

RECISSION UNDER THE TRUTH-IN-LENDING ACT: PROTECTING DEBTOR AND CREDITOR ALIKE

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During the post-World War II economic resurgence in America, consumer credit became readily available.¹ The increased volume of credit transactions overwhelmed many consumers with financing terms, some of which were confusing² and usurious.³ In 1968, Con-

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1. From 1950 to 1971, outstanding consumer credit rose from \$21.5 to \$137.2 billion. The National Commission on Consumer Finance report attributed the increased use of consumer credit to "the natural adaption of consumer and business to changes in the ability and willingness of consumers to incur debt, as well as to a continued shift towards the ownership of assets." NATIONAL COMMISSION ON CONSUMER FINANCE, CONSUMER CREDIT IN THE UNITED STATES 5 (1972) [hereinafter cited as CONSUMER CREDIT].

Greater urbanization of the population also led to increased dependence on credit. In 1950, over 15% of the population was rural, whereas the percentage dropped to less than 5% by 1970. Also, young married consumers tend to be heavy credit consumers and from 1950 to 1971 the number of people in the 18-to-24 age group grew from 18.6 million to 28.2 million. This more than 50% increase exceeded the 33% increase in all other age brackets.

The shift to asset ownership is evidenced by the increase in home ownership. The commission notes that credit used to acquire homes is not statistically considered as consumer credit, but adds that home ownership is accompanied by purchase of numerous durable goods, such as washing machines, refrigerators and lawn-mowers. *Id.* at 6.

2. Before the Act's passage, creditors used a variety of methods for computing finance charges. Some creditors employed a monthly rate; others based the charge on the original amount rather than on the declining balance. Creditors often informed debtors of the dollar amount without reference to the rate, and sometimes included incidental charges without explanation. H.R. REP. NO. 1040, 90th Cong., 2d Sess., reprinted in [1968] U.S. CODE CONG. & AD. NEWS 1962, 1970.

3. The concept of usury is of Biblical origin and encompassed any payment for

gress responded to the consumers' plight⁴ by enacting the Truth-in-Lending Act⁵ (TILA) to promote the informed use of credit⁶ through

the use of money. A modern definition of usury refers to "charging a rate of interest, service charge or other charge upon the loan or forbearance of any money, goods, services or things in action in excess of the rate permitted by the Constitution, statute or regulation governing the transaction." PRACTISING LAW INSTITUTE, USURY LAWS AND MODERN BUSINESS TRANSACTIONS 22 (1979).

Current state statutes set guidelines for permissible interest rates charged for the use of money. The legal interest rate, established by statute, applies to the principal if no interest rate was previously agreed upon. The contract rate, generally higher than the legal rate, determines the highest rate parties may agree upon. For a chart of state interest and usury rates, see 1 CREDIT RESEARCH CENTER, A COMPILATION OF FEDERAL AND STATE LAWS REGULATING CONSUMER FINANCIAL SERVICES 118-36 (1977).

State legislatures, however, usually pass several exceptions to the general usury rate. For example, a much higher rate of interest is allowed for small loans. In Missouri, the general usury rate is 9% per annum, MO. STAT. ANN. § 408.020 (Vernon Supp. 1980), but 2.218% per month is allowed for small loans. *Id.* § 408.100. For general discussions, see CONSUMER CREDIT, *supra* note 1, at 94-95; B. CLARK & J. FONSECA, HANDLING CONSUMER CREDIT CASES 4 (1972) [hereinafter cited as CLARK & FONSECA].

Interest rates are not always easy to calculate and various charges incident to a transaction may constitute "interest" for purposes of the usury laws. *See, e.g.*, Thrift Funds of Baton Rouge, Inc. v. Jones, 274 So. 2d 150 (La. 1973), *cert. denied*, 414 U.S. 820 (1973) (held that late charge may be interest for usury purposes). However, if parties acted in good faith without intent to violate usury laws, the general rule is that late charges are allowable. *See also* Hayes v. First Nat'l Bank of Memphis, 256 Ark. 328, 507 S.W.2d 701 (1974); H.D.S. Trading Co. v. Redisch, 19 Misc. 2d 716, 186 N.Y.S.2d 696 (Sup. Ct. Queens Co. 1959); Lew v. Goodfellow Chrysler-Plymouth, 6 Wash. App. 226, 492 P.2d 258 (1971); notes 19-20 and accompanying text *infra*.

4. Consider, for example, the case of an electrical worker who paid \$175 in 11 months on a \$123.88 television set and still owed \$182. N.Y. Times, Aug. 17, 1963, at 25, col. 5, as quoted in Note, *Truth in Lending Act: The Impossible Dream*, 22 CASE W. RES. L. REV. 89, 90 n.6 (1970).

According to the National Better Business Bureau, before TILA, home improvement frauds cost consumers \$500 million to \$1 billion annually. *Hearings on S.J. Res. 130, S. 3065 and S. 3066 Before the Senate Commerce Comm.*, 90th Cong., 2d Sess. at 75 (1968).

5. The Truth-in-Lending Act is Title I of the Consumer Credit Protection Act (CCPA), 15 U.S.C. §§ 1601-1667e (1976). Congress originally designed the Act as a disclosure measure. Subsequent amendments, however, have developed the Act's regulatory features. For example, the 1974 Fair Credit Billing amendments, 15 U.S.C. §§ 1666-1666j (1976), impose several requirements on creditors that are unrelated to disclosure. A credit card issuer cannot prohibit a merchant who honors the card from offering a discount for cash payment. *See generally* Schober, *The Development of the Truth in Lending Act in Congress and the Courts*, 3 OKLA. CITY U. L. REV. 457 (1979). There are currently nine titles in the CCPA. Title II deals with extortionate extensions of credit. Title III covers garnishment. Title IV established the Na-

meaningful disclosure of credit terms.⁷ To enforce this consumer protection legislation, Congress employed mechanisms such as administrative regulation,⁸ civil liability⁹ and criminal sanctions.¹⁰ Congress also empowered the Federal Reserve Board¹¹ to promulgate regulations¹² to effectuate the purposes of the Act.

tional Commission on Consumer Finance. Title V contains general provisions and effective dates for the other four titles. The Fair Credit Reporting Act composes Title VI. Title VII, the Equal Credit Opportunity Act, became effective on Oct. 28, 1975. Title VIII, the Fair Debt Collection Practices Act, was enacted on Sept. 20, 1977. The final title, the Electronic Fund Transfer Act, was enacted Nov. 10, 1978.

6. The Act defines "credit" as "the right granted by a creditor to a debtor to defer payment of debt or to incur debt and defer its payment." 15 U.S.C. § 1602(e) (1976). The extension of credit is available to any natural person for personal, family, household or agricultural purposes. *Id.* § 1602(h). See *Adema v. Great Northern Dev. Co.*, 374 F. Supp. 318 (N.D. Ga. 1973) (buyer of recreational property for investment is not a consumer within the meaning of the Act).

Congress exempted certain transactions in § 1603, including: credit transactions for business purposes or those to government instrumentalities; loans, other than real property transactions, exceeding \$25,000; transactions in securities or commodities by a registered broker-dealer; and transactions under public utility tariffs.

