplification Hearings*]. Of particular note is Senator Proxmire's recognition of the difficulties. *Id.* at 4-5, 115-19, 353-55; see S. REP. NO. 720, 95th Cong., 2d Sess. 2 (1978). For a strong judicial expression, see *Sanders v. Auto Assocs.*, 450 F. Supp. 900 (D.S.C. 1978); *Wilson v. Allied Loans, Inc.*, 448 F. Supp. 1020 (D.S.C. 1978).

sponsors disclaiming responsibility for the present law, consumers and creditors alike claiming that disclosure statements are unnecessarily complex, and a steady stream of litigation flowing. The ground rules for disclosure become so complex that creditors convinced a number of pro-consumer legislators to adopt a novel procedure permitting the Federal Reserve Board to issue so-called "blessed letters," a mechanism which protects creditors from legal challenges that had their source in the vagaries of the disclosure requirements.³ A related disclosure statute, the Real Estate Settlement Procedures Act, proved so unworkable that an embarrassed Congress had to reform real estate transaction disclosure rules that had been effective less than a year.⁴ There is a widespread conviction that something has gone wrong but little understanding of what it is, and what can be done.

This conviction has led to a movement for Truth in Lending "simplification."⁵ "Simplification" is one of those terms that diverse groups support in theory; differences come about quickly when the concept is defined. Truth in Lending simplification may mean a less restrictive statute, easier to read and less information-packed forms; reduced liability; additional defenses; greater pre-

3. 15 U.S.C. § 1640(f) (1976); see Reg. Z, 12 C.F.R. § 226.1(d)(3) (1978). The so-called "blessed letters" are ex parte letters which immunize creditors from civil liability if they follow a staff-approved disclosure practice. Unfortunately, the letters have substantially eroded the consumer protections in the Act itself. See, e.g., FRB Off. Staff Int. No. FC-0130, [1974-1977 Transfer Binder] CONS. CRED. GUIDE (CCH) ¶ 31,570 (1977) (permitting post-sale disclosures in many credit transactions); FRB Off. Staff Int. No. FC-0060, [1974-1977 Transfer Binder] CONS. CRED. GUIDE (CCH) ¶ 31,570 (1977) (exempting late charge similar to finance charge on open end plan); cf. *Willis v. Town Fin. Corp.*, 416 F. Supp. 10 (N.D. Ga. 1976) (letter stating that creditors are not required to disclose that security interest in after-acquired consumer goods is limited to property acquired within ten days of transaction provides less protection than that given by the courts). The "blessed letter" practice has come under criticism on the grounds that letters are an ex parte declaratory judgment and also amount to administrative rulemaking without compliance with the Administrative Procedure Act (APA), 5 U.S.C. §§ 551-706 (1976). As this Article was being completed, the Board amended Regulation Z to permit public comment on "blessed letters." 12 C.F.R. § 226.1(d)(2) (1978).

4. Pub. L. No. 93-533, 88 Stat. 1724 (1974), as amended by Real Estate Settlement Procedures Amendments of 1975, Pub. L. No. 94-205, 89 Stat. 1157 (1976). See Rohner, *Consumer Credit Legislation in the Ninety-Fourth Congress—and a Look Ahead*, 9 U.C.C. L.J. 307, 345-49 (1977).

5. Several Truth in Lending simplification bills were introduced in Congress early in 1977. Senator William Proxmire (D. Wis.), Chairman of the Senate Banking Committee, took the lead in pushing a composite bill through that Committee; it passed the Senate on May 10, 1978. S. 2802, 95th Cong., 2d Sess., 124 CONG. REC. S7232 (daily ed. May 10, 1978); see S. REP. NO. 720, 95th Cong., 2d Sess. 2 (1978). No action was taken on S. 2802 in the House of Representatives before the 95th Congress adjourned. A virtually identical bill, S. 108, has been introduced in the 96th Congress, and, at this writing, has been reported favorably from the Senate Banking Committee. Since a more complete legislative record exists as to S. 2802, references to proposed simplification legislation will be limited to that bill.

emption of state law; or a host of other concepts. Fundamentally, these varied perceptions are grounded in differences regarding the described functions and achievable purposes of Truth in Lending ("TIL"), and they invite an analysis which can draw on a decade of experience with the present law.

The purpose of this Article is to take a hard look at the possible objectives of a disclosure statute such as TIL, and ask the basic question whether these objectives are attainable, and if so, what type of a statute can best effectuate the legislative policies. Given the lawmakers' fascination with disclosure-type legislation in the scheme for protecting consumers, and the myths that accompany such legislation, this undertaking should prove useful.

I. AFFECTING TRANSACTIONAL BEHAVIOR

The basic premises of TIL were that consumers needed certain information to make essential decisions in consumer credit transactions and that the information then available as part of the contracting process, or provided as a result of state law requirements, was inadequate. Proponents of Truth in Lending intended and expected the disclosed information to influence a consumer's behavior in the particular transaction in which the disclosures were furnished. The Act itself faithfully articulates this purpose: "It is the purpose of this subchapter to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit"⁶

To accomplish this purpose, the Act and the Board's implementing Regulation Z adopt a number of conventional means of conveying information. First, the Act standardizes certain concepts such as the Finance Charge and the Annual Percentage Rate (APR).⁷ Then, Regulation Z designates an "official name" for many of the concepts and requires that creditors use only the official name.⁸ Once a consumer understands a particular term, fu-

6. 15 U.S.C. § 1601(a) (1976); *see, e.g.*, *Johnson v. McCrackin-Sturman Ford, Inc.*, 527 F.2d 257, 262-63 (3d Cir. 1975).

7. The APR reflects the relationship between the finance charge and the amount financed expressed as an annualized rate of interest. *See* Reg. Z, 12 C.F.R. § 226.5 (1978). The need for standardization was caused by widespread consumer confusion and misinformation and the disparities in methods of stating interest rates in consumer credit transactions, *e.g.*, add on, discount, monthly, and fees. *See* H.R. REP. NO. 1040, 90th Cong., 1st Sess. 8-9, 13 (1967); S. REP. NO. 720, 95th Cong., 2d Sess. 2 (1978); Note, *Truth in Lending: The Impossible Dream*, 22 CASE W. RES. L. REV. 89, 92-94 (1970).

8. *E.g.*, Reg. Z, 12 C.F.R. § 226.8(b)(2), (3), (c), (d) (1978). The courts have understood and faithfully enforced this notion of standardization. For example, in a credit sale, if there are no "other charges," the "unpaid balance" and "unpaid balance of cash price" will be the same; if there is no required deposit balance or prepaid

ture comparisons are quite simple. Often, the consumer need not even understand the term fully—the consumer may only need to know that higher is worse, or the term itself may have a pejorative connotation.⁹ There are also more generalized presentation requirements—“clearly, conspicuously, and in meaningful sequence”¹⁰—for displaying the data. Finally, the Act requires certain important information in the contract to be included on the Truth in Lending Statement. Cumulatively, these disclosures seek to enhance consumer understanding, simplify the consumer’s task in processing information, and dramatically reduce search costs. In increasing the consumer’s ability to process information and search for the best buy, the Act should also discourage creditors from shifting risks to the consumer; the consumer is particularly vulnerable to such risk shifting when the cost of understanding the risk is greater than the cost of the risk being shifted. Overall, the information should affect the decision to use credit and to use a particular source of credit.¹¹

This legislation assumes that consumers will behave differently in their credit transaction if they are given the best possible TIL disclosure statements. If the desired result has not been achieved, the argument goes, it is because an adequate set of disclosures has not yet been designed. But there is every indication

finance charge, the “unpaid balance” and “amount financed” will be the same. Courts have required disclosure of both terms and have explained that the Act was designed to facilitate shopping by standardizing concepts and terms; the consumer could not be expected to know that the amount financed in one transaction was the same as the unpaid balance in another if not specifically stated. *See Ives v. W.T. Grant Co.*, 522 F.2d 749, 756-59 (2d Cir. 1975); *Chapman v. Rhode Island Hosp. Trust Nat’l Bank*, 444 F. Supp. 439 (D.R.I. 1978); *Grey v. European Health Spas, Inc.*, 428 F. Supp. 841 (D. Conn. 1977); *Lewis v. Walker-Thomas Furniture Co.*, 416 F. Supp. 514, 517 (D.D.C. 1976). *See also Powers v. Sims & Levin Realtors*, 396 F. Supp. 12, 20 (E.D. Va. 1975), *rev’d on other grounds*, 542 F.2d 1216 (4th Cir. 1976) (creditor violated regulations because it failed to state required number of payments, even though simple addition by consumer would provide missing figure).

9. 15 U.S.C. §§ 1605-1606 (1976). This technique has been widely adopted in other contexts. For example, the Magnuson-Moss Warranty Act forces manufacturers to label less desirable warranties as “limited warranties,” 15 U.S.C. § 2303(a)(2) (1976); other legislation requires furs and wool products to be labeled accurately, 15 U.S.C. §§ 68-69 (1976); and the FDA has required labeling products as “orange drink” rather than “orange juice,” *see Collier & Merrill, “Like Mother Used to Make”: An Analysis of FDA Food Standards of Identity*, 74 COLUM. L. REV. 561 (1974); *cf. E. COX, R. FELLMETH & J. SCHULTZ, THE NADER REPORT ON THE FEDERAL TRADE COMMISSION* (1969) (discussing deceptive advertising practices).

10. Reg. Z, 12 C.F.R. § 226.6(a) (1978).

11. There is a basic question as to whether there should be any intervention at all in competitive markets. This in turn raises the questions of whether the consumer credit market is “competitive,” and whether one can speak of “competitive markets” on non-numerical contractual provisions. *See Schwartz & Wilde, Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis*, 127 U. PA. L. REV. — (1979).

that attaining this expressed purpose is a forlorn hope. Behavioral scientists, public opinion research, consumer research, and our own common sense tell us the same thing: consumer behavior in a particular transaction is almost certainly *not* going to be affected by a TIL disclosure statement, notwithstanding the quality of that statement.¹²

A. *Theoretical Analysis of the Impact of Transactional Disclosures*

1. The Timing Problem

There is a fundamental fallacy in the present approach to TIL disclosures. From the beginning, the disclosure requirements were premised on the notion that the TIL statement should include the particulars of the transaction that the consumer is considering. But the disclosures cannot be made until the consumer and the creditor have negotiated a basic agreement whose particulars can be ascertained. Thus, there must always be a fixing of prices and terms before the consumer receives the disclosure statement.

The Act resolves this dilemma by permitting creditors to make the disclosures as part of the contracting process, or in other words, after some sort of preliminary agreement has been reached that permits the preparation of the disclosure forms.¹³ Thus, the disclosures come at, or very shortly before, the consummation of a transaction to which the consumer is already verbally and psychologically committed.¹⁴ At this point, comparative shopping by the consumer is unlikely.¹⁵ Moreover, it is equally unlikely that at

12. We have avoided any analysis of the studies on the effect of TIL upon consumer behavior. They show uniformly that TIL has virtually no transactional impact. The studies are cited in Landers & Chandler, *The Truth in Lending Act and Variable-Rate Mortgages and Balloon Notes*, 1976 AM. B. FOUNDATION RESEARCH J. 35, 65 n.64. See also Brandt & Day, *Information Disclosure and Consumer Behavior: An Empirical Evaluation of Truth in Lending*, 7 U. MICH J.L. REF. 297, 308-15 (1974).

13. In a typical automobile credit sale, for example, the buyer and seller would have to reach a mutual agreement on at least the following details before a disclosure statement could be prepared: the basic cash price; incidental charges, as for title and taxes; the amount of any cash downpayment; the value of any trade-in; desired credit life, disability, and property damage insurance; the rate or dollar amount of finance charge; and the repayment schedule. This list does not include the many required disclosure items which are probably not negotiable, such as finance charge components, taxes, security interests, delinquency charges, and prepayment consequences.

14. In addition to overcoming the consumer's psychological commitment to the deal informally made, subsequent disclosures must cope with the strong possibility that the consumer will reject information that casts doubt on the wisdom of the "informal" decision already reached. Psychologists call this phenomenon "cognitive dissonance." See Whitford, *The Function of Disclosure Regulation in Consumer Transactions*, 1973 WIS. L. REV. 400, 426.

15. Some courts have made it easier for creditors to avoid any possible transactional use of disclosures by permitting preliminary application forms which contain

this point the consumer will opt to pay with cash. Thus, the present Act does not put usable credit information into the consumer's hands at a time when it will affect transactional behavior.¹⁶

2. Relationship of the Consumer's Creditworthiness and the Credit Decision

Many consumers who make credit purchases or take loans do so in circumstances where they must obtain credit. For example, the National Commission on Consumer Finance found that seventy-two percent of credit sales involved consumers who could not pay cash,¹⁷ and insofar as consumer loans are used to purchase property or services, the consumer's need is likely to be equally acute. The customer who shops for credit must therefore shop for two things: cost and eligibility. Such a consumer does not seek those terms that are best in the abstract, but rather, the best terms offered by a creditor who will approve his credit. It does the consumer no good to discover a creditor offering a nine percent rate if he does not qualify for that rate.¹⁸

In the chronology of most credit transactions, there is a preliminary fixing of terms (sometimes with some measure of disclosure), a determination of the consumer's creditworthiness, and then, full disclosure. The consumer's shopping energies may dissipate upon a favorable determination of creditworthiness;¹⁹ moreover, the creditor's continuing ability to revoke a favorable credit

substantial credit information but do not comply with TIL. *See Stanley v. R.S. Evans Motors, Inc.*, 394 F. Supp. 859 (M.D. Fla. 1975); *USLIFE Credit Corp.*, 5 CONS. CRED. GUIDE (CCH) ¶ 98,279 (ALJ 1977), *rev'd*, 5 CONS. CRED. GUIDE (CCH) ¶ 97,938 (FTC 1978).

The staff also seems determined to permit disclosures when they are least likely to be effective. One opinion permits creditors to delay giving the disclosures until after the consumer agrees to the purchase and actually takes the product home and keeps it awhile, so long as the purchase can be cancelled. FRB Off. Staff Int. No. FC-0130, [1974-1977 Transfer Binder] CONS. CRED. GUIDE (CCH) ¶ 31,731 (1977). If the value of pre-transaction disclosure is questionable because it is too late to affect transactional behavior, any benefit from disclosure after the consumer has taken the product home and used it is truly ephemeral.

16. Possible solutions to this problem are discussed at notes 79-83 & accompanying text *infra*.

17. NATIONAL COMM'N ON CONSUMER FINANCE, *CONSUMER CREDIT IN THE UNITED STATES* 182 (1972) [hereinafter cited as NAT'L COMM'N]; Jordan & Warren, *Disclosure of Finance Charges: A Rationale*, 64 MICH. L. REV. 1285, 1321 (1966). While some of these purchases could be deferred, many others could not. Also, in many cases the economic return to consumers from certain purchases is sufficiently great to make the purchase rational even if the APR is very high. NAT'L COMM'N, *supra*, at 183; accord, Kripke, *Consumer Credit Regulation: A Creditor-Oriented Viewpoint*, 68 COLUM. L. REV. 445, 469 (1968).

18. *See* Whitford, *supra* note 14, at 418 & n.75.

19. Studies of behavior indicate that when two parties each have a "yes or no" decision to make, an expressed affirmative decision by one participant tends to result in an affirmative decision by the other. *See generally* Asch, *Studies of Independence*

determination will likely act as a constraint upon overly aggressive bargaining by the purchaser. Finally, the consumer's own sense of proportion may attach more importance to whether he can get the amount of credit he wants, whether he can get it quickly, and whether the lender is otherwise accommodating.²⁰

3. Shopping Costs

In most transactions, shopping for credit after receipt of the TIL disclosures is simply irrational on a cost-benefit basis. To be sure, shopping or "search behavior" may take place at many stages of the transaction.²¹ There may be "diffused" shopping which does not focus on a specific creditor but seeks general information about prevailing rates and terms. This kind of information may be obtained by talking to friends and reading consumer publications or advertisements. In many cases, the information will be based on the consumer's own previous credit experiences.

The consumer also may attempt to obtain information from specific creditors, either in person or on the phone. Such attempts almost always focus on the acquisition of information relating to APR and monthly payments, partly because other TIL information is too complex for oral presentation and requires calculations that the creditor has not made. Further, one suspects that the consumer is most interested in APR and monthly payments. The Truth in Lending Act has influenced such forms of search with its requirement that creditors quote rates in APR terms. It is clear, however, that TIL was not intended principally to affect consumer behavior before the formal disclosures are furnished;²² a far different and simpler statute would have done that job.

The Act contemplates that shopping will occur *after* receipt

and Conformity: A Minority of One Against a Unanimous Majority, 70 PSYCH. MONOGRAPHS. No. 9, # 416 (1956).

20. See Kripke, *Gesture and Reality in Consumer Credit Reform*, 44 N.Y.U.L. REV. 1, 6 n.16 (1969); Note, *Consumer Legislation and the Poor*, 76 YALE L.J. 745, 750 (1967). A study of pre-TIL credit buyers found that, even when consumers were aware of differences in rates, they attached greater importance to other aspects of the credit arrangement. Among those other aspects were familiarity with the creditor, prior satisfactory dealings with the creditor, convenience, and concern about their eligibility for the lower rates. White & Munger, *Consumer Sensitivity to Interest Rates: An Empirical Study of New Car Buyers and Auto Loans*, 69 MICH. L. REV. 1207, 1222-28 (1971); see D. CAPLOVITZ, *THE POOR PAY MORE* 19, 53-54 (1963) (low-income consumers shop at stores which will extend credit); Whitford, *supra* note 14, at 422.

21. See Nelson, *Information and Consumer Behavior*, 78 J. POL. ECON. 311, 312-18 (1970) (discussing the economic parameters of search activity); Stigler, *The Economics of Information*, 69 J. POL. ECON. 213 (1961).

22. It may even be that creditors are now more reluctant to make advance oral disclosures. This was the finding of a student study titled "Shopping for Credit in New Orleans: An Exercise in Futility," reprinted in *Simplification Hearings*, *supra* note 2, at 333-41.

of the disclosure statement, and it is at this point that shopping is not cost effective. To decide whether to engage in such search activity, the consumer must determine whether the marginal cost of further search exceeds the marginal return. In somewhat simplified fashion, the consumer who receives a disclosure statement and is considering whether to shop for an additional source must consider the cost of shopping (C), the benefit (B) to be obtained by shopping, and the probability (P) that the benefit will be obtained. The value of shopping (V) can be evaluated by the following equation:²³

$$V = P(B) - C$$

Only if V is a positive figure is shopping rational.

In more concrete terms, assume the consumer purchases a color TV at a price of \$450 less a \$50 downpayment. The first dealer quotes a finance charge of \$40 (roughly eighteen percent) for payments over a one year period. We may assume that the lowest APR under present market conditions would be about nine percent, which would produce a finance charge of \$20. To obtain this maximum saving, the consumer must consider the costs of shopping: both expenses for gas and wear and tear on a car or the cost of public transportation, and the value of lost time ("opportunity costs"). If the consumer decides to shop at two of the twenty other dealers in the area, and the consumer estimates the cost of shopping at \$5 per dealer, the equation would be as follows:

$$V = .10(40-20) - \$10$$

$$V = -\$8$$

Here, shopping would be irrational for the consumer.

To be sure, the matter is a bit more complicated. The costs of shopping and the likelihood of finding the least expensive source vary directly: where there is more shopping, the costs of shopping rise as does the likelihood of finding the least expensive source. One must build into the probability figure the likelihood that the consumer will find the least expensive source on the first try rather than the last. In the above equation, the cost of shopping is not \$10 since there is a five percent (one in twenty) chance that the consumer will find the best price on the first try; thus, the shopping cost would be $\$5 + .95(\$5)$ or a total of \$9.75. But on the other hand, the notion that the consumer will stop searching when he finds the best price assumes that he will know that a given price is "lowest." If this assumption is not made, the theoretical cost of

23. This formula fails to distinguish between fixed sample and sequential search strategies. See Hirshleifer, *Where Are We in the Theory of Information?*, AM. ECON. REV., May 1973, at 31, 36; Rothchild, *Models of Market Organization with Imperfect Information: A Survey*, 81 J. POL. ECON. 1283, 1287-89 (1973). For our purposes, however, such a simplified formula should make the point adequately. See generally M. DEGROOT, *OPTIMAL STATISTICAL DECISIONS* (1970).

shopping increases because the consumer must shop further to "confirm" \$20 as the lowest price. Finally, it may be possible for the consumer to search by less expensive means such as advertisements or phone. Even this technique, however, is limited because the consumer must eventually receive the TIL statement to use the full panoply of disclosures effectively, and this almost always will require the costly process of visiting the creditor's premises.

The above model involves a limited search and makes some unduly favorable assumptions. For one, it assumes a relatively efficient market in which the cost of credit can be identified readily. Indeed, one of the expressed functions of TIL is to make the market efficient by forcing disclosure of the APR in standardized fashion. Unfortunately, this goal may be elusive. If the consumer is considering purchases of similar but not identical products from different dealers, he must first determine the "value" of each product. Small differences in value may seriously distort the stated APR. In addition, some merchants make the task more difficult by systematically burying finance charges in the cash price; in such cases, the disclosed APR is virtually worthless as a standard for measuring the cost of credit.²⁴ Moreover, we have assumed a search for only one term—APR. One of the purposes of TIL is to permit comparison of a large number of terms. As the consumer attempts to compare multiple terms, it becomes increasingly difficult to engage in pre-contract shopping to identify the probable best buy and to obtain adequate oral information in person or on the phone. In sum, the costs of search for the best buy based on all the information disclosed is likely to be substantially higher than the figures in the model because of the complexity of the information and the need for careful and individualized attention to the terms offered by different creditors.²⁵

The basic hypothesis of the above discussion is that cost-benefit considerations preclude search on the basis of the TIL disclosure statement in virtually all smaller transactions (*i.e.*, under

24. The existence of widespread burying of finance charges has been widely acknowledged. See Jordan & Warren, *supra* note 17, at 1301; Kripke, *supra* note 20, at 6-7; Landers, *Determining the Finance Charge Under the Truth in Lending Act*, 1977 AM. B. FOUNDATION RESEARCH J. 45, 135-45; Wallace, *The Uses of Usury: Low Rate Ceilings Reexamined*, 56 B.U.L. REV. 451, 482-87 (1976) (citing authorities). Unfortunately, there has been little scholarly thought given to assessing the scope and extent of burying and its impact on TIL.

25. This difficulty is somewhat analogous to the problem the consumer faces in searching for information about a product's characteristics and quality. See Hirshleifer, *supra* note 23, at 37-38; Holton, *Consumer Behavior, Market Imperfections, and Public Policy*, in INDUSTRIAL ORGANIZATION AND ECONOMIC DEVELOPMENT 102 (Markham & Papanek eds. 1973); Nelson, note 21 *supra*. This Article will later show that TIL does not improve the consumer's ability to search for the best "terms." See notes 54-72 & accompanying text *infra*.

\$2,000) and in most mid-range transactions (*i.e.*, \$2,000—\$10,000) as well. In the smaller transactions, creditors' overhead costs and the price of money tend to minimize differences in rates and other terms.²⁶ At the same time, when small amounts of money are involved, the dollar differences of quite substantial variations in APRs tend to yield insignificant total dollar differences, as in the example presented earlier.

Even in the mid-range transactions, rates and terms may be similar within a given type of creditor (*e.g.*, banks or retailers), thus making search not cost-effective.²⁷ There is ample evidence that consumers have adequate knowledge of the relative costs of different types of creditors (*i.e.*, that banks charge less than finance companies),²⁸ and if they do not, this information usually can be obtained relatively inexpensively from friends, by phone, or through advertisements. Although TIL disclosure statements, with their intricate detail, are likely to be effective in identifying the most favorable transaction among creditors of the same type who offer prices and other terms that are within narrow ranges, it is in this case that the marginal cost of search will usually exceed the marginal return from further search. Indeed, some econometric studies suggest that the consumer usually will be bet-

26. In 1971, the average direct cost per personal loan at New York banks making 20,000 loans was \$48.43. D. ROGERS, CONSUMER BANKING IN NEW YORK 117 (1974). While costs will vary for different types of creditors, such direct costs are likely to be a substantial component of the finance charge for many types of credit transactions. See generally NAT'L COMM'N, *supra* note 17, at 139-47.

27. For example, a consumer might well discover marked differences in the automobile credit rates offered by credit unions, commercial banks, and consumer finance companies. But if that consumer belonged to no credit union, and had to rule out bank loans because of downpayment requirements, he would probably find no appreciable differences among rates offered by competing finance companies. In many markets, average rates of creditors within a given category are fairly similar. For example, a survey of five leading banks in Boston revealed APRs ranging from 9.76% to 11.08%. The differences among leading banks in such cities as Dallas, Seattle, San Francisco, Miami, and Washington, D.C. were less. Consumers' Union, *How to Save on a Car Loan*, 43 CONSUMER REP. 202 (1978). Assuming that \$5,000 is financed for 48 months, the dollar difference is about \$140. Note, too, that both the amount financed and length of time substantially exceed most typical consumer credit transactions other than home mortgages.

It may be argued that these are "averages" and the consumer can bargain to get better rates. But this cuts both ways, for the process of individualized shopping and "haggling" involves substantial transaction costs including in-person shopping, follow-up negotiations, and the inability to compare by way of advertisements or generalized surveys.