7. 15 U.S.C. § 1601 (1976).

8. Enforcing agencies are listed in *id.* § 1607(a) & (c), which designate the Federal Trade Commission as the residual enforcing agent. In 1974, Congress amended the Act, deleting the Interstate Commerce Commission and adding the Farm Credit Administration to its scheme. Act of Oct. 28, 1974, Pub. L. No. 93-495, § 403, 88 Stat. 1517.

9. Section 1640(a) provides in pertinent part:

[A]ny creditor who fails to comply with any requirement . . . with respect to any person is liable to such person in an amount equal to the sum of—

- (1) any actual damage sustained by such person as a result of the failure;
- (2)(A) in the case of an individual action twice the amount of any finance charge in connection with the transaction, . . . except that the liability under this paragraph shall not be less than \$100 nor greater than \$1,000.

10. Criminal sanctions for a creditor's wilful and knowing nondisclosure of required information or provision of false information include a fine of not more than \$5,000, or imprisonment for not more than one year, or both. *Id.* § 1611.

11. *Id.* § 1604. The Supreme Court upheld the Board's authority in *Mourning v. Family Publications Serv., Inc.*, 411 U.S. 356 (1972). See also *Strompolos v. Premium Readers Serv., Inc.*, 326 F. Supp. 1100 (N.D. Ill. 1971).

12. The Board regulations pertaining to Truth in Lending are known as Regulation Z, codified at 12 C.F.R. §§ 226.1-.15 (1980). There are some discrepancies between the Act and Regulation Z provisions. The Act requires creditors to disclose clearly and conspicuously, 15 U.S.C. § 1631 (1976), while the Regulation further provides for clear and conspicuous disclosure "in meaningful sequence." 12 C.F.R. § 226.6(a) (1980). In assessing the meaningful sequence requirement, the 7th Circuit

The Truth-in-Lending provisions include a right to rescind¹³ a consumer credit transaction that is secured by an interest¹⁴ in the debtor's residence. The consumer's right of rescission in these transactions differs from common law rescission.¹⁵ Initial judicial interpretations of the rescission section resulted in "consumer victories."¹⁶ However, a line of subsequent decisions¹⁷ modified the impact of the Truth-in-Lending legislation as amended in 1974¹⁸ and produced several pro-creditor decisions. District courts faced with the task of applying the Act's section 1640 civil remedies in light of the rescission section rendered conflicting opinions as to the sections' interrelationship.

Exercise of judicial discretion in awarding relief for Truth-in-

applied a "logical relation" test rather than an "arithmetical relation" test. *Allen v. Beneficial Fin. Co.*, 531 F.2d 797 (7th Cir. 1976), *cert. denied*, 429 U.S. 885 (1976).

The Board also issues two types of opinion letters: Official Staff Interpretations and Unofficial Staff Letters. 12 C.F.R. § 226.1(d)(4) (1980). As of mid-1978, the Act had produced 60 Official Board Interpretations, 59 Official Staff Interpretations, over 1,200 published staff opinion letters and more than 9,000 TIL lawsuits filed in federal courts. Brandl, *An Overview and Introduction to the Annual Survey of Consumer Law Development*, 34 BUS. LAW. 1401 (1979).

13. 15 U.S.C. § 1635 (1976).

14. The right of rescission "does not apply to the creation or retention of a first lien against a dwelling to finance the acquisition of that dwelling." *Id.* § 1635(e).

15. See notes 48-53 and accompanying text *infra*.

16. See Paer, *Truth-in-Lending: Protection for the Consumer or for the Creditor?*, 24 EMORY L.J. 357 (1975). Among the early "consumer victories" Paer discusses are *Grubb v. Oliver Enterprises, Inc.*, 358 F. Supp. 970 (N.D. Ga. 1972) (first Truth-in-Lending judgment to award significant attorney's fees); *Buford v. American Fin. Co.*, 333 F. Supp. 1243 (N.D. Ga. 1971) (failure to disclose \$1 notary fee violated Act); *Ratner v. Chemical Bank New York Trust Co.*, 329 F. Supp. 270 (S.D.N.Y. 1971) (actual imposition of finance charge is irrelevant for civil liability).

17. "In the early part of 1974 the pendulum began to swing in favor of the creditor. The Federal Reserve Board, as well as a number of courts, apparently began to feel they had gone far enough and perhaps too far in protecting the consumer: they decided to retreat." Paer, *supra* note 16, at 364-65.

18. Pub. L. No. 93-495, §§ 406-408(d), 88 Stat. 1518 (1974). Proposed legislation to reform the Truth-in-Lending Law has received recent Congressional attention. On May 1, 1979, the Senate passed Senator Proxmire's bill, S. 108. The purpose of S. 108, entitled the Truth-in-Lending Simplification and Reform Act, is "to facilitate compliance by simplifying the requirements imposed under that Act, [and] to facilitate administrative enforcement." S. 108, 96th Cong. 1st Sess. (1979).

The House passed a similar bill, H.R. 4986. As of May 1, 1980, however, Congress had taken no further action to reform the Truth-in-Lending laws. For a discussion of S. 108's effect on current legislation, see CONSUMER CREDIT 1980 (PLI), *Commercial Law & Practice*.

Lending disclosure violations transforms litigation into a guessing game for creditors and debtors. This note will describe TILA's debtor remedies, examine the judicial approaches to these sections and evaluate the concurrent availability of rescission and civil liability. This analysis of the courts' current rationales may aid the attorney in assessing his debtor-client's position in seeking relief under Truth-in-Lending. After an overview, this note recommends incorporation of the debtor's obligation into the judgment as consistent with the Congressional intent of protecting consumers without inequitably penalizing creditors.

I. BACKGROUND

Prior to Truth-in-Lending, consumer credit protection consisted primarily of small loan legislation¹⁹ and usury laws.²⁰ The former set standards for those licensed in the small loan industry; usury laws limited the amount of interest allowed for the use of money. The scope of these measures, however, was narrow and did not encompass credit sales of goods.²¹ The rationale was that merchants who sold on credit were not lenders²² since cash paid over a period of time was not worth as much as the total price at the time of purchase. Under this theory, merchants, allowed to increase the price of the goods to account for the difference between the time-purchase price and the cash price, were not considered to be assessing an interest charge.²³ As consumer credit purchases increased, states responded

19. All states except Arkansas have enacted small loan laws to protect prospective borrowers from loan-sharking. Under these acts, a state agency is authorized to license lenders and supervise their activities. B. CURRAN, *TRENDS IN CONSUMER CREDIT TRANSACTIONS* 16 (1965) [hereinafter cited as CURRAN]. See generally R. NUGENT & L. ROBINSON, *REGULATION OF THE SMALL LOAN BUSINESS* (1935).

20. See generally CURRAN, *supra* note 19, at 15.

21. See Note, *supra* note 4, at 95.

22. The Supreme Court in *Hogg v. Ruffner*, 66 U.S. (1 Black) 115, 118-19 (1861), stated:

But it is manifest that if A propose to sell to B a tract of land for \$10,000 in cash, or for \$20,000 payable in ten annual instalments, and if B prefers to pay the larger sum to gain time, the contract cannot be called usurious. A vendor may prefer \$100 in hand to double the sum in expectancy, and a purchaser may prefer the greater price with the longer credit. . . . Such a contract has none of the characteristics of usury; it is not for the loan of money, or forbearance of a debt.

23. CURRAN, *supra* note 19, at 13. See also Note, *supra* note 4, at 95.

with retail installment sales acts.²⁴ These acts included disclosure provisions similar to truth-in-lending requirements. The Truth-in-Lending Act was a federal attempt to integrate the various earlier legislative acts and cover all consumer credit transactions.

A. *Legislative History*

Both houses of Congress introduced consumer protection bills in early 1960²⁵ with a stated purpose of assuring 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."²⁶ The Act, passed several years after these

24. See generally Hogan, *A Survey of State Retail Instalment Sales Legislation*, 44 CORNELL L.Q. 38 (1958).

25. Senator Paul Douglas (D. Ill.) introduced the "Consumer Credit Labeling" bill on January 7, 1960. S. 2755, 86th Cong., 2d Sess., 106 CONG. REC. 95, 97 (1960). "The purpose of the bill is to require lenders and vendors to tell the truth about interest rates and finance charges" and thus achieve economic stabilization. *Id.* at 97. The bill required disclosure of the total amount of finance charges and the percentage that amount bears to the outstanding balance in terms of simple annual interest. *Id.* (remarks of Senator Douglas). However, the bill was never voted out of the subcommittee. See, Schober, *supra* note 5, at 457-58 (1979).

On April 27, 1961, Senator Douglas introduced another bill, entitled the Truth in Lending Act. This second attempt was more expansive in scope. Schober, *supra*, at 459. S. 1740, 87th Cong., 1st Sess., 107 CONG. REC. 6778 (1961). Section 4 of this bill required the following disclosures:

- (1) the cash price or delivered price of the property or service to be acquired;
- (2) the amounts, if any, to be credited as down payment and/or trade-in;
- (3) the difference between the amounts set forth under clauses (1) and (2);
- (4) the charges, individually itemized, which are paid or to be paid by such person in connection with the transaction but which are not incident to the extension of credit;
- (5) the total amount to be financed;
- (6) the finance charge expressed in terms of dollars and cents; and
- (7) the percentage that the finance charge bears to the total amount to be financed expressed as a simple annual rate on the outstanding unpaid balance of the obligation.

Id. at 6853 (remarks of Sen. Douglas). After extensive hearings, this bill also failed to clear the subcommittee.

26. 15 U.S.C. § 1601 (1976). The Truth-in-Lending Act's disclosure requirement serves a descriptive function and a shopping function, thus allowing a consumer to choose in a credit transaction between any available source and his own resources. See Comment, *Private Remedies Under the Truth-in-Lending Act: The Relationship Between Rescission and Civil Liability*, 57 IOWA L. REV. 199 (1971). For a discussion of the Act's functions and the effectiveness of the disclosure requirement, see CONSUMER CREDIT, *supra* note 1, at 171-91. In this 1972 report, the National Commission on Consumer Finance concluded that the Act had been less effective in effecting the

initial attempts, regulates open-end credit where the consumer receives credit or goods on credit and the cost of credit is based on the outstanding unpaid balance as computed at periodic intervals.²⁷ This provision encompasses revolving charge accounts and institutional credit card and check credit plans. In these open-end situations, the creditor must furnish disclosures before the first transactions.

Other forms of consumer transactions, such as retail installment sales and installment loans, utilize closed-end credit.²⁸ These involve the extension of a fixed amount of credit determined at the transaction's outset and repayable in a specified number of installments at a predesignated amount. The Act requires closed-end credit disclosures to precede the transaction's consummation.²⁹

The Act in its final form resulted from much compromise.³⁰ Originally, neither the Senate nor the House bill mentioned rescission. The Senate bill, however, did provide a civil remedy.³¹ During de-

descriptive and economic stabilization functions than it had in effecting the shopping function. *Id.* at 191.

27. 15 U.S.C. § 1602(i) (1976); 12 C.F.R. § 226.2(x) (1980).

28. Closed-end credit is also known as "other than open-end" credit. 15 U.S.C. § 1638 (1976). This note focuses on closed-end transactions. A creditor must disclose finance charges as defined under Regulation Z. 12 C.F.R. § 226.4 (1980). Disclosure must also inform the consumer of the date on which the finance charge begins to accrue. *Id.* § 226.8(b)(1). Compliance with TILA also requires disclosure of the annual percentage rate, *id.* § 226.8(b)(2); repayment schedule and total, *id.* § 226.8(b)(3); default and late charges, *id.* § 226.8(b)(4), and any security interest, *id.* § 226.8(b)(5). A recent survey of consumer law development noted that reported cases indicate compliance with open-end disclosure requirements is less troublesome than compliance with closed-end provisions. Miller, *Truth in Lending Act*, 34 BUS. LAW. 1405 (1979).

29. For a discussion of open-end and closed-end credit, see Feldman, *A Review of the Provisions of Federal Statutes and Implementing Regulations in the Field of Consumer Credit*, 3 OKLA. CITY U. L. REV. 477 (1979).

30. See Schober, *supra* note 5, who explains:

There was a little something for almost everyone. Retailers wanted open-end credit excluded. It was not, but open-end creditors were given the right to make the optional disclosure of the "average effective annual percentage rate of return" on open-end accounts. The real estate industry wanted first mortgages exempted completely. They were not, but the disclosure of the amount of the finance charge was not required in first purchase money real property transactions. Proponents of states' rights wanted a broad exclusion for states with similar laws. They did not get it, but the Federal Reserve Board was given authority to grant exemptions to states with "substantially similar" laws where there was "adequate provision for enforcement."

Id. at 459-60.

31. See S. 2755, 86th Cong., 2d Sess. (1960).

The intent of the Senate was unequivocal. The Act was to be enforced solely by

bate in the House, Representative Cahill sponsored an amendment³² requiring disclosure in a three-day period prior to execution of the contract. A conference committee³³ replaced without explanation³⁴ the three-day notice before execution provision with the present three-day right of rescission. Congress thus adopted the Truth-in-Lending Act in a form that reflects both Senate concern with civil enforcement and House emphasis on administrative enforcement.

B. *Statutory Provisions*

1. Rescission: Subsection 1635(a)

The right of rescission under subsection 1635(a) applies to consumer credit transactions³⁵ where the creditor obtains a security in-

consumers through private suits for a civil penalty which would secure substantial compliance with the Act. The House expressed itself with equal clarity; voicing concern for the unsophisticated consumer of modest means for whom recourse to civil litigation or the Attorney General was unrealistic, it announced that administrative enforcement would be fundamental to the purpose of the Act.