28. See F. JUSTER & R. SHAY, CONSUMER SENSITIVITY TO FINANCE RATES: AN EMPIRICAL AND ANALYTICAL INVESTIGATION 59-61 (Nat'l Bureau of Econ. Res., Occasional Paper No. 88, 1964); Brandt & Day, *supra* note 12, at 322-26; Day & Brandt, *A Study of Consumer Decisions: Implications for Present and Prospective Legislation*, in 1 NATIONAL COMM'N ON CONSUMER FINANCE TECHNICAL STUDIES 29-30, 95, 112-16 (1972); Kripke, *supra* note 20, at 4; Kripke, *supra* note 17, at 460-64, 462 n.42, 466 & n.51.

ter off by accepting the first offer in cases where search costs are high, as they are when the search takes the form of comparing disclosure statements, and distribution of prices is narrow.²⁹

In sum, the consumer who is inclined to search will probably adopt the least costly expedient: searching by advertisements or telephone communications. Such pre-contract and pre-disclosure search permits broad coverage of creditors, frees the consumer from any psychological "confrontation" with a given creditor, and may prove to be most cost effective because, after this early search, only in the rare case will the marginal return from search *after* receipt of the TIL statement exceed the costs of search.³⁰ Although TIL could be designed to reduce the marginal cost of further search (*e.g.*, by requiring creditors to send a fully completed TIL statement upon request to the consumer's house,³¹ an idea not being proposed), the present Act is ill-suited to serve such an objective.³²

B. *Infirmities in Truth in Lending*

The consumer who attempts to make some use of TIL in transactional behavior faces a difficult chore. In many instances, the statement is virtually unreadable and filled with numerous categories of information. To some extent, this situation reinforces the cost-benefit problem of increasing search costs well above their theoretical minimum. Moreover, the consumer faces a special problem in evaluating the terms of the transaction: because the basic principles of TIL have not been applied to "term" disclosure, it is difficult to understand and evaluate the data. Finally, the consumer faces an equally serious problem because in-

29. See, *e.g.*, Tesler, *Searching for the Lowest Price*, AM. ECON. REV., May 1973, at 40.

30. In non-credit transactions, consumers shop more intensively for higher-priced products than lower-priced products. See Bucklin, *Testing Propensities to Shop*, J. MKTG., Jan. 1966, at 22; Newman & Staelin, *Prepurchase Information Seeking for New Cars and Major Household Appliances*, 9 J. MKTG. RESEARCH 249, 251-52 (1972); Udell, *Prepurchase Behavior of Buyers of Small Electrical Appliances*, J. MKTG., October 1966, at 50.

31. For example, creditors could be required to send a fully completed disclosure form to consumers upon request. The costs of implementation would probably be far out of proportion to the benefits, and such an idea has not been suggested seriously. We only make the point that search costs can be reduced if that is the paramount objective.

32. Some economists make an even more basic criticism. They have suggested that ordinary market mechanisms would probably provide information that was desired by a significant number of consumers. By definition, then, if disclosure must be compelled by the state, it is of relatively little importance and/or will influence a small number of purchases. See R. POSNER, *ECONOMIC ANALYSIS OF LAW* §§ 4.7, 13.3 (2d ed. 1977); Whitford, *supra* note 14, at 428. Any evaluation of this point is beyond the scope of our discussion.

formation pertinent to the decision-making process is not included.³³

1. Cognitive Overload

The consumer's behavior in the transaction will not be affected if the credit disclosures are so numerous and, in conjunction with other contract provisions, so formidable as to create a "cognitive overload." That is, the consumer becomes overwhelmed by the aggregate mass of words and figures and reacts by ignoring the disclosures entirely.

A typical retail installment sale contract may be printed on both sides of a legal-sized sheet of paper containing the pertinent credit information, descriptions of the item purchased, warranty and servicing information, credit and property insurance provisions, and much more. The credit disclosures may be interspersed among the other items on the face of the form, and some disclosures may refer to other disclosures in other portions of the form. The completed document is given to the consumer at a time and under circumstances that are not conducive to careful reading and study. Many consumers are simply unable to sort out, process, and evaluate all of the information presented. The unconscious response may be to ignore everything—except, perhaps, a quick confirmation that this is in fact the "right" contract.

There is, admittedly, no "hard" evidence that this is occurring in the case of Truth in Lending Statements. But, in a recent and provocative study, Professor Jeffrey Davis has shown that consumer understanding may be increased by dropping some disclosures and simplifying others, thus suggesting that some type of information excesses may inhere in the present requirements.³⁴ This phenomenon of cognitive overload also has been postulated in other disclosure contexts, and there is no reason to doubt that something of the sort occurs with respect to credit disclosures as well. Available studies suggest that typical consumers can manage six, seven, or maybe eight "bits" of information, but that more

33. A related problem is that, in some cases, the disclosed information is simply inaccurate as a basis for consumer behavior. For example, the inclusion of "optional" insurance in the amount financed tends to distort the APR vis-à-vis a comparable transaction without insurance. Also, the consumer's inability to obtain a high rate of return on money "saved" by paying a lower APR means he may be much better off taking a higher APR for a shorter period of time. Inclusion of some front-end costs in the amount financed (filing fees and some real estate closing costs) tends to distort both the APR and finance charge. The problem of partial burying of the finance charge is unresolved. See Landers, *supra* note 24, at 81, 132-34, 135-45 & n.219.

34. Davis, *Protecting Consumers from Overdisclosure and Gobbledygook: An Empirical Look at the Simplification of Consumer-Credit Contracts*, 63 VA. L. REV. 841 (1977).

than eight likely will produce overload results.³⁵ Obviously, the present Act requires disclosure of substantially more than this quantum level. Indeed, the nature of the information involved in a credit context, and the relative stressfulness of the situation, suggest that cognitive overload is more likely to occur in the case of credit disclosures than in those cases where it has been identified already. Clearly, a consumer will not use disclosed information for shopping purposes if he has not focused on it.³⁶

Of course, some consumers can process more complex information.³⁷ There is no "correct" way to make this sort of policy judgment. However, if the purpose of the Act is to influence a substantial portion of the credit-consuming public, attention must be paid to the phenomenon of cognitive overload for the mass of consumers.

There are several theoretical ways to reduce information overload, but each presents its own difficulties and may frustrate other desired functions of the disclosure scheme. The most obvious response is to reduce the number of items disclosed to within the manageable range of six or eight that is suggested by the empirical data. To do this, however, means deciding that some of the information now disclosed is expendable. Which items should go? Should we omit itemizations, for instance, of the finance charge or of the amount financed?³⁸ Should we drop disclosures of terms relating to default or security? Indeed, which of the current disclosures are the most important? Professor Davis supports deletion of the insurance disclosure while consumer advocates regard these disclosures as of key importance.³⁹ It is impossible to as-

35. See Miller, *The Magic Number Seven Plus or Minus Two: Some Limits on our Capacity for Processing Information*, 63 PSYCH. REV. 81 (1956). See generally Bettman, *Consumer Information Acquisition and Search Strategies*, in *THE EFFECT OF INFORMATION ON MARKET BEHAVIOR* (A. Mitchell ed. 1978); see also Jacoby, Speller & Kohn, *Brand Choice Behavior as a Function of Information Load: Replication and Extension*, 1 J. CONSUMER RESEARCH 33 (1974).

36. The very notion of "information overload" has hardly won wholesale acceptance. Compare Russo, *More Information Is Better: A Reevaluation of Jacoby, Speller and Kohn*, J. CONSUMER RESEARCH, Dec. 1974, at 68, and Summers, *Less Information Is Better?*, 11 J. MKTG. RESEARCH 467 (1974), with Jacoby, *Information Load and Decision Quality: Some Contested Issues*, 14 J. MKTG. RESEARCH 569 (1977), and Jacoby, Szybillo & Busato-Schach, *Information Acquisition Behavior in Brand Choice Situations*, 3 J. CONSUMER RESEARCH 209 (1977), and Scammon, "Information Load" and Consumers, 4 J. CONSUMER RESEARCH 148 (1977).

37. Some studies suggest that "smarter" consumers cannot process more items of information; they can, however, process more complex bits of information. Davis, *supra* note 34, at 848-49.

38. This is the approach of the Senate bill. S. 2802, 95th Cong., 2d Sess. § 14(a) (1978).

39. Davis, *supra* note 34, at 862 & n.71. Indeed, the FRB's own simplification proposal not only retained the present insurance provisions, but added a right of rescission which required further disclosures. S. 1846, 95th Cong., 1st Sess. § 5 (1977).

sume a consensus on this question, especially if we wish to retain some of the other functions for credit disclosure described below.

Another possible response to information overload would be to separate from the underlying contract those credit disclosures the consumer should heed for shopping purposes. This might be accomplished by requiring the key disclosures on a separate sheet of paper—a kind of credit “price tag.” Or perhaps the critical disclosures might remain on the contract document, but in a clearly conspicuous, segregated position—perhaps boxed at the top of the front page.⁴⁰ Requiring disclosure on a separate sheet, though, would add another piece of paper in all transactions, with attending costs and clutter, and would create new problems in policing. A boxed separate disclosure statement on the original contract, on the other hand, would still compete for attention with other contract provisions and would require duplicative statements of the important credit terms—once in the disclosure box and again as part of the contract.

In short, any attack on information overload involves substantial trade-offs. Further, much of the complexity of present consumer credit agreements flows from provisions required or permitted by state law, on which federal disclosure requirements are superimposed. Without substantial preemption of state laws, reducing the number of disclosures to produce a disclosure format that would capture consumer attention is probably an impossibility.⁴¹ Even then debate would continue over which disclosures are to be retained as essential “bits.”

In addition, it is suggested here that all the discussions of information overload and the imperfections of present methods of delivering information are somewhat beside the point. That is, proponents assume, as stated at the outset, that TIL will affect transactional behavior if the statement is improved.⁴² And, as “proof” that TIL is effective, they cite increases in consumer awareness.⁴³ The fallacy is to equate knowledge and understand-

40. The Senate bill temporizes as to the exact format, requiring only that the disclosures “shall be conspicuously segregated from all other terms, data, or information provided in connection with a transaction, including any computations or itemization.” S. 2802, 95th Cong., 2d Sess. § 14(b) (1978).

41. *Cf.* *Mason v. General Fin. Corp.*, 542 F.2d 1226 (4th Cir. 1976) (mixing of federal and state required disclosures violates intent of the Truth in Lending Act to create a uniform system of credit terminology across states and lending institutions). Even preemption may not do the job, since an increasing portion of the clutter results from various federal laws. For example, Professor Davis recommends deleting the FTC “holder” notice. Davis, *supra* note 34, at 361-62. We are not particularly sanguine about the prospects of realizing agreement of federal regulators in eliminating a disclosure such as the FTC holder notice which was considered a “major” step in assuring consumer protection.

42. *See* note 6 & accompanying text *supra*.

43. Opponents of “simplification” repeatedly rely on increased awareness of

ing with transactional behavior. Undoubtedly there is a relationship: transactional behavior cannot be affected if consumers do not understand their credit transactions. But the converse is not necessarily true; simply because consumers have greater understanding does not mean that their immediate transactional behavior will be affected. Implicit in our earlier discussion is an acceptance of the conclusion that transactional behavior is not likely to be affected by TIL disclosures.⁴⁴ And it has already been noted that there is no hard evidence that suggests otherwise.⁴⁵

2. Dysfunction in the Delivery of Information

Common sense suggests that an individual's ability to comprehend information is related to the conditions under which the information is imparted and must be learned. Most TIL disclosures are given under circumstances that are extremely stressful and not suited to careful deliberation and analysis. Usually, at least in closed end transactions, the information is given by a person sitting or standing in close proximity to the consumer. The physical conditions are likely to be at least mildly intimidating—a "sterile" bank, a small room, other persons milling around. The consumer may be distracted by children, noise, interruptions, or unrelated conversation; and there may be subtle references to the need for speed.⁴⁶ The person with whom the consumer "negotiates" the credit arrangement may be an authority figure (the "credit man") who is separated from the sales activities and is somewhat forbidding.⁴⁷ The consumer may lack a desk and paper and pencil to make any calculations. This is not to say that consumers will not do their best, but it does suggest that whatever

APRs as a reason for not changing TIL. See, e.g., *The Attack on Truth in Lending*, 42 CONSUMER REP. 6-08-10 (1977). The most this suggests is that present requirements for disclosing the APR not be changed. This is a straw man: so far as the authors are aware, there has been no serious suggestion for such a change.

44. See notes 13-32 & accompanying text *supra*.

45. See note 12 & accompanying text *supra*.

46. Numerous studies show that the relative stressfulness of a situation affects the consumer's ability to process information. See, e.g., Wright, *The Harassed Decision Maker: Time Pressures, Distractions and the Use of Evidence*, 59 J. APPLIED PSYCH. 555 (1974) (subjects buying cars under time pressures or distractions consider fewer attributes and weighted negative information more heavily).

One study of car buyers showed that 40% of new car buyers received the disclosures within 10 minutes of signing the contract and another 27% within one hour of signing. Comment, *The Impact of Truth in Lending on Automobile Financing—An Empirical Study*, 4 U.C.D.L. REV. 179, 200 (1971). See generally Day & Brandt, *Consumer Research and the Evaluation of Information Disclosure Requirements: The Case of Truth in Lending*, J. CONSUMER RESEARCH, June 1974, at 21.