Note, *Truth in Lending Act Litigation: Concurrent Recourse to Rescission and the Civil Penalty*, 43 GEO. WASH. L. REV. 840, 842 (1975). See H.R. REP. NO. 1040, 90th Cong., 1st Sess. 9 (1967); S. REP. NO. 392, 90th Cong., 1st Sess. 9 (1967); 113 CONG. REC. 18,401-02 (1967) (remarks of Sen. Proxmire); 113 CONG. REC. 18,412 (1967) (remarks of Sen. Bennett). See also *Hearings on H.R. 11601 before the Subcomm. on Consumer Affairs of the House Comm. on Banking & Currency*, 90th Cong., 1st Sess., pt. 2, at 828 (1967). 114 CONG. REC. 14,486-87 (1968) (remarks of Sen. Proxmire).

32. H.R. 11601, § 203(e), 90th Cong., 2d Sess. (1968).

33. S. REP. NO. 392, 90th Cong., 1st Sess. (1967).

34. The House managers compelled a vote before debate during the passage of the conference report, thus accounting for the lack of legislative history. 114 CONG. REC. 14,486-93 (1968). There is some indication, however, that the inclusion of the rescission provision stemmed from congressional concern regarding abuses in the home-improvement and second-mortgage industry. 114 CONG. REC. 1611 (1968) (remarks of Rep. Cahill).

35. Consumer credit transactions usually consist of consumer loans and credit sales. For a general discussion, see S. MORGANSTERN, *LEGAL REGULATION OF CONSUMER CREDIT* (1972). Regulation Z, 12 C.F.R. § 226.3 (1980) governs the exempted transactions.

Credit must be extended by a "creditor" as defined by 12 C.F.R. § 226.2(s) (1980). A creditor is one who in the ordinary course of business extends or arranges the extension of consumer credit or offers to extend or arrange such credit, which is payable in more than four installments. See *Manning v. Princeton Consumer Discount Co.*, 533 F.2d 102 (3d Cir. 1976), cert. denied, 429 U.S. 865, rehearing denied, 429 U.S. 933 (1976) (automobile dealer receiving a commission for referring a customer to a financing agency is a creditor); *James v. Ragin*, 432 F. Supp. 887 (W.D. N.C. 1977) (extension of credit ten times in five years in not "isolated and incidental extension of credit"). There must be a finance charge connected with the transaction. For speci-

terest³⁶ on the debtor's primary residence.³⁷ Section 226.9(b) of Regulation Z requires the creditor³⁸ to provide the customer with no-

fied purposes, the term "creditor" refers to credit card issuers and those persons who honor cards. 12 C.F.R. § 226.2(s) (1980). See generally Case Note, *Consumer Protection—Truth in Lending Act—"Creditor"—Definition and Election of Remedies*, 21 WAYNE L. REV. 977 (1975).

36. As defined by the regulations:

'Security interest' and 'security' mean any interest in property which secures payment or performance of an obligation. The terms include, but are not limited to, security interests under the Uniform Commercial Code, real property mortgages, deeds of trust, and other consensual or confessed liens whether or not recorded, mechanic's, materialmen's, artisan's, and other similar liens, vendor's liens in both real and personal property, the interest of a seller in a contract for the sale of real property, any lien on property arising by operation of law, and any interest in a lease when used to secure payment or performance of an obligation.

12 C.F.R. § 226.2(gg) (1980). See *N.C. Freed Co. v. Board of Governors*, 473 F.2d 1210 (2d Cir. 1972) (meaningful disclosure must include the statutory liens and treat them uniformly under the Act). But see *Meyers v. Clearview Dodge Sales, Inc.*, 539 F.2d 511 (5th Cir. 1976), cert. denied, 431 U.S. 929 (1977); *Mims v. Dixie Fin. Corp.*, 426 F. Supp. 627 (N.D. Ga. 1976) (assignment and waiver of homestead does not create a security interest).

Prior to the TILA's enactment, most creditors took a security interest in the form of a cognovit note. The note's terms entitled the creditor to a judgment without notice to the debtor and could award him a judgment lien on the debtor's principal residence. Thus, such a credit transaction could result in the loss of the obligor's home. S. MORGANSTERN, *LEGAL REGULATION OF CONSUMER CREDIT* 16-17 (1972).

Mechanic's and materialman's liens can come under the TILA's rescission provision in a single payment transaction, even though a finance charge is not conspicuously imposed. "If a plumber or a materialman offers a discount for prompt payment, he is imposing a finance charge under Regulation Z § 226.8(o), and the transaction is subject to rescission even though he does not record his lien." Abraham, *Some Rescission Problems in Truth-in-Lending*, 87 BANKING L.J. 867, 869 (1970).

One commentator considers the mechanic's lien "insidious because, unlike the consensual lien . . . the mechanic's lien (in those states in which it arises by operation of law) requires no affirmative act on the part of the customer and little or nothing on the part of the creditor." Burstein, *There's Truth in Lending, But is There Right in Rescission?* 2 REAL EST. REV. 83, 84 (1972).

37. Thus, if a consumer has more than one residence, the Act does not cover any transactions involving liens on secondary abodes. For examples, the rescission provision is inapplicable where a vacation home is concerned. The staff members of the Federal Reserve Board have expressed the opinion that transactions involving a vacant lot on which a debtor expects to build his primary residence are rescindable. However, Burstein disagrees because the consumer does not need the protection of the right of rescission since "the roof over his head" is not jeopardized. Burstein, *supra* note 36, at 86.

38. See note 35 *supra*. The Act also provides for the involvement of more than one creditor in a transaction. 12 C.F.R. § 226.6(d) (1980).

rice³⁹ of this right; the regulations even specify the typeface size required for such notice.⁴⁰ If a creditor receives the customer's signed acknowledgment of receipt of required disclosures, a rebuttable presumption of delivery arises.⁴¹ Creditors must delay performance until satisfied that proper disclosure has been made and the customer has chosen not to exercise his rescission right.⁴²

The obligor has until midnight of the third business day⁴³ after the consummation of the transaction or following the delivery of all required disclosures⁴⁴ in which to notify the creditor of his intention to

39. The creditor must furnish the customer with two copies of the notice of opportunity to rescind and the customer can use one copy to cancel the transaction. *Id.* § 226.9(b) (1980). In a case involving multiple obligors, the court in *Gerasta v. Hibernia Nat'l Bank*, 411 F. Supp. 176 (E.D. La. 1976), *modified*, 575 F.2d 580 (5th Cir. 1978), held that the creditor was liable for disclosures to only one of two property owners. Reg. Z § 226.6(e)'s allowance of disclosure only to the primary customer does not apply to transactions that can be rescinded.

The requirement of notice of the rescission right relates to TILA's purpose of allowing consumers to compare. *See James v. Home Const. Co.*, 458 F. Supp. 54 (S.D. Ala. 1978) (Act does not require extension to successor obligor; plaintiff, administrator of his mother's estate, not allowed to rescind on home-improvement contract).

40. The print must be not less than 12-point bold-faced type. 12 C.F.R. § 226.9(b) (1980).

41. 15 U.S.C. § 1635(c) (1976).

42. 12 C.F.R. § 226.9(c) (1980). Creditors may not:

- 1) Disburse any money other than in escrow;
- 2) Make any physical changes in the property of the customer;
- 3) Perform any work or service for the customer; or
- 4) Make any deliveries to the residence of the customer if the creditor has retained or will acquire a security interest other than one arising by operation of law.

43. A business day is any calendar day except Sunday and the following legal holidays: New Year's Day, Washington's Birthday, Memorial Day, Independence Day, Labor Day, Columbus Day, Veteran's Day, Thanksgiving Day and Christmas Day. 12 C.F.R. § 226.9(a) n.14 (1980).

44. Essentially there are two identifiable three-day periods under the Act. The first one is the three-day period following the transaction's consummation which serves as a "cooling-off" period. This grants relief to consumers that have fallen prey to high-pressure sales tactics. *Boyd, The Federal Consumer Credit Protection Act—A Consumer Perspective*, 45 NOTRE DAME LAW. 171, 188 (1970).

The second period in which a debtor may rescind arises from the creditor's failure to disclose. This right to rescind may be seen as a continuing one if the disclosures remain deficient. *Ljepava v. M.L.S.C. Prop., Inc.*, 511 F.2d 935, 944 (9th Cir. 1975). *See also Sosa v. Fite*, 498 F.2d 114, 118 (5th Cir. 1974); *Wachtel v. West*, 476 F.2d 1062 (5th Cir. 1973). However, the regulations provide that the right to rescind expires either three years after the transaction's consummation, or on the date the customer transfers away the property, whichever occurs first. 15 U.S.C. § 1635(f) (1976);

rescind.⁴⁵ The obligor can only modify or waive the right to rescind in two situations. These exceptions apply when credit is needed to meet a "bona fide immediate personal emergency of the customer"⁴⁶ or when a three-day delay "will jeopardize the welfare, health or safety of natural persons or endanger property which the customer owns or for which he is responsible."⁴⁷

2. Common Law Rescission and Subsection 1635(b)

Generally, a wrong gives rise to several coexisting remedial rights. At common law, the injured party had to elect one remedy. Alternative remedies were deemed inconsistent.⁴⁸ Thus, a party to a contract had to choose between suing for damages or seeking rescission since the former affirmed the contract and the latter avoided it.⁴⁹ Theoretically, this election doctrine prevented a plaintiff's double recovery.

A party electing rescission⁵⁰ must act consistently with the remedial goal of placing parties in the positions they would have been in if the contract had not been executed. Common law required that the plaintiff notify the other party of his intention not to be bound by the

12 C.F.R. § 226.9(h) (1980). See Note, *Truth-in-Lending: Judicial Modification of the Right of Rescission*, 1974 DUKE L.J. 1227, 1233 n.31.

45. The rescinding consumer must notify the creditor by mail or telegram or other writing expressing his intention to rescind. 12 C.F.R. § 226.9(a) (1980). The debtor need not state his reason for exercising his right of rescission. See Griffith, *Truth-in-Lending: Some Aspects*, 26 DEPAUL L. REV. 566, 588 (1977).

46. 12 C.F.R. § 226.9(e)(1) (1980). See *Ljepava v. M.L.S.C. Prop., Inc.*, 511 F.2d 935, 944 (9th Cir. 1975) (holding waiver ineffective because no "bona fide emergency" existed since lenders knew from title they had ordered that no foreclosure was imminent). For a discussion of *Ljepava*, see Note, *The Truth in Lending Act: A Summary of Consumer's Remedies*, 22 S.D. L. REV. 322, 334 (1977).

47. 12 C.F.R. § 226.9(e)(2) (1980). The customer must give the creditor a separate dated and signed statement describing the situation that necessitates the modifying or waiving of the rescission right. *Id.* § 226.9(e)(3).

48. One policy argument is that election of remedies prevents vexatious litigation and supports the view that a litigant should not hold inconsistent positions. See generally Dobbs, *Pressing Problems for the Plaintiff's Lawyer in Rescission: Election of Remedies and Restoration of Consideration*, 26 ARK. L. REV. 322, 325 (1972).

49. Dobbs, *supra* note 48 at 328. See *Eastburn v. Galyen*, 313 S.W.2d 794 (Ark. 1958); *Lee, Executrix v. Erickson*, 226 Ark. 442, 291 S.W.2d 238 (1956).

50. The term "rescission" refers to both rescission at law and the equitable remedy of cancellation. The scope of this note encompasses only the former. Plaintiffs may, however, resort to equity courts for rescission. Dobbs, *supra* note 48, at 343.

Under the latter procedure, the plaintiff seeks a court's decree of equity, thus eliminating the consumer's need to guess about his legal rights. Dobbs, *supra*, at 343.

contract. The rescinding party also had to restore or offer to restore whatever consideration he received pursuant to the bargained-for agreement.⁵¹ The tender of restoration is closely related to the election issue, because the debtor's failure to return or attempt to return the consideration may be perceived as a decision to retain the contract.⁵²

By enacting the Truth-in-Lending Act, Congress modified common law rescission to afford consumers a private means of enforcement.⁵³ Under section 1635, once the borrower exercises his right to rescind, he is no longer liable for any finance charges and any security interest becomes void.⁵⁴ Within ten days of notification, the creditor must return any money or property and take any action necessary "to reflect termination of any security interest created under the transaction."⁵⁵ Only after the creditor's performance must the debtor tender⁵⁶ any consideration received or its reasonable value. Upon the creditor's failure to take possession of the consideration, the property vests in the customer without obligation to pay.⁵⁷ The Act protects consumers by requiring creditors to initiate action and by creating the possibility of a consumer windfall.

3. Civil Liability: Section 1640

Congress provided a second private enforcement mechanism for consumers through section 1640's imposition of civil liability for creditor nondisclosure of required information.⁵⁸ The aggrieved debtor is entitled to any "actual damages"⁵⁹ upon bringing an action within one year of the violation.⁶⁰ Many errors or nondisclosures,

51. S. WILLISTON, CONTRACTS § 1454, at 10 (3d ed. 1970).

52. Dobbs, *supra* note 48, at 325.

53. "The Truth in Lending Act provides the consumer with a new substantive basis for voiding a credit agreement and reorders the sequence of rescission and tender." Note, *supra* note 44, at 1231.

54. 12 C.F.R. § 226.9(d) (1980).

55. *Id.*

56. 15 U.S.C. § 1635(b) (1976).

57. *Id.*

58. *Id.* § 1640. S. 108, discussed in note 18 *supra*, would limit civil liability and class action exposure to violations of 15 U.S.C. §§ 1635, 1637(a), (b)(4-10), and 1638(a)(2), (3), (4), (5), (6) or (9).

59. 15 U.S.C. § 1640(a)(1) (1976).

60. *Id.* § 1640(e).

Any action under this section may be brought in any United States district court,

however, do not involve actual damages.⁶¹ For example, a creditor's nondisclosure of a default charge⁶² does not cause the non-defaulting debtor pecuniary harm. Additionally, actual damages present problems of proof and calculation.⁶³

Second, the nondisclosing creditor may also be liable for a penalty of twice the transaction's finance charge. The minimum penalty in such cases is one hundred dollars, the maximum one thousand dollars.⁶⁴ As amended,⁶⁵ section 1640 also provides for class action damages, subject only to a maximum recovery.⁶⁶ Awarding litigation costs and reasonable attorney's fees also encourages consumer action.⁶⁷

or in any other court of competent jurisdiction, within one year from the date of the occurrence of the violation.