47. Consumers may respond readily to the subtle command of authority, especially if they have the illusion of free choice. See Milgram, *Some Conditions of Obedience and Disobedience to Authority*, 18 HUMAN REL. 57, 57-67 (1965). See also P. ZIMBARDO, *THE COGNITIVE CONTROL OF MOTIVATION* (1969).

optimum value can be obtained from TIL transactional disclosures is not likely to be attained, indeed, even approached, under such conditions.⁴⁸

Many consumer credit transactions arise in connection with the purchase of a product. The consumer may suffer from what might be called a "decisional overload." That is, the credit terms are likely to have much less significance in the consumer's eye than the color, model, brand name, accessories, and cash price of the item purchased. The consumer is likely to give much more thought to, and be much more excited about, the overall purchase than its credit aspect which, after all, will be only a fraction of the total investment. Fully aware of the credit cost implications, the consumer may give them no more significance than the cost of the air conditioning in the car he is purchasing; "credit" is something he must tolerate to get behind the wheel. Indeed, from the consumer's point of view, the decision to get air conditioning has greater economic significance than the credit terms since the cost of air conditioning almost always exceeds any saving which might be obtained by shopping for credit.⁴⁹

Consumer surveys demonstrate that consumers making a purchase on credit consider product-related decisions to be more important than credit-related decisions.⁵⁰ Moreover, it may be that the typical consumer is simply unable to evaluate multiple components of the transaction and weigh them as part of an overall package.⁵¹ Instead, the consumer may just shop for price and significant options and defer to the credit-seller on other matters.

The insurance provisions of TIL furnish a good example of this effect. Under TIL, credit life and credit accident and health insurance are not included in the finance charge unless the purchase is voluntary and the consumer specifically requests the

48. One study of persons who financed the purchase of automobiles showed that approximately 75% spent less than 30 minutes in gathering and evaluating information relating to the financing arrangements. Friedman, *Using Simulation Techniques to Predict the Behavioral Effects of New Laws: The Case of Truth-in-Lending Legislation and the Consumer*, 54 J. APPLIED PSYCH. 297, 298 (1970).

49. The cost of air conditioning on a 1978 Buick Century (a medium priced car) is about \$550. If the consumer finances \$5,000 for 48 months at 10%, the finance charge is \$1087; at 13%, it is \$1439. The potential saving is thus \$352. As noted earlier, the amount "saved" is not likely to be as high as 3%. See note 27 *supra*.

50. NAT'L COMM'N, *supra* note 17, at 181-82; Brandt & Day, *supra* note 12, at 317-19; cf. Leff, *Contract as Thing*, 19 AM. U.L. REV. 131, 145-47 (1970) (describing a fictional car purchase).

51. There is considerable data which suggests that consumers consider a small number of features in making purchase decisions, even if information on more features is readily available. See Hansen, *Consumer Choice Behavior: An Experimental Approach*, 6 J. MKTG. RESEARCH 436 (1969); Jacoby, Szybillo, & Busato-Schach, note 36 *supra*; Katona & Mueller, *A Study of Purchase Decisions*, in 1 CONSUMER BEHAVIOR 30 (L. Clark ed. 1954).

insurance after disclosure of the price and voluntary nature of the purchase.⁵² Here, then, the Act goes beyond passive receipt of information, to require affirmative action by the consumer. Moreover, the unspoken premise of the TIL approach, indeed the essence of the consumer advocates' position on this issue, is that credit insurance is overpriced and ought not to be purchased in most transactions. In fact, the TIL insurance scheme has proven almost totally ineffective in insurance purchase decisions, and regulatory bodies continue their concern over insurance penetration rates of between ninety and one hundred percent.⁵³ The failure of TIL to affect this problem should give some pause for thought as we speak about influencing consumer decisions on terms of the contract that have less economic significance than insurance.

3. The "Term Disclosure" Dilemma

Term disclosure generally refers to those contractual and non-numerical items that are required to be disclosed by the Act. In particular, the Act requires disclosures of prepayment penalties and rebates; default, delinquency and late payment charges; security interests; and, in open-end accounts, the method of determining the balance to which finance charges will be imposed.⁵⁴

The first question to be addressed is why disclosure of term items is required at all. If we assume, contrary to what has been said above, that some disclosures may affect transactional behavior, the question remains whether *these* disclosures will affect transactional behavior. The answer appears to be negative: consumers will likely not understand the issues and cost dimensions of term disclosure, and even if they did, the economic consequences would be de minimis so that change in transactional behavior would not be rational on a cost-benefit basis.

It has already been noted that the basic purpose of Truth in Lending is to standardize the concepts involved in consumer credit decisions and to use standardized terminology as an aid to decision making.⁵⁵ This approach theoretically lowers the cost to the consumer of acquiring information and should prevent creditors from shifting costs to consumers by virtue of consumer apathy

52. 15 U.S.C. § 1605(b) (1976); Reg. Z, 12 C.F.R. § 226.4(a)(5) (1978).

53. The Federal Reserve Board cited this data in suggesting that consumers be given a right to cancel such insurance for a time after the credit transactions. BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, 62D ANNUAL REPORT 1975, at 277-78 (1976). The Federal Trade Commission, on the other hand, used the same experience to support its contention that credit insurance premiums should be included in the finance charge in all cases. See *Simplification Hearings*, *supra* note 2, at 136 (statement of Lewis H. Goldfarb, Acting Assistant Director for Special Statutes, Federal Trade Commission).

54. See Reg. Z, 12 C.F.R. §§ 226.7(a)(2), (b)(1)(viii), .8(b)(4)-(7) (1978).

55. See notes 6-9 & accompanying text *supra*.

or inability to evaluate the trade-offs involved. Thus, consumers can compare the "finance charge" of one transaction with another, with certainty that they are comparing the same thing. It must be assumed, however, that consumers will know that finance charge is synonymous with cost of credit—otherwise, the comparison itself will not aid in the decision-making process. The strength of this approach is that the key comparison is reduced to a numerical amount—the consumer simply must know that highest is worst.

The very premises of cost disclosure are inapplicable to TIL requirements for term disclosures. There is, for example, no standardization of terminology: a security interest may be called a "consensual security interest under the Uniform Commercial Code," a "mechanic's lien," a "mortgage" or some other term. Whether there are substantive differences in these terms from the consumer's point of view is not clear. And if there are differences, whether they are relevant to the consumer's decision is also unclear. A second example of the inapplicability of the premises of cost disclosure to term disclosure is the unfeasibility of numerical comparisons. For example, consider two methods that may be utilized to compute and disclose rebates on prepayments: rebate by the rule of 78s⁵⁶ or rebate by the actuarial method less an acquisition charge of \$15. The consumer cannot possibly make a rational decision on the preferability of one of these methods; indeed, even the expert probably cannot, because the answer will depend on the amount of the loan and the timing of the prepayment.⁵⁷ Therefore, the basic premises of cost disclosure as circumscribed in TIL law—standardization of terminology and numerical comparisons for simplified credit shopping—have not been employed in the area of term disclosure.

56. See generally Landers, *Truth in Lending: Closed End Credit*, PRAC. LAW., June 1978, at 36; note 57 & accompanying text *infra*.

57. The Board has essentially conceded that this disclosure is meaningless; the Board's justification is that the explanation would be incomprehensible anyway and would further complicate the disclosure statement. See *Bone v. Hibernia Bank*, 493 F.2d 135, 140 (9th Cir. 1974) (TIL does not require an explanation of the rebate method); Wallace, *supra* note 24, at 467; cf. Hunt, *The Rule of 78: Hidden Penalty for Prepayment in Consumer Credit Transactions*, 55 B.U.L. REV. 331, 349-50 (1975) (Federal Reserve Board position is that prepayment rebate disclosure requirement is satisfied merely by reference to the name of the method used to compute the rebate).

One of the somewhat ironic twists on this whole rebate issue came in the hearings on Regulation Z when Congresswoman Sullivan told Governor Robertson of the Board that she did not understand what the rule of 78s was. Governor Robertson stated that he hoped this would be explained in TIL disclosure statements even though the Board's model forms—which were part of the hearings record—contained no such explanation. *Hearings on Consumer Credit Regulations Before the Subcomm. on Consumer Affairs of the House Banking and Currency Comm.*, 91st Cong., 1st Sess. 404 (1969). It is unlikely that counsel for plaintiff in *Bone* knew of this exchange, which was buried in the thousands of pages of hearings on TIL.

Even assuming that the consumer could understand the "term" issues in a manner that would permit effective decision making, it is doubtful that shopping would be rational in the sense of producing benefits. Most of the term disclosures relate to two circumstances—early payment or default. Aside from small loans, default is an infrequent occurrence, and thus the economic consequences are not relevant to the vast majority of consumers. Thus, even assuming wide differences in default charges, the consumer must weight these extensive differences in light of the small probability of default. While it may be argued that consumers know that they might default and therefore might consider the charge, it is more likely that a consumer will not consider the possible charges for default at all because he does not expect to default.⁵⁸ In any event, a rational consumer will have to consider additional costs of a given default package multiplied by the likelihood of default, with the total discounted by a consumer's rate of return reflecting the fact that any default will be in the future, and balance these against the costs of shopping and other cost items. For example, if the difference in the "value" of the default package offered by two creditors is \$200—probably a high figure—and the chance of using it is seven percent, also high⁵⁹ (and eliminating any figure for the discount entirely), the economic import is only \$14—not an amount for which it is rational to do extensive shopping. Also, it must be remembered that the search costs are high because of the lack of standardization and the difficulty of evaluating the cost factors. Finally, the TIL Act provides no helpful guide to evaluating the relative benefits and detriments of different cost and non-cost items, for example, how much higher a finance charge the consumer should pay for "favorable" default provisions. The figures may be staggering: a recent study suggests that the difference in default packages on a \$1300 loan must be \$850 to make it rational for the consumer to pay an addition of

58. Abundant evidence suggests that many defaults occur because of events which are essentially unpredictable such as loss of job, reduced wages (e.g., no overtime), health problems, marital difficulties, or other calamities. See D. CAPLOVITZ, *CONSUMERS IN TROUBLE: A STUDY OF DEBTORS IN DEFAULT* 77, 167-74 (1974); Greer, *Creditors, Remedies and Contract Provisions: An Economic and Legal Analysis of Consumer Credit Collection*, in 1 NATIONAL COMM'N ON CONSUMER FINANCE TECHNICAL STUDIES 7-9 (1972); cf. D. STANLEY & M. GIRTH, *BANKRUPTCY: PROBLEM, PROCESS, REFORM* 47 (1971) (consumer who does not foresee his predicament is unlikely to plan for it when engaging in a credit transaction).

59. See R. JOHNSON, *COST/BENEFIT ANALYSIS OF CREDITORS REMEDIES* 16-17 (1978) (prepared for FTC in connection with proposed Trade Regulation Rule). Actually, this seven percent figure is unduly high since it includes many persons whose default was simply one or two late payments, which would give rise only to a late charge. The number of consumers whose default was sufficiently serious to raise the question of valuing default remedies is probably closer to two or three percent.

one percent to the APR.⁶⁰ Present-day TIL statements give the consumer no help in making this kind of evaluation.

Borrowers from small loan companies are said to have a much higher than average default rate, but it is precisely for these borrowers that the default disclosures are not likely to influence transactional behavior. First, many of these borrowers are rationed in that they cannot qualify for all the credit they want. These consumers will take credit at any price, and *a fortiori*, on any terms.⁶¹ Moreover, small loans tend to involve lesser amounts than other credit transactions, with the result that the dollar consequences of different default provisions will not be as great. Again, shopping becomes irrational on a cost-benefit basis. Finally, these consumers tend to be the least well-educated, thus suggesting even higher search costs to evaluate different default provisions and determine which is best.⁶²

Many of the same factors apply in the case of prepayment provisions. Most consumers do not expect to prepay, dollar differences are not great, information is not presented meaningfully, and search costs are high.

The net result is that disclosure of default and prepayment terms is unlikely to influence the consumer's decision in the particular transaction. It is, of course, possible to argue that consumers "ought" to get disclosure because the terms are "important." This Article will examine other justifications for disclosure that will take account of these arguments. But there is no serious basis to assume that consumers will consider the term disclosures in making immediate credit decisions.⁶³

4. The Omissions from Term Disclosure

Even assuming that the consumer does take the time to read and evaluate the "term" disclosures and has sufficient knowledge and understanding to determine the various "trade-offs" involved, TIL does not provide him with the information necessary for a rational decision. Put another way, TIL leaves out information which is of greater importance than information which is put in, with the result that a decision based on TIL information may be irrational. Some of this information is contained in the underlying contract and can be included if the consumer takes the additional time to review it; still other information requires an

60. R. JOHNSON, *supra* note 59, at 23.

61. See NAT'L COMM'N, *supra* note 17, at 179; Johnson, *The Uniform Consumer Credit Code and the Credit Problems of Low-Income Consumers*, 37 GEO. WASH. L. REV. 1117, 1119 (1969); Kripke, *supra* note 20, at 6; Kripke, *supra* note 17, at 461 n.40.

62. This increase may be balanced by the fact that the value of the time lost by searching (the opportunity cost) is likely to be less for such consumers.

63. See note 78 *infra*.

understanding of the Uniform Commercial Code, other consumer credit legislation, or judicially developed common law.