Id.

61. S. REP. NO. 278, 93d Cong., 1st Sess. 3 (1973); Alop & Rosenberg, *Remedies Under the Truth-in-Lending Act: Selected Issues*, 60 CHIC. B. REC. 40, 41 (1978).

62. 15 U.S.C. § 1638(a)(9) (1976).

63. The ease of calculating actual damages varies with the nature of the specific violation involved. For example, if a change is understated rather than omitted, "it would be fitting to hold that payments in excess of disclosed amounts are actual damages." Alop and Rosenberg, *supra* note 61, at 42.

Generally, the burden of proof is on the debtor asserting injury under the Act. *See Grandway Credit Corp. v. Brown*, 295 So.2d 714 (Fla. 1974). The court in *Burrell v. City Dodge, Inc.*, 5 CONS. CRED. GUIDE (CCH) ¶ 98,764 (N.D. Ga., June 21, 1974) set the standard of proof of actual damages:

If a consumer is damaged as the result of a violation of the (Truth in Lending) Act, his damages presumably would be measured by the difference between the cost of alternative credit which he may have chosen had the terms of the credit been fully disclosed and the cost of the credit extended.

Id. at ¶ 88,391.

64. 15 U.S.C. § 1640(a)(2)(A) (1976). Plaintiff may bring an action under this subsection without a showing of financial loss. *Dzadovsky v. Lyons Ford Sales, Inc.*, 593 F.2d 538 (3d Cir. 1979).

65. Pub. L. No. 93-495, §§ 406-408(d), 88 Stat. 1518 (1974). The 1974 amendment of § 1640 reflects Congressional awareness of judicial reluctance to certify class actions. *See Fischer, From Rattner to Qui Tam: Truth-in-Lending Class Action Developments*, 24 HASTINGS L.J. 813, 833-35 (1973).

66. 15 U.S.C. § 1640(a)(2)(B) (1976) ("the total recovery . . . shall not be more than the lesser of \$500,000 or 1 per centum of the net worth of the creditors").

67. *Id.* § 1640(a)(3). Courts usually determine reasonable attorney's fees. *Thomas v. Myers-Dickson Furniture Co.*, 479 F.2d 740, 748 (5th Cir. 1973). *See also Hannon v. Security Nat'l Bank*, 537 F.2d 327 (9th Cir. 1976) (unlicensed law school graduate who represented himself not awarded attorney's fees); *Manning v. Princeton Consumer Discount Co., Inc.*, 533 F.2d 102 (3d Cir. 1976), *cert. denied*, 429 U.S. 865 (1976). The *Hannon* court held that the purpose of awarding attorney's fees was "to

Although Congress drafted section 1640 to deter and punish violations, that provision also recognizes the possibility of harsh results and attempts to prevent inequities. Thus, a creditor can avoid section 1640 liability by notifying the concerned debtor of the error and making any appropriate adjustments within fifteen days of discovery and before institution of any action.⁶⁸ The Act also prohibits recovery based on unintentional bona fide errors.⁶⁹ No liability is imposed for good faith compliance with any rule, regulation, or Federal Reserve Board interpretation.⁷⁰ Anticipation of consumer windfalls also prompted restricting recovery for multiple nondisclosures. Multiple failures to disclose in a single credit transaction only give rise to a single award.⁷¹

II. RELATIONSHIP BETWEEN SECTION 1635 AND SECTION 1640

Since the Truth-in-Lending Act's passage, the issue of whether or not a consumer can bring an action for both rescission and civil damages has arisen frequently.⁷² A reading of the legislative history does

make a litigant whole and to facilitate private enforcement of the Truth in Lending Act." 537 F.2d at 328.

68. 15 U.S.C. § 1640(b) (1976). S. 108 § 8(b)(6) would amend the Act to require disclosure within 60 days of discovery. See note 18 *supra*.

69. 15 U.S.C. § 1640(c) (1976). By a preponderance of evidence the creditor must show that the violation was not intentional and resulted "notwithstanding the maintenance of procedures reasonably adapted to avoid any such error." *Id.* The court in *Haynes v. Logan Furniture Mart, Inc.*, 503 F.2d 1161 (7th Cir. 1974), reasoned that requiring consumers to prove creditors intentionally violated the Act would produce a hollow remedy for consumers. *Id.* at 1166. The court held that voluntary and deliberate acts and omissions were intentional. *Id. Contra*, *Welmaker v. W.T. Grant Co.*, 365 F. Supp. 531 (N.D. Ga. 1972) (credit provisions of department store's coupon-book plan violate TILA, but court held defendants did not intend to violate and had made good-faith errors, so liability would result in "manifest injustice"). See also Comment, *Truth-in-Lending—Standing—Statutory Recovery Available Despite Absence of Actual Injury Since Statute Defines Injury in Fact*, 47 Miss. L.J. 560, 566 (1976) (unintentional violation defense could have curbed suits motivated by grudge against creditor but it has generally been read out of the statute by the courts).

70. 15 U.S.C. § 1640(f) (1976). For a discussion of the good-faith defense, see Paer, *Truth-in-Lending*, *supra* note 16. "Restricting the good faith defense is extremely important to private enforcement for otherwise the plaintiff's attorney cannot gauge the strength of his case prior to engaging in expensive discovery." *Id.* at 367.

71. 15 U.S.C. § 1640(g) (1976). However, continued failure to disclose after a recovery has been granted gives rise to rights to additional recoveries. *Id.*

72. See generally Comment, *supra* note 26. "The Act does not indicate whether rescission and civil liability are inconsistent and thus mutually exclusive remedies, or

little to clarify the interrelationship of the two sections.⁷³ Courts must therefore interpret the Act's provisions according to their view of its legislative purpose. Courts that regard the Truth-in-Lending Act as remedial in nature consider the Congressional goal to be restoration of the parties. Other decisions, however, stress that Congress designed the penal provisions of the Act to ensure creditor compliance.⁷⁴

A. *Judicial Interpretations*

The district court in *Bostwick v. Cohen*⁷⁵ was the first to evaluate the concurrent availability of rescission and civil damages. The *Bostwick* court held that the traditional election of remedies doctrine⁷⁶ was applicable to the Act's provisions. As such, the plaintiff waived her right to civil damages by exercising her right to rescind.⁷⁷ The court relied on the principle that the common law should not be superseded unless a statute clearly intends that result.⁷⁸

The *Bostwick* court classified the civil liability section as remedial rather than punitive. According to this rationale, once rescission is granted, the debtor is afforded a remedy and the parties are restored to their previous status. In addition, the court in *Bostwick* found that the rescinding consumer is not within the class of persons which the civil liability section is deemed to protect. The Act seeks to protect the "aggrieved debtor,"⁷⁹ and the *Bostwick* court held that a con-

essentially complimentary, and therefore, to be treated as conjunctive recourses." *Id.* at 203.

73. The mutual exclusivity of the sections is important only in certain circumstances. It is only an issue when a security interest is taken on the debtor's home and there is a violation of the disclosure requirements. This violation is subject to a one-year statute of limitations as provided in § 1640. See Note, *supra* note 31, at 843.

74. Note, *supra* note 31, at 859 (§ 1640 acts primarily as a penalty for enforcement; compensation is a secondary function).

75. 319 F. Supp. 875 (N.D. Ohio 1970) (plaintiff sought statutory damages for defendants' alleged failure to make required disclosures in connection with a credit agreement for installation of a swimming pool).

76. See notes 48-49 and accompanying text *supra*.

77. 319 F. Supp. at 877.

78. *Id.* Generally in the absence of a clear intention, a statute should not supersede common law. 3 J. SUTHERLAND, STATUTES & STATUTORY CONSTRUCTION § 6201 at 164-65 (3d ed. 1943).

79. 319 F. Supp. at 878 n.1. See Case Note, *supra* note 35, at 986.

sumer allowed to rescind does not suffer an injury since the creditor can no longer impose a finance charge.

Most courts disagree with *Bostwick* and allow conjunctive relief in certain situations. The Supreme Court in 1973 set forth a liberal interpretation of the Act. In *Mourning v. Family Publications Service, Inc.*,⁸⁰ the consumer-client defaulted on a five-year magazine subscription contract that provided inadequate credit information. The Court stated that the Act demonstrated a legislative policy change from *caveat emptor* to "[l]et the seller disclose."⁸¹ Congress sought to achieve this change "[b]y erecting a barrier between the seller and the prospective purchaser in the form of hard facts."⁸²

The *Mourning* court rejected the argument advanced in *Bostwick* that lack of a finance charge prevented imposition of a civil penalty.⁸³ It did add, however, that the minimum sanction would be appropriate in such cases.⁸⁴ A New York district court partially followed this reasoning in *Ratner v. Chemical Bank New York Trust Co.*⁸⁵ *Ratner*

80. 411 U.S. 356 (1973). Plaintiff, a 73-year-old widow, sought to recover statutory penalty and costs for defendant's failure to reveal the total amount due, the unpaid balance or the service and finance charges with respect to a five-year magazine subscription. The signed contract stated that plaintiff could not cancel and provided for acceleration of the entire balance due upon any default.

81. *Id.* at 377.

82. *Id.*

83. The court upheld the Board's use of the "more-than-four-installment" rule, which extended the coverage of the Act to any transaction that was payable in more than four installments. 12 C.F.R. § 226.2(k) (1972). The rule was to prevent creditors from burying finance charges in seemingly cost-free arrangements. Even if such a service is "free" to consumers, it is obviously costing the creditors something and this would probably result in higher prices. See CONSUMER CREDIT, *supra* note 1, at 184-85; Clontz, *The Contract*, in CONSUMER CREDIT 1976: THE ANATOMY OF THE CREDIT TRANSACTION 99, 107 (1976).

84. 411 U.S. at 376.

85. 329 F. Supp. 270 (S.D. N.Y. 1971) (bank was held liable for failing to disclose the nominal annual percentage rate in monthly billings to customers who had outstanding balances, but who had incurred no finance charges). *Ratner* is most noted for its holding on class action suits regarding Truth-in-Lending. The *Ratner* court held that a suit for violation of Truth-in-Lending could not be maintained as a class action. The court's rationale was that since the Act provided civil penalties under § 1640, each consumer could act as his own "private attorney general" and thus the incentive of a class action remedy was not necessary. The court also foresaw the potentially devastating effect on creditors of a recovery by a large group of class members. See also *Haynes v. Logan Furniture Mart, Inc.*, 503 F.2d 1161 (7th Cir. 1974) (Congress must have realized class actions were part of the existing body of law prior to Act's passage and did not expressly or impliedly exclude their use).

held that incurring or paying a finance charge was irrelevant in determining section 1640 liability. That liability, the court said, was based upon the creditor's failure to disclose as required by the Act.⁸⁶ The *Ratner* court agreed with *Bostwick* and deemed section 1640 remedial, but in dictum went beyond *Bostwick* by characterizing section 1640 as a liquidated damages provision.⁸⁷

B. *Analysis of the Relationship Between Section 1635 and Section 1640*

Characterizing the Act's overall function as penal rather than remedial supports the availability of conjunctive relief. The *Bostwick* and *Ratner* view of section 1640 as a strictly remedial provision is susceptible to much criticism. First, subsection 1640(a)(1) provides for guaranteed minimum relief, while at the same time imposing a limit on creditor liability. This is inconsistent with a remedial view of the provision, since actual damages⁸⁸ would be the best measure of liability for remedial purposes. One analysis of the Act has put this another way: The lack of a relationship between the extent of liability and the injury involved suggests that compensation is not a primary statutory purpose.⁸⁹

Second, Congress provides a bona fide error defense in subsection 1640(2)(c), which excuses unintentional bona fide errors by creditors.⁹⁰ This also indicates the section's penal nature. The intent element would be irrelevant if Congress intended a strictly compensatory remedy. Courts recognizing these penal elements may be more willing to award civil penalties in conjunction with remedial measures.

In enforcing the Act, some courts also examine equitable factors⁹¹ and thus apply judicial discretion.⁹² In using this "discretionist"⁹³

86. For a discussion of *Ratner*, see Note, *supra* note 31, at 848-49.

87. *Id.* at 849.

88. See 15 U.S.C. § 1640(a)(2)(A) (1976). Congress added the language pertaining to actual damages in the 1974 amendments. Pub. L. No. 93-495, §§ 406-408(d), 88 Stat. 1518 (1974). See note 59 and accompanying text *supra*.

89. Note, *supra* note 31, at 854.

90. 15 U.S.C. § 1640(c) (1976). See note 69 and accompanying text *supra*.

91. The Supreme Court stated that "it would not be construction but legislation to restrict the meaning of the statute in accord with narrower legislation in other states, because in the judgment of a court it might be equitable to do so." *Holden v. Stratton*, 198 U.S. 202, 210 (1905).

92. The propriety of such discretion "of course will depend on the equities present

approach to section 1635, a court may balance certain factors such as:

(1) whether the creditor asserted a good faith defense to the borrower's act of rescission; (2) of what significance the creditor's violation would be to a reasonable consumer, comparison-shopping for credit; (3) whether the borrower indicated either willingness or ability to repay the loan proceeds; and (4) whether other means of enforcing creditor compliance are available.⁹⁴

Avoiding a literal reading of section 1635, some courts condition an award of rescission upon the debtor's tender of consideration. The court in *Palmer v. Wilson*⁹⁵ recognized that the Act abolished the debtor's tender as a prerequisite to rescission, yet still upheld the court's equitable powers to require tender. The *Palmer* holding reflects judicial fear that a literal application of TILA will too harshly and inequitably penalize creditors.⁹⁶ Congressional failure in the 1974 amendments to contradict the courts' use of the discretionary approach indirectly lends legislative support to this judicial trend.