What must be disclosed and what need not be disclosed with respect to default best illustrates this problem. The present Act requires disclosure of a late charge, additional charges that may be imposed unilaterally by the creditor upon default, and in some jurisdictions, the right of a creditor to accelerate the maturity of the obligation.⁶⁴ Also, the creditor must disclose any security interest it has. But default has far more serious consequences from the consumer's perspective. The most important are: it sets into motion a process of acceleration, which is sometimes disclosed;⁶⁵ repossession, which is never disclosed; the imposition of additional charges for the repossession and collection, which is rarely stated in dollar terms; sale of the collateral, which is never disclosed; and the consumer's possible liability for a deficiency, which also is never disclosed.⁶⁶ In addition, there is no disclosure that if the consumer elects to refinance the obligation—an option often offered—there may be substantial front-end charges.

In connection with default, the most important information may not be "legal" in nature at all. That is, although a missed payment may trigger default, acceleration, and repossession, many creditors often defer invoking these remedies while the consumer attempts to cure.⁶⁷ One study has found that there were

64. The question whether an acceleration clause must be disclosed as a default charge may represent the nadir of Truth in Lending analysis. There is at least a three-way split among the federal circuit courts on the issue, with some district courts taking still a fourth view. *See* *St. Germain v. Bank of Hawaii*, 573 F.2d 572 (9th Cir. 1977) (disclose whether rebate upon acceleration and method of making rebate); *Begay v. Ziems Motor Co.*, 550 F.2d 1244 (10th Cir. 1977) (no disclosure regardless of rebate); *Johnson v. McCrackin-Sturman Ford, Inc.*, 527 F.2d 257 (3d Cir. 1975) (no disclosure if rebate; unearned interest not rebated); *Garza v. Chicago Health Clubs, Inc.*, 347 F. Supp. 955 (N.D. Ill. 1972) (disclosure always required). The Federal Reserve Board staff has taken yet a fifth view. FRB Off. Staff Int. No. FC-0054, 5 CONS. CRED. GUIDE (CCH) ¶ 31,522 (1977) (apparently, disclose if rebate upon acceleration is different from rebate upon prepayment). *See* *McDaniel v. Fulton Nat'l Bank*, 571 F.2d 948 (5th Cir. 1978) (en banc) (following FRB approach as a "practical one in a debatable area . . . where uniformity is desirable").

65. *See* *Begay v. Ziems Motor Co.*, 550 F.2d 1244 (10th Cir. 1977). Judge Holloway dissented from the court's holding that an acceleration clause was not a default charge because: "If the lighter burden of no more than \$5.00 for a late payment is a required disclosure where acceleration of the whole debt is not demanded, why should not the heavier burden of all unearned finance charges being collectable as a part of the accelerated debt be disclosed?" *Id.* at 1250; *accord*, *Chapman v. Rhode Island Hosp. Trust Bank*, 444 F. Supp. 439 (D.R.I. 1978).

66. *Cf.* F.R.B. Off. Staff. Int. No. FC-0117, [1974-1977 Transfer Binder] CONS. CRED. GUIDE [CCH] ¶ 31,703 (1977) (consumers do not have to be told that they are not subject to a deficiency judgment if the creditor repossesses the collateral at a time when the loan balance is under \$1250).

67. Creditors often provide a phone number, or "hot-line," for consumers to call if they are unable to meet payments. For example, the widely publicized "simple

more than thirty formal or informal contacts before creditors invoked repossession; but there probably are substantial differences among creditors.⁶⁸ Thus, an informed consumer would want to obtain some idea of the creditor's actual collection policy: is it easygoing, firm but fair, or tough?

Of perhaps equally great significance are the panoply of collection weapons that do not involve the collateral but would likely impact the consumer's decision. Such matters as the degree of offensiveness of the creditor's collection efforts, his ability to put pressure on the debtor through significant persons such as employers or neighbors or to obtain and enforce a judgment by execution or garnishment, and the creditor's willingness to report defaults to a credit bureau, are prime examples. Indeed, the possibility of injury to the physical or emotional well-being of the consumer, and the possibility that the collection effort may produce outrage and frustration, are probably of greater concern to the consumer than the pure "pecuniary" considerations.⁶⁹ It is impossible to value such costs.⁷⁰ In addition, many states have exemption laws that prevent creditors from seizing specified property to satisfy debts, and the newly enacted Bankruptcy Reform Act contains a lengthy list of property that will be exempt in the event of a bankruptcy proceeding.⁷¹ However, the consumer who engages in a credit transaction often is not told that the creation of a security interest in otherwise exempt property will defeat the exemption in a state collection proceeding, nor can we expect him to be told of the special rules in bankruptcy concerning security interests in exempt property.⁷² In the Fifth Circuit, creditors must now disclose

English" form of Citibank states: "Hotline: If something should happen and you cannot pay on time, please call us immediately at [number]."

68. See Johnson, *Denial of Self-Help Repossession: An Economic Analysis*, 47 S. CAL. L. REV. 82, 94 (1973). Professor Johnson's data has been questioned, but even if substantially overstated, it makes the basic point that collection efforts are not limited to pure "legal" issues. See also Dauer & Gilhool, *The Economics of Constitutionalized Repossession: A Critique for Professor Johnson and a Partial Reply*, 47 S. CAL. L. REV. 116, 139 n.70 (1973).

69. Recent consumer literature emphasizes the significance of these psychic costs. See Wallace, *supra* note 24, at 459 & nn.34 & 35, 473, 492 & n.172 (citing authorities); cf. Wallace, *The Logic of Consumer Credit Reform*, 82 YALE L.J. 461, 471-72 (1973) (default leads to low self-image resulting in substantial shame and embarrassment).

70. See Leff, *Injury, Ignorance and Spite—The Dynamics of Coercive Collection*, 80 YALE L.J. 1 (1970) (enumeration of harms inflictible upon the debtor by the creditor in a theoretical game context).

71. Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, tit. I, 92 Stat. 2549, 11 U.S.C.A. § 522 (West Pamph. 1979).

72. Under the Bankruptcy Reform Act of 1978, 11 U.S.C.A. §§ 101-1331 (West Pamph. 1979), non-purchase money security interests in certain exempt consumer goods or tools of the debtor's trade will not be enforceable against the debtor in bankruptcy. *Id.* § 522(f). On the other hand, a purchase money security interest in such items will be effective in bankruptcy. Although these "fine points" of exemption law

a waiver of exemptions as a security interest;⁷³ there is no explanation of what an "exemption" is or what it means to lose this benefit.

The point to be made is not that the term disclosures now required have no significance. Rather, it is that other, more significant factors are undisclosed and that these have the effect of making any decision based on the disclosed factors of questionable rationality.

5. The Federal Trade Commission Trade Practices Rule

Perhaps the most striking evidence of the failure of TIL to affect transactional behavior on the terms of credit contracts has come from the Federal Trade Commission ("FTC"). In its recently proposed Trade Regulation Rule on Credit Practices, the FTC seeks to (1) outlaw cognovit notes, waivers of exemption, and wage assignments; (2) limit the taking of security interests and require an identification of each item of encumbered property; (3) require repossessing creditors to credit the fair market value of seized property; (4) prohibit attorney's fees; (5) limit late payment and deferral charges; and (6) regulate co-signer practices. These rules concern some matters that are subject to TIL disclosure requirements and some which are unregulated.⁷⁴

It is interesting to examine the FTC's justification for the rule.⁷⁵ The Commission argues that consumers have no bargaining power over the terms of the transaction but must accept credit contracts on a "take-it-or-leave-it" basis. There are resplendent references to inadequate information as to the probability of default or the operation of default remedies, and, perhaps even more importantly, the creditor's ability to badger and threaten the defaulting consumer in a way that will make the consumer's life downright miserable. The FTC suggests that consumers lack adequate information and that they cannot possibly understand the economic and social costs of the risks being assumed when they agree to the matters to be regulated. Finally, it is argued that these matters are not significant to creditors but have an enormous impact on consumers. One must stand in awe of this reasoning as

may have enormous consequences in the event of default and bankruptcy, the consumer will remain ignorant of them.

73. See *Lamar v. American Fin. Sys.*, 577 F.2d 953 (5th Cir. 1978); *Elzea v. National Bank of Georgia*, 570 F.2d 1248 (5th Cir. 1978).

74. FTC, Proposed Trade Regulation Rule Regarding Credit Practices, 40 Fed. Reg. 16,347 (1975).

75. See FTC Memorandum in Support of Trade Regulation Rule to Limit Creditor Remedies (Apr. 19, 1974) [hereinafter cited as FTC Memorandum]. See also Wallace, *Toward a New Approach to Default—Model of Constructive Consumer Credit Reform* (FTC Bureau of Cons. Protection).

applied to TIL. As to those matters covered by present TIL requirements, TIL has been singularly ineffective in having any discernible impact on the bargaining process, the learning process, or the evaluatory process. As to those matters not covered by TIL, TIL has been woefully inadequate; disclosures have been omitted in areas of major consumer significance. Indeed, although not addressed to this point, parts of the FTC Report imply that this is a significant limitation of TIL.⁷⁶

This is not the appropriate place to evaluate the FTC's proposal. However, it does not seem remiss to question whether an assault on the underlying credit practices should not be accompanied by a more realistic assessment of what disclosure can and cannot be expected to accomplish.⁷⁷ Furthermore, taking the FTC's report on its face leads us to suggest that the FTC has, at least tacitly, reached many of the same conclusions about term disclosure that have been set forth here.⁷⁸

C. *Can Truth in Lending Affect Transactional Behavior?*

If TIL is to affect transactional behavior, transactional information must be provided to consumers in time to permit its utilization as part of the decision-making process. Deficiencies in the present Act could theoretically be remedied by two approaches. Under one approach, some sort of waiting period would be required between the time the credit information is put into the consumer's hands and the time he is permitted to make a binding contract. Alternatively, the emphasis of TIL would be changed from disclosure of information regarding the particulars of the consumer's transaction to some type of generalized disclosure for the creditor's transactions. There are serious objections to both approaches.

The waiting period approach could be implemented by

76. See also FTC, Proposed Trade Regulation Rule Regarding Credit Practices, 40 Fed. Reg. 16,347 (1975).

77. Proponents of substantive regulation of credit terms are frequently realistic in their assessment of the value of disclosure. See, e.g., Wallace, *supra* note 24, at 475-76, 494; cf. Jordan & Warren, *supra* note 17, at 1320-22 (value of disclosure to most consumers is limited; could be enhanced by provision of effective consumer protection in area of creditors' remedies).

78. One well-known consumer organization has failed to address adequately the issues in the debate over term disclosures. On several occasions, Consumers' Union urged retention of the term disclosures because of their importance for decisionmaking. See Recommendations of Federal Credit Legislation Subcomm. of the Corporations, Banking and Business Law Comm. of the Young Lawyers Division of the ABA (Mar. 22, 1978) (dissenting opinion). But its editors told consumers shopping for new cars that "you can locate the lemons before you sign on the dotted line. Just keep your eye on the APR." 43 CONSUMER REP. 201 (1978). The entire discussion of new car loans is addressed to cost alone. There is nary a mention that consumers should also consider the terms of the credit contract.

(1) requiring a set time period between disclosure and the making of a binding contract, or (2) delaying the binding effect of a contract signed at the time the disclosures are given by some sort of rescission or "cooling off" period.⁷⁹ The former method presents three obvious difficulties. First, since the consumer would, by definition, have to use the creditor's facilities and personnel twice, there would be increased costs. The longer the period, the greater the attending costs, because the process of making a binding contract is likely to require a more complete review of what was transacted at the time the disclosures were furnished. Second, there are difficult policing requirements, especially if the period is to be rather short, for example, one hour. Third, and perhaps most important, this method would dramatically alter credit practices since the consumer's initial commitment to the transaction would be weaker. Thus, creditors might be expected to spend much more effort the first time to "sell" the consumer and to solidify the particular deal.⁸⁰ While some consumers would say that this approach is desirable, there is no question that it will cost more, perhaps substantially more.

The rescission method suffers from precisely the opposite problem, that is, it is not likely to be effective. Studies of "negative option" plans suggest that consumers rarely utilize the plans, and the FTC repeatedly has condemned such arrangements on precisely this ground.⁸¹ Moreover, the consumer is already psychologically and verbally committed to the particular transaction; and, again, costs will increase, perhaps considerably. In the case of a loan, creditors will have to choose between not disbursing the money and thereby requiring a second "visit," or disbursing it and facing the potential risk of non-collection upon rescission. In sales of goods, sellers may be reluctant to allow the consumer to take the item home and thereby save delivery and handling costs. In

79. Vermont formerly permitted a one day cooling off period on retail sales of goods and services, both cash and credit, if the consumer had not received a substantial portion of the goods or services. VT. STAT. ANN. tit. 9 § 2454 (1971). The statute was later limited to door to door sales, with a three day cooling off period. *Id.* § 2454 (Supp. 1978).

The pending Senate bill would approximate the first of these approaches in home mortgage transactions, by requiring that good faith estimated disclosures be given within three days after loan application. S. 2802, 95th Cong., 2d Sess. § 14(b) (1978). In most mortgage transactions, there will be a built-in delay of several weeks or months before settlement, so the consumer has a period of time to consider the disclosures and theoretically to shop elsewhere.