III. VARIETIES OF AVAILABLE CONSUMER RELIEF

Acknowledging the evolution of Truth-in-Lending judgments toward decisions favoring creditors,⁹⁷ this section assesses the relief available to consumers. To consider a typical situation, consumers often contract for home-improvement work. The parties to such a contract may agree to monthly installment payments that cover the

in a particular case, as well as consideration of the legislative policy of full disclosure . . . and the remedial-penal nature of the private enforcement provisions of the Act." *Palmer v. Wilson*, 502 F.2d 860, 862 (9th Cir. 1974).

93. The terms "discretionalist" approach and "literalist" approach were coined in Note, *Consumer Protection: Judicial Approaches to Rescission and Restoration under the Truth in Lending Act*, 53 WASH. L. REV. 301 (1978).

94. *Id.* at 312.

95. 502 F.2d 860 (9th Cir. 1974) (action by plaintiff-borrowers against lenders for failure to state the total of payments due and the amount financed, and failure to inform of right to rescind).

96. In loan situations, courts applying a discretionist approach usually order deferred restoration because of the debtor's inability to repay the amount borrowed. "Deferred restoration can be accomplished by either conditioning termination upon the borrower's compliance with a realistic repayment plan, or granting termination unconditionally and entering judgment for the creditor in the amount of the loan proceeds." Note, *supra* note 93, at 313.

97. See note 17 *supra*. Paer suggests that the economic difficulties recently experienced in the business sector prompted the courts to ease the creditors' burden. Paer, *supra* note 16, at 365.

cost of the service and include finance charges. If the contract falls short of Truth-in-Lending disclosure requirements,⁹⁸ the debtor may be entitled to some form of relief.

One possible resolution is an award of total conjunctive relief: rescission, statutory damages and attorney's fees.⁹⁹ Under this scheme, the amount of the note is rescinded and the debtor is entitled to the return of all monies paid plus damages. The creditor invokes the forfeiture rule¹⁰⁰ if he fails to act upon the debtor's notification of his intention to rescind. The creditor is also liable for attorney's fees.¹⁰¹ Several courts, although relying on different rationales, have designated this as the proper remedy. In *Sosa v. Fite*,¹⁰² the court applied the Act literally and stated that forcing a debtor to elect a remedy would undercut the legislation's effectiveness. The *Eby v. Reb Realty*

98. See note 28 *supra*.

99. 15 U.S.C. §§ 1635, 1640 (1976).

100. *Id.* § 1635 (1976), 12 C.F.R. § 226.9(d) (1980). "[T]he Act flatly provides that if his creditor continues in his untoward ways, the debtor incurs no obligation to pay for property which he is at the same time entitled to keep." *Sosa v. Fite*, 498 F.2d 114, 119 (5th Cir. 1974). Where the rescinding plaintiffs borrowed from the defendants, the loan's unpaid principal balance was considered "property" within the meaning of the Act. *Strader v. Beneficial Fin. Co.*, 551 P.2d 720 (Colo. 1976). For a discussion of *Strader*, see Comment, *Consequences of the Creditor's Failure to Acknowledge Rescission by the Debtor under Strader v. Beneficial Fin. Co.*, 48 U. COLO. L. REV. 437 (1977).

Strader was an action under Colorado's Uniform Consumer Credit Code. Often there are discrepancies between the state-enacted uniform code and the federal act, but the states are obligated not to adopt inconsistent rules. See Miller, *Living with Both the UCCC and Regulation Z*, 26 OKLA. L. REV. 1 (1973).

101. In the hypothetical situation, if the consumer agreed to a note of \$5,000 for the home improvement of which he paid \$400, and the court awards the maximum amount of damages under § 1640(a)(1), then the judgment would produce the following results:

Amount of Note	\$ 5000.00
Full Rescission	<u>-5000.00</u>
Debtor Owes	<u>-0-</u>
Return of Monies Paid	400.00
Damages	<u>+1000.00</u>
	1400.00
Attorney's Fees	<u>+750.00</u>
Creditor Owes	\$ 2150.00

102. 498 F.2d 114 (5th Cir. 1974) (plaintiff only sought § 1635 rescission, but court allowed recovery of attorney's fees).

*Co.*¹⁰³ court also held that a literal interpretation dictated conjunctive relief and rejected the argument that such an approach would produce inequitable consequences. It has also been noted that a literal interpretation promotes uniformity of results in TILA actions.¹⁰⁴

Nevertheless, the Tenth Circuit in *Burley v. Bastrop Financial Co.*¹⁰⁵ employed judicial discretion and characterized the relief as conditional. *Burley* involved a consumer transaction secured by a mortgage on the debtor's primary residence. Defendant did not provide notice of the right of rescission. Plaintiff's attorney sent a letter of rescission, but defendant did not respond. The *Burley* court ordered the creditor to return the plaintiff's down payment, directed termination of the mortgage on the debtor's property and ordered dismissal of defendant's state court action. The court indicated that this was the appropriate remedy since the creditor failed to mitigate its violations. These cases illustrate that under certain circumstances the literalist and discretionist approaches may prescribe identical remedies.

By balancing various elements, a court using its discretion can devise a wide range of alternative remedies. Many courts find the literal approach's forfeiture theory¹⁰⁶ unacceptable. Thus, some condition a contract's rescission upon the debtor's repayment of the balance, while voiding the security interest. These courts conjunctively award statutory damages and attorney's fees.¹⁰⁷ In *Pedro v.*

103. 495 F.2d 646 (9th Cir. 1974) (plaintiff, a purchaser of real property, sought rescission and twice the amount of the finance charge under § 1640).

104. One commentator notes that a reason the legislature set out the sequence of events in the statute was to achieve uniformity. The same author objects to using a balancing approach to allow a creditor to avoid its obligation. Comment, *supra* note 100, at 445.

105. 407 F. Supp. 773 (W.D. La. 1975).

106. See note 100 *supra*.

107. See note 101 *supra*. Then assuming the same facts and adding a finance charge of about \$1,550.00, under this judicial approach the result would be:

Pacific Plan of California,¹⁰⁸ the court recognized that Pacific Plan's disclosure violations gave rise to statutory damages and cancellation of the transactions. Plaintiff gave timely notice of exercising her right of rescission and defendant offered to cancel the transaction upon Pedro's payment of a limited sum. The court regarded defendant's limited offer as forfeiting its right to restitution, but affirmed the borrower's admission of an equitable obligation to restore the net balance she received.¹⁰⁹

Concern with the rescinding consumer's unjust enrichment also contributed to the court's decision in *Gerasta v. Hibernia National Bank*.¹¹⁰ The *Gerasta* court acknowledged that rescission does not preclude section 1640 relief, but upheld the position that such relief is dependent upon "a court's sense of equity"; therefore, the court may deny the request when the facts don't merit section 1640 relief.¹¹¹

Another possible solution in a loan transaction situation is a grant of rescission based on repayment of the principal with the security interest staying in effect.¹¹² The leading case endorsing this position is *Palmer v. Wilson*.¹¹³ The *Palmer* court expressed concern over the

Amount of Note	\$ 5000.00
"Rescission"	
a. finance charge	<u>-1550.00</u>
	3450.00
b. return