80. *Cf. Sher, The Cooling Off Period in Door-to-Door Sales*, 15 UCLA L. REV. 717, 730-32, 733-35 (1968) (salesman's function is to bring consumer to point of decision; if decision involves greater commitment, more sales effort is likely to be required).

81. *See* 16 C.F.R. § 425.1 (1978) (FTC's trade regulation rule on negative option plans).

both cases, there are also the costs of turning one transaction into two.

The alternative of providing more generalized disclosure has its own disabilities because of a basic premise of TIL that consumers will compare the costs and terms of their transaction. To the extent information is generalized, the consumer will lack meaningful information about his particular transaction. For example, since bank consumer loan rates are likely to vary within a relatively narrow range, simply telling the consumer that the average rate is twelve percent, or that the range is ten to fourteen percent does not give him enough information for advance comparisons. Indeed, there is ample evidence that consumers have fairly good institutional knowledge of which lenders charge less, that is, that banks generally charge less than finance companies, and consumers probably do not need TIL for this purpose;⁸² instead, they need it to compare the relatively smaller differences that are likely to exist within a single class of creditors. In addition, practical limitations on presentation dictate relatively little information—certainly much less than on the typical TIL statement.

In fact, each of the possible techniques for generalized disclosure has distinct weaknesses. Posting of credit terms within the creditor's premises requires that the consumer visit those premises, that he be aware of the postings, and that he have the time and convenience to examine them without pressure to get on with his business. The collection and dissemination of rates and other terms through brochures or flyers prepared by the creditor, or by a public or private institution on a geographical basis, may involve substantial implementation costs; the data is probably out of date by the time of publication; and there remains the difficulty of getting the information into the consumer's hands in a timely manner.⁸³ Advertising of credit terms through print or electronic media is haphazard in its impact: creditors cannot be compelled to advertise, there is no assurance that consumers will see or react to the ads, and traditional concerns about deceptive advertising are more likely to inhibit than to enhance a creditor's willingness to publicize terms. In sum, generalized information cannot be expected to affect transactional behavior in the same way individualized disclosure might.

Our conclusion is that generalized disclosure is not a substitute for TIL-type disclosures in affecting consumer decisions. If

82. See note 28 *supra*.

83. The Senate bill would direct the Federal Reserve Board to experiment with the preparation and dissemination of APR brochures. S. 2802, 95th Cong., 2d Sess. § 18(a) (1978). At an earlier time, some of the Small Loan Acts required rate posting. See B. CURRAN, TRENDS IN CONSUMER CREDIT LEGISLATION 38 (1965).

properly organized, individual disclosure might prove effective, but substantial changes are necessary in both the method of delivering the pertinent information and the timing of delivery. It may be that the costs of effective delivery far outweigh the benefits to be derived.

II. ALTERNATIVE FUNCTIONS OF TRUTH IN LENDING

A. *Limited Transactional Impact—The Alert Function*

If it is too much to expect TIL disclosure statements to affect transactional behavior on a large scale, perhaps they may have a more limited impact. That is, TIL disclosures are not expected to facilitate shopping as such, but they do lead to a general awareness of rates and other terms. If the TIL statement reveals rates and terms that are within anticipated norms, the consumer is satisfied; but a TIL statement containing rates or terms that are outside of anticipated norms acts as a red flag. It alerts the consumer, at the very least, to examine the proposal with greater than usual care. This effect is consistent with studies of consumer behavior that suggest that consumers do not shop for what might be termed the "best buy," but rather shop for goods and services that will satisfy their wants and that are within an acceptable level of price and quality.⁸⁴ For example, a consumer who wishes to buy a portable color television may not shop if the quoted price is between \$400 and \$500 unless there are other factors which cause dissatisfaction, such as a negative experience with the salesperson, but will refuse to buy at \$550.

In concrete terms, this "alert function" might work as follows. A consumer making a credit purchase of a new car brings an awareness that the APR should be in the twelve to eighteen percent range.⁸⁵ A consumer quoted an APR of seventeen percent does not shop elsewhere because this is consistent with his expectations, and the cost-benefit factors noted earlier inhibit shopping. But a consumer who receives a TIL statement with an APR of thirty percent will be alerted, at least, to question the reason for such a rate, and perhaps, to take his business elsewhere. It should be emphasized that this is not a shopping response as such; rather it is a negative response to a particular credit grantor.⁸⁶ This

84. See Permut, *Consumer Information Processing* 7-8 (Memo to the FRB May 28, 1977).

85. Of course, it is necessary to increase consumer "awareness" of rate norms. There are indications that TIL has been quite effective in accomplishing this limited objective. See FEDERAL RESERVE BOARD, 1977 CONSUMER CREDIT SURVEY 3-7 [hereinafter cited as 1977 CONSUMER CREDIT SURVEY]; BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, 64TH ANNUAL REPORT 1977, at 334-38 (1978).

86. There is some evidence that consumers behave in this way, although the im-

"alert function" is quite consistent with the economic cost-benefit analysis suggested earlier.⁸⁷ That is, the "alert" cases are situations where the credit costs (APR) so clearly exceed the norm that the marginal return from further search is likely to exceed the cost.

If this is the function of a disclosure statement, then it is possible to make some tentative judgments about what TIL should require. First, since the alert function is essentially an immediate response to an unexpected stimulus, disclosures must be relatively simple and uncluttered. The consumer will not be "alerted" to something that is hidden in a maze of fine print. Second, the disclosures must be such as to permit rough and ready comparisons. Numerical figures are perhaps best suited to this purpose, since consumers can readily make a side-by-side comparison with an expected norm. By the same reasoning, to the extent that there is no "norm," this process is unlikely to occur. Third, the disclosures should not require further analysis for comparative purposes. Since the alert function is, in essence, a conditioned reflex to a single stimulus, the alert is much less likely to occur if the consumer must go through one or more analytical or mathematical steps to determine whether the particular matter is within an anticipated norm.⁸⁸

If the alert function is the principal objective of TIL, then the TIL statement would be expected to emphasize the crucial "cost" terms, since these are most likely to alert the consumer to a questionable transaction. For example, such matters as the APR, the finance charge, the periodic payment, and perhaps "other charges" (*e.g.*, for insurance, filing fees, added services) would be included. On the other hand, many of the computational disclosures would be eliminated since these are not designed for head-to-head comparative purposes and tend to detract attention from those numerical categories of information which are supposed to alert the consumer. Similarly, disclosure of the terms of the transaction would not be included in their present form because of the consumer's inability to evaluate term items against acceptable norms so as to trigger the "alert" response and because many of the term disclosures require several analytical steps to make the

part of TIL is less than clear. Thus, when some bank cards eliminated the free ride period, consumers responded with vocal complaints. But, it was not the TIL disclosures of the elimination of the free ride that triggered the response; rather, it was the unexpected appearance of a finance charge on the monthly statement.

87. See notes 23-32 & accompanying text *supra*.

88. This phenomenon is somewhat similar to designating an official name for a product (*e.g.*, peanut butter) and anticipating that consumers will not buy a similar product without the official name (*e.g.*, peanut spread).

comparisons.⁸⁹ To the extent that term disclosures were to be included, the Act would have to be revised to serve the alert function better. Thus, if it were expected that consumers would compare rebate methods, the Act might give standardized or official names to different methods in the hope of encouraging this kind of side-by-side comparison. For example, a rebate by the actuarial method might be termed the "preferred rebate method," and the rule of 78s method the "nonpreferred rebate method."⁹⁰ Such an approach could enable the consumer to make direct comparisons and would alert him to an unfavorable rebate method.

There is, however, a danger of overemphasizing the price terms. All terms are really "cost" terms in that they affect the overall cost of credit. Insofar as the price-tag items such as APR and finance charges are stressed, creditors may be encouraged to shift costs to consumers by adjusting default provisions or other terms.⁹¹ Legislatures have recognized this possibility: creditors have been prohibited from including certain terms in credit contracts on the assumption that consumers are unable to evaluate the trade-offs involved.⁹² But short of forcing competition on price-tag items by a comprehensive standardization of credit contracts, and, to some extent, creditor practices, regulations will leave creditors considerable freedom to alter term provisions to avoid the impact of competition on price-tag items. This tactic may be particularly pernicious, since the main impact of such cost shifting is likely to fall on defaulting borrowers because many of the terms of the credit contract which shift risks pertain to default. While it may be arguable social policy whether or not non-defaulting lower risk borrowers should pay higher prices for credit to absorb losses that are properly allocable to higher risk borrowers who have a strong likelihood of defaulting, it seems relatively certain that higher risk borrowers should not be burdened with costs that properly should be borne by all borrowers.

89. See, e.g., notes 56-57 & accompanying text *supra*.

90. See note 57 & accompanying text *supra*.

91. See NAT'L COMM'N, *supra* note 17, at 24; see FTC Memorandum, *supra* note 75, at 279. Some high risk lenders use default provisions to compel frequent refinancings which generate added income in the form of front-end charges and fees not subject to rebate requirements.

92. For example, recent consumer credit legislation sets a ceiling on insurance charges, defines "default," restricts delinquency charges, regulates rebate methods, limits the taking of security interests, and regulates or prohibits post-default charges for repossession, resale, and attorney's fees. See UNIFORM CONSUMER CREDIT CODE (1974).

Another example of this phenomenon is the prohibition by many states, and now by the Federal Trade Commission, of a waiver of defense clause giving the creditor holder in due course status. See 16 C.F.R. § 433 (1978). See generally Comment, *The FTC's Holder-in-Due-Course Rule: An Ineffective Means of Achieving Optimality in the Consumer Credit Market*, 25 UCLA L. REV. 821, 822-27 (1978).

B. *A Contract Synopsis*

TIL may be viewed as an attempt to provide consumers with a summary of the important information on the entire credit contract for use not only at the time of transaction but also during the performance phase of the agreement. Although that was not the original conception of TIL, there has been increasing talk of the need to serve this function.⁹³ A glance at the typical consumer credit contract, with its maze of fine print and seemingly obscure and arcane provisions, further reveals this need.

Disclosure in the form of a contract synopsis serves a number of interrelated functions. The TIL statement would translate and explain the contract, and the consumer should be better able to understand its content during contracting, performance, or default. The TIL statement also serves a related purpose: it acts as a badge of good faith and enables the consumer to verify and check the basic contract charges, his own responsibilities, and the rights of the creditor. In this sense, the disclosure may produce greater emotional satisfaction with the transaction and a feeling that the consumer is not being deceived.⁹⁴ Though the gain is difficult to quantify, there is something to be said for eliminating consumer suspicion and increasing the consumer's sense of confidence and well-being.⁹⁵ If such were the objective of the Act, disclosure in less legalistic, everyday language of such matters as computational elements, security interests, and the creditor's collection rights would become important.

The contract synopsis can also serve another function, one which consumers support strongly. The disclosures provide a

93. See *Simplification Hearings*, *supra* note 2, at 286, 298, 307-09.

94. In the survey by the National Commission on Consumer Finance, consumers who had recently engaged in a credit transaction and said that they noticed TIL information were asked in what way the information was used. Fifty-four percent answered that they did not have a specific purpose, but felt better knowing charges and rates. In another question, consumers who said that they used TIL information generally in credit transactions were asked how they used the information. Forty-five percent said that they felt better knowing charges and rates. See Brandt & Day, *supra* note 12, at 309-10. In the recent Federal Reserve Board survey, more than 80% of the respondents, excluding those who responded that they did not know, agreed with the statement that TIL makes people more confident in dealing with creditors. These figures were contained in the "raw data" for the survey but, for reasons that are unclear, were not included in the final report. 1977 CONSUMER CREDIT SURVEY, *supra* note 85, at 11, 19.

95. It is sometimes suggested that providing such information has intrinsic worth. Cf. Dauer & Gilhool, *supra* note 68, at 147-49 (availability of constitutionalized repossession provides debtor with a measure of control over events affecting him; thus there is intrinsic value to the procedure itself); Summers, *A Critique of Professor Fried's Anatomy of Values*, 56 CORNELL L. REV. 598, 620-23 (1971) (Professor Fried argues that laws have not only instrumental value, but have intrinsic value as "ends in themselves").

means by which sunlight can be shed on state-law contract provisions that are archaic, oppressive, unconscionable, or outright illegal. The clearest manifestation of this effect occurs when the TIL disclosures reveal terms that are illegal under applicable state law: for example, excessive interest or other charges, impermissible insurance provisions, overbroad security interests, or improper rebate methods.⁹⁶ Contract synopsis disclosure not only permits the consumer to seek remedies for violations but also discourages the use of impermissible terms for their *in terrorem* value.⁹⁷

But even for those contractual provisions that are not clearly unlawful, TIL would serve a law reform function. Even though TIL would not affect the underlying state law, meticulous disclosure would bring to the fore contract provisions long hidden in the boilerplate. Recent litigation over disclosure of the right of acceleration,⁹⁸ credit insurance,⁹⁹ and non-purchase money security interests¹⁰⁰ serves this purpose. In the long run the disclosures could help to promote substantive law reform through uncovering contract provisions that might not be justifiable in the present marketplace. In other words, consumers now agree to outlandish terms like acceleration because they do not understand the impact or costs of the terms. Disclosure would likely reduce the imbalance between creditor and consumer understanding. While disclosure does not benefit consumers in their immediate transactions, it may result in the eventual elimination of many untoward practices. This could occur through litigation, through the political process, or through publicity embarrassing creditors into not using certain terms or at least reassessing the need for them.¹⁰¹ For example,

96. Consumer spokespersons stress the utility of TIL disclosures for this purpose. See *Simplification Hearings*, *supra* note 2, at 278 (statement of James Boyle). See also *id.* at 299 (testimony of Willard P. Ogburn, National Consumer Law Center).

97. In this connection, assume a creditor's TIL statement discloses a right claimed by the creditor which violates state law. Is there a violation of TIL or only of the applicable state law? See *Pinkett v. Credithrift of America, Inc.*, 430 F. Supp. 113 (N.D. Ga. 1977); *cf. Gennuso v. Commercial Bank & Trust Co.*, 566 F.2d 437 (3d Cir. 1977) (cannot disclose confession of judgment clause if not taken).

98. See cases cited at note 64 *supra*.

99. *E.g.*, *Hickman v. Cliff Peck Chevrolet, Inc.*, 566 F.2d 44 (8th Cir. 1977) (disclosure of credit life insurance premium as part of amount financed was proper).

100. *E.g.*, *Anthony v. Community Loan & Inv. Corp.*, 559 F.2d 1363 (5th Cir. 1977) (reference to security interest in personal property and to rights and remedies under U.C.C. sufficient to apprise borrower of security interest created in "closed-end, nonsale credit transaction"); *Gennuso v. Commercial Bank & Trust Co.*, 566 F.2d 437 (3d Cir. 1977) (failure adequately to describe property subject to security interest violative of TIL); *Blackmond v. Walker-Thomas Furniture Co.*, 428 F. Supp. 344 (D.D.C. 1977) (failure to provide clear description of all property subject to security interest violative of TIL).

101. The best recent example of this phenomenon has been the movement to "simple English forms." In the process of drawing up such forms, creditors have dispensed with asserting many of their "traditional" rights.

creditors might be expected to deliberate before contracting for an attorney's fee of twenty percent upon default or to conclude that level term credit life insurance was unnecessary.

Consumer advocates rely on the "contract synopsis" function rather than the original concept of affecting transactional behavior because it promotes subjective values and produces intrinsic rewards. It does not purport to affect transactional behavior and, therefore, is not capable of evaluation in functional terms. Indeed, consumers have switched to the contract synopsis justification partially because of some embarrassment over the failure of the statute to produce any discernible impact on transactional behavior. To say that this was not the original purpose of TIL misses the point; consumer advocates would argue that TIL is promoting this highly desirable function, and its historical *raison d'être* is irrelevant so long as its present *raison* is meaningful and important. And who is to say that promoting consumer understanding and a better sense of well-being is not a significant public benefit?

It is difficult to determine what types of disclosures contribute to a person's sense of satisfaction and well-being, but some tentative thoughts can be ventured. First, the statement must be clear and easily understood.¹⁰² A consumer is unlikely to be reassured and satisfied by something he cannot comprehend. Second, the disclosure statement must not conflict with the consumer's understanding developed during the negotiation stage, nor can the statement be contradicted by non-TIL information elsewhere on the same document, since such inconsistencies are not likely to reassure the consumer. Finally, the synopsis must be accurate and complete; important terms should not be omitted that may later come to haunt the consumer. Unfortunately, the Act, as presently construed, does not produce a contract synopsis that meets these tentative objectives.

A quick perusal indicates that present TIL statements are frequently unclear and incomprehensible. It is unlikely that consumers understand such terms as deferred payment price, security interest, rule of 78s, prepaid finance charge, and the like, which are all features of most present day TIL statements. It is also probable that consumers do not fully appreciate the distinction between unpaid balance of cash price, unpaid balance, amount

102. The Senate bill attempts to do this in several ways. First, it would require brief explanatory phrases to accompany the chief disclosure items. S. 2802, 95th Cong., 1st Sess. § 14(a) (1978) (amending § 128(a)(8) of the Truth in Lending Act, 15 U.S.C. § 1638(a) (1976)). Second, it directs the Federal Reserve Board to prepare model disclosure forms and model clauses which utilize "readily understandable language to simplify the technical nature of the disclosures." *Id.* § 5(a) (amending § 105 of the present Act, 15 U.S.C. § 1604(a) (1976)).

financed, and deferred payment price.¹⁰³ In addition, the present law allows creditors to integrate TIL disclosures with other disclosures that are required by federal or state law, and with the contractual terms themselves. Thus, although one would expect a contract synopsis to be segregated from the documents being summarized, this is a rare occurrence. In sum, it is not surprising to find survey results showing that consumers in overwhelming numbers find present TIL statements to be complicated.¹⁰⁴

The contract synopsis function is similarly undermined if "inconsistent" disclosures are permitted elsewhere on the form.¹⁰⁵ For example, a consumer is hardly likely to feel confident and reassured if he reads the APR as eighteen percent, and elsewhere the document states that interest is computed at the rate of "\$10 per \$100 add on."¹⁰⁶ Real estate transactions are an area of continuing confusion, since the disclosed APR, calculated by including points and other front-end charges, is a mysterious figure to consumers who are accustomed to thinking in terms of the contract rate applicable to the unpaid balance. Similarly, a consumer is unlikely to feel reassured if the TIL statement contains a one-sentence description of "default charges" and a ten paragraph section of the contract entitled "remedies upon default."¹⁰⁷

What terms should be included in the synopsis and, of perhaps even greater importance, what terms should be left out? By definition, not all contractual terms can be included, since the statement would no longer be a synopsis. Should the included terms be those that will affect the larger number of consumers, such as missing a payment and incurring a late charge, or those that have the largest economic or physical consequences, such as default, seizure and sale of collateral, and liability for a deficiency

103. Even Senator Proxmire expressed some bewilderment about these terms during the Senate hearings. *Simplification Hearings*, *supra* note 2, at 116-17.

104. In the recent Federal Reserve Board survey, more than 80% of respondents (excluding "don't know" answers) agreed with the statement that TIL statements are complicated, and almost 75% of the respondents (excluding "don't know") agreed that some TIL information is not very useful. See 1977 CONSUMER CREDIT SURVEY, *supra* note 85, at 19.

105. An application containing credit information not in TIL terminology or format, and with important items omitted, is likely to confound the consumer. See note 15 *supra*.

106. Yet under the present Act a creditor may feel obliged to describe the rate in this way to comply with state law. *Cf.* *Mason v. General Fin. Corp.*, 542 F.2d 1226 (4th Cir. 1976) (State disclosure statutes are subordinate to but not preempted by TIL). Federal regulations explicitly permit inconsistent disclosures under state law. Reg. Z, 12 C.F.R. § 226.6(b) (1978).

107. This suggests the wisdom of some form of comprehensive preemption provision. See S. 1501, 95th Cong., 1st Sess. § 15 (1977). The need to distinguish between state disclosure laws and state substantive laws regulating consumer credit transactions may make the problem insoluble. For example, should the TIL Act preempt a state law which requires a promissory note to provide for "interest" at six percent?

judgment? Should disclosure be required when the economic consequences are small or, perhaps, when a particular matter is regulated by statute?¹⁰⁸

The authors suggest that these are the relevant questions to ask if Congress is serious about providing a contract synopsis. We could also suggest that the present Act is vulnerable to a charge of being misleading insofar as it attempts to provide such a synopsis. It has been noted that disclosure is required of terms that have little economic significance and terms that frequently are regulated by statute; but terms such as acceleration, rights and limits upon nonjudicial repossession, liability for deficiency judgments (including both the balance of the debt and "extra" charges occasioned by the default), a creditor's willingness to forego collection, the consumer's ability to obtain a refinancing or deferral, and "cure" periods are omitted. A consumer who faces default and confronts these consequences, none of which appear on the "synopsis," might have a sense of being "bushwhacked."

There are other difficulties with the use of TIL disclosures for the "synopsis" function. One is the consumer's perception of disclosure. It is not clear that consumers readily understand the distinction between a law that requires creditors to disclose certain information and a law that regulates the content of the information, that is, the terms of the consumer credit contract itself. In this connection, some congressional proponents of TIL have had to answer letters from angry constituents who queried why TIL regulation permitted the creditor to charge an APR of twenty-two or twenty-five percent. In fact, the disclosures may have quite an opposite effect from the intended purpose of requiring disclosure so that a consumer can evaluate the transaction for himself. That is, the federal disclosures may reduce the consumer's guard since the aura of regulation may suggest that he already is protected.

Moreover, it should be recognized that the "contract synopsis" function conflicts with other TIL objectives. To the extent that consumers can be taught to evaluate relative credit costs, it becomes more difficult to accomplish such evaluations when the statement includes additional terms. It is unlikely that consumers can or will be turned into walking consumer protection experts, and as more term disclosure is included, the impact of the cost information inevitably will be minimized. This is not to urge the

108. Moreover, if it is decided to disclose default charges, what is a default charge? Does it include a five dollar late fee, 10% attorney's fee, cost of repossession, failure to rebate a portion of the finance charge, right of acceleration, or other consequence of default? These are difficult questions to answer, but they are ones which must be answered by those who would support the contract synopsis notion. See generally Landers, *Truth in Lending: Closed End Credit*, PRAC. LAW., June 1978, at 32.

abandonment of the synopsis function; it is only to illustrate inconsistencies among TIL objectives.

Although the "contract synopsis" serves a law reform function, it is difficult to regard such a goal as a serious basis for the present Act. First, it is somewhat misleading to talk about shedding sunlight on provisions that have always been "hidden." These provisions in question have long been included in state statutes and in contractual documents, and at least sophisticated consumer representatives have been aware of their existence.¹⁰⁹ Also, if creditors have been utilizing such archaic and oppressive procedures, the victimized consumers must have been aware as well. Finally, the impact of disclosure on such unfair provisions is not clear. In some cases, it will be a bit easier for consumer lawyers to find substantive state law violations in consumer contracts; and, there is certainly an inducement for consumer lawyers to essay law-reform allegations in the form of TIL violations on behalf of clients in default who have no other substantive defense. But fulfilling this end would require a detailed and intricate TIL statement, since general and superficial information is likely to be ineffective in unearthing violation of the typically technical provisions of state regulatory statutes. Whether it will reform the law is problematical: disclosure has not led to reform in the past when reform-worthy provisions have been hidden in the contract; where significant reform of state consumer credit law *has* occurred—in the states enacting the Uniform Consumer Credit Code, for example—it is impossible to trace that reform directly to abuses brought to light through Truth in Lending disclosures. If there is a need for substantive law reform, one can only wonder whether disclosure requirements will contribute to that effort.

C. *Special Issues of Open-End Credit*

Most of the prior discussion pertains largely to closed-end credit, although many of the comments are equally pertinent to open-end credit. The peculiar nature of open-end credit causes the disclosure issues to be somewhat different, and some attention should be given to these special elements.

TIL requires disclosures to be given in open-end credit transactions at two points: at the opening of an account, and at the time of each periodic statement, usually monthly.¹¹⁰ The time relationship between the opening of a credit account and the first credit transaction varies. In some cases, the account is opened at

109. The drafters of the Model Consumer Credit Act evidently knew enough about most of these provisions to provide for their prohibition. MODEL CONSUMER CREDIT ACT (1973).

110. Reg. Z, 12 C.F.R. § 226.7(a), (b) (1978).

the time of the first transaction, and if this is the case, the disclosure issues are similar to those for closed-end transactions. Most typical of these cases are accounts opened by retailers at the time the consumer desires to make a purchase. On the other hand, consumers may open an account, as in the case of a bank credit card, before any specific transaction is undertaken.

With respect to the pre-use disclosures in open-end credit, the shopping goal is even more tenuous. At the time of an individual purchase or cash advance with an existing credit card, the consumer is powerless to shop for a better credit deal no matter how well-informed he is about the costs incident to the use of that card. His "shopping" option is essentially limited to paying cash or using those credit cards he has and the seller accepts. Moreover, at the time of his initial application for open-end credit, the consumer is unlikely to have many specific transactions in mind, and his attention is more likely to focus on the usefulness of that particular open-end plan than on its credit terms. For instance, he may want simply to gain access to a particular department store, or he may desire the general convenience, widespread acceptance, or prestige of a bank card. With the rates for open-end credit so uniform, and other terms, such as the balance assessment method, so arcane, the consumer probably would not shop for open-end credit on any comparative basis at all. Moreover, the initial disclosures suffer from an important defect: they attempt to explain a plan in the abstract, without any concrete examples. Whether the consumer can be expected to understand a highly intricate credit plan in the abstract is open to question.

For our purposes, the important disclosure is the billing statement. Most of the consumer's credit decisions are based on the billing statement, and the billing statement frequently provides actual figures representing the consumer's transactions which illustrate the operation of the plan. Several important distinctions between the typical open-end disclosure and the typical closed-end disclosure merit comparative analysis. First, in closed-end disclosure, the TIL statement represents only part of the documentation of the transaction, and frequently, additional contractual provisions are on the face or back of the documents. In contrast, the typical open-end disclosure statement serves as both the required disclosures under TIL *and* the underlying contract. In other words, in the area of open-end disclosure, TIL has captured the essence of the contractual arrangement. Second, the consumer engages in repetitive transactions which generate the same TIL form. The consumer is constantly reminded of the critical credit provisions, and he is in a position to revise or modify his

use of that credit plan if its terms strike him as unacceptable.¹¹¹ The repeated disclosures, therefore, have a considerably greater chance of affecting transactional behavior than the one-shot disclosures in closed-end transactions. Third, the nature of open-end credit means that monthly finance charges are likely to be small. For example, an open-end account of \$1,000 will usually involve a monthly charge of \$15. Moreover, since the consumer can always pay in full, he does not face the same level of economic consequences as when he agrees to a closed-end transaction extending over a considerable period of time.¹¹²

Most important, however, is the dearth of competition on the nominal APR: virtually all open-end creditors will charge the statutory maximum. Whatever competition there is comes in the form of differences in billing methods, or, more precisely, on three billing "issues": (1) is there a "free ride" for new purchases; (2) how is the balance determined for the purpose of computing the finance charge; and (3) are there finance charges on amounts paid in full during the billing period?

Present day open-end plans differ markedly in answering each of these questions, and there are a number of permutations and combinations of the basic calculational elements. For our purpose, it is enough to appreciate that although all plans may use the same nominal APR, the true APR when calculated on a historical basis differs markedly depending on the particular method employed.¹¹³ On a randomly selected group of accounts, the highest may be well over fifty percent more than the lowest, and it is possible to construct a set of "horribles" in which the true APR under some of the methods will exceed one hundred percent.¹¹⁴

To the extent that competition, if any, is realized between billing methods, the TIL statement will affect consumer behavior only to the extent that the consumer can understand the method employed by a given plan and evaluate that method against other

111. See *Ratner v. Chemical Bank Trust Co.*, 329 F. Supp. 270 (S.D.N.Y. 1971).

112. Consumers can prepay closed-end obligations and get somewhat the same result. But consumers do not think in terms of prepayment, and often for a good reason: there are frequently contractual penalties and an absence of rebates of front-end charges, which together make prepayment costly indeed. Moreover, closed-end transactions tend to have much larger balances, thus making early payment financially difficult.

113. See *McAlister & DeSpain*, *The Effect of Alternative Billing Methods Upon Retail Revolving Credit Yields* (Credit Research Center, Purdue University 1976); S. REP. NO. 278, 93D CONG., 1ST SESS. 29-37 (1973) (additional views of Senators Proxmire and Hathaway); Kripke, *supra* note 17, at 466-67.

114. For example, the previous balance method gives no credit for payments of less than the full balance due. Thus, if the consumer is billed \$100 on the billing date and pays \$85 the next day, the finance charge is computed on the full \$100. At a monthly charge of 1.5%, the finance charge will be \$1.50. The actual APR is almost 120%.

alternatives. It strains credulity to think that consumers can do this under present circumstances. A glance at a typical description of billing methods quickly reveals intricate language, technical terminology, and an absence of examples, except insofar as the consumer's own subsequent transactions provide examples. Indeed, many bank card statements contain descriptions of three or four different billing methods, each of which is used for different components of the card plan. The consumer is unlikely to understand these provisions and is likely to be in a similar quandary when he sees the eighteen percent nominal rate and an actual rate which is somewhat different.¹¹⁵ Finally, the emphasis on the nominal rate as the key shopping item, and the fairly common knowledge of the similarities of nominal rates, is patently misleading since it tends to detract attention from the important differences in billing methods and suggests that, contrary to reality, all creditors charge approximately the same amount.

It can be argued that the available information permits the consumer to comprehend the different methods if he takes the time and effort. Moreover, given a number of transactions and the length of time involved, the consumer has an economic incentive to acquire the necessary information. This may be true, but it tends to contradict the basic assumption of TIL that consumers need help in processing and understanding transactional information. Indeed, none of the TIL aids—standardization of concepts, official names, “meaningfulness,” and numerical comparison—is adapted to this problem. Moreover, the consumer is not alerted to the need to get more information; he is told that the most important numerical disclosure—the APR—is the same for everyone.

One must conclude, reluctantly, that billing method descriptions cannot be simplified so that they will be understood readily. The answer, if there is one, may be to designate one or more methods by “official names” in the hope that competition will encourage creditors to use them. For example, the average daily balance method with a free ride for new purchases and no charges for payment in full could be designated as the “preferred billing method”; creditors using it or any more favorable method would only be required to state that they used the “preferred billing method.” Other creditors might be required to explain their methods, or creditors using a particularly “expensive” billing method could be required to state that they used the “high cost billing method.” Such an approach would be consistent with the

115. This can often occur when, for example, a consumer obtains a cash advance for which there is a one-time two dollar fee. On the first monthly statement, the actual APR will be higher than 18% because the two dollar charge is computed into the finance charge on top of the periodic rate for that month. Reg. Z, 12 C.F.R. §§ 226.5(a)(3), .7(b)(1)(v), (vi) (1978).

original objective of TIL: to produce standardized terminology to reduce search costs.¹¹⁶

D. *Consumer Defenses to Creditor Actions*

The present Act has served a different function from those discussed above. In many cases, it has provided consumers with a defense to a creditor's collection action. Sometimes, the consumer had no defense at all aside from the possibility of filing some sort of insolvency proceeding, and other times the consumer's "real" defense was much more difficult to assert. A combination of a favorable statute, easy to find violations, procedural advantages, minimum damages, and payment of attorney's fees made the TIL defense a viable consumer weapon.¹¹⁷ To consumer advocates, the fact that the TIL claim was, in a sense, feigned, was of no moment. The consumer had a real grievance and was permitted to exercise it through the legal system.

Until recently, the TIL claim could be used offensively or defensively to reduce the creditor's claim or, privately, as a basis for negotiation and settlement. More recently, the stakes have escalated considerably. Courts in two states have held that the existence of a TIL violation *ipso facto* makes the entire obligation void.¹¹⁸ These decisions have not been based on the Act itself, but on little used state rules that transactions that violate federal law are void. Even under the present statute, creditors have strong inducements to settle TIL actions;¹¹⁹ if the creditor's risk in litigation becomes the possible invalidity of every single credit transaction using a particular form, the inducements are correspondingly greater.

There may be something to be said for a statute that acts as a safety valve for disgruntled consumers. The trouble with this purpose is that it cannot be kept within its banks—there is no assurance that consumers who assert violations have any real grievance beyond inability to pay, or that if they do, their grievance is against the particular creditor whose form contains the violations. And the resulting warfare between consumers and creditors clogs court calendars, inflicts arguably needless costs on creditors (an

116. See generally Landers, *Open End Credit Disclosure Requirements Under the Truth in Lending Act*, 52 S. CAL. L. REV. — (1979).

117. See Landers, *Some Reflections on Truth in Lending*, 1977 U. ILL. L.F. 669.

118. See *American Buyers Club v. Grayling*, 53 Ill. App. 2d 611, 368 N.E. 3d 1057 (1977); *Conrad v. Beneficial Fin. Co.*, 57 A.D.2d 91, 394 N.Y.S.2d 923 (1977); cf. *Hernandez v. Kerry Buick Inc.*, 5 CONS. CRED. GUIDE (CCH) ¶ 98,094 (N.D. Ill. 1977) (if TIL violation, cannot recover finance charge at all as a matter of state law).

119. See Landers, *supra* note 117, at 680-83. See also *Hearings on S. 3008 Before the Consumer Affairs Subcomm. on the Senate Comm. on Banking, Housing and Urban Affairs*, 94th Cong., 2d Sess. 409-12 (1976) (statement of Rhett Tanner).

adverse court decision may require a complete reprinting of forms), and increases the political polarization between consumer and creditor representatives.

TIL, by virtue of its complexity and the likelihood of finding an arguable violation, is not an efficient way to handle general consumer grievances against a particular creditor or against the "system." But there is no easy answer to what is more efficient. Numerous scholars have considered the legal system's proper response to small claims that cannot be prosecuted economically within the present judicial framework. Answers range from ignoring small losses completely to setting up elaborate systems of small claims and community courts. However, this is not the time to address the issue of appropriate ways to resolve such disputes.¹²⁰

The status quo does, however, present a political dilemma. Many creditors view TIL simplification in terms of reduction in disclosures, model forms, reduced liabilities, or something else that will furnish significant protection against the recurring threat of TIL litigation. Consumers, on the other hand, have viewed the Act as an effective weapon for vindicating consumer grievances and are reluctant to lose that utility. A legitimate question remains: whether any consumer loss should be replaced by something else, and if so, what that something else should be.

III. LONG-TERM CONSUMER EDUCATION

TIL has been discussed up to now in terms of single transactions, but consumer credit need not be thought of in such terms: it may be viewed instead as a continuum of transactions. That is, rather than thinking of one individual consumer shopping for one credit purchase, we might visualize a given consumer engaging in a lifetime of credit transactions: some repetitive, such as credit card purchases; others quite rare, such as a home mortgage; and still others falling somewhere in between, such as car purchases, large appliance purchases, and signature loans. So viewed, it is not anticipated that any single disclosure will produce either immediate behavioral change or an individual sense of satisfaction and well-being. Rather, the disclosures might be designed to exert an educational influence on the consumer's credit behavior over time. The use of standardized language on similar forms in disparate transactions, for example, aids in consumer understanding, reduces the costs of mastering each subsequent transaction, and lowers search costs. Indeed, it may be that directing regulatory activities toward improving consumer understanding is the best

120. See generally D. RICE, CONSUMER TRANSACTIONS, chs. 6, 21 (1975).

method of implementing the goal of affecting transactional behavior.

This objective, it would seem, has already partially been achieved. That is, TIL has led to the adoption of an understandable and certain vocabulary for credit transactions so that when consumers and creditors speak of the finance charge or the Annual Percentage Rate, they are talking about the same thing. This standardization has made it easier to teach about consumer credit, especially at the secondary school level. In addition, constant repetition of the APR seems to have increased consumer awareness of the general cost of credit.

Even if the goal is simply consumer education, there is still much to be done. TIL has not achieved uniformity in stating late charges, information on security interests, and the like. Indeed, the Federal Reserve Board has conceded that consumers cannot possibly understand the rule of 78s¹²¹ and the courts seem unable to agree on the meaning of the terms default charges and prepayment penalties.¹²² As one moves from credit cost information to credit term information, the long-term educational impact may be undermined by an absence of standardization of concepts.

Apart from the problem of certainty of concepts is the question of how best to serve this education function. Regardless of the number of transactions, the consumer will not be educated unless at some point he examines the documents. This does not require study at the point of transacting, but the document can be sufficiently forbidding that the consumer will never read it.¹²³ Thus, the effectuation of this purpose requires a level of disclosure that can draw the typical consumer's attention. Probably it is more important that the credit cost disclosures be highlighted and expressed in understandable language. Hopefully, a process of assimilation and self-education would then sensitize the consumer to credit cost variables, and better prepare him for each subsequent transaction. Ultimately, despite the frequency with which the consumer receives credit card statements and closed-end disclosures, the statement may be too complex for any substantial educational impact beyond an awareness of prevailing rates.

CONCLUSION

Despite its legislative history, Truth in Lending has only a

121. See note 57 & accompanying text *supra*.

122. See FRB Off. Staff Int. No. FC-0044, [1974-1977 Transfer Binder] CONS. CRED. GUIDE (CCH) ¶ 31,535 (1977); FRB Off. Staff Int. No. FC-0102, *id.* ¶ 31,680.

123. The FRB survey indicates that the vast majority of respondents, about two thirds, disagree with the statement that most consumers read TIL statements carefully. See 1977 CONSUMER CREDIT SURVEY, *supra* note 85, at 15-19.

doubtful utility in affecting transactional behavior by consumers, largely because of built-in diseconomies: the disclosures are too complex, they come too late, and the consumer may not consider the stakes worth the shopping effort. Other unintended but arguably desirable functions for credit disclosure have emerged through experience under TIL: alerting consumers to unfair terms, establishing the creditor's good faith, synopsisizing the credit contract, providing a vehicle for law reform, and offering consumers a means of achieving rough justice. For all of these, TIL is an imperfect tool. The one function of credit disclosures that seems most consistent with the original legislative intent, and the most capable of achievement, is the effectuation of an ongoing, long-term rise in consumer education and sophistication about credit matters.

At this writing, congressional consideration of Truth in Lending simplification is far from complete. The hopes and motivations of interested parties are as diverse as the possible functions for disclosure, and the proposals for simplification reflect that diversity. The pending bills also reflect the inevitable scars of political compromise.

It is impossible to predict, and fruitless to speculate on, the outcome of these efforts, nor is it worthwhile to dwell on specific aspects of those proposals. Suffice it to say that they contain images and shadows of virtually all the notions presented here. To be in the public interest, any ultimate "simplification" of TIL will require the lawmakers to face, honestly and forthrightly, the functions the disclosure scheme ought to and can perform. It is hoped that this analysis aids in that process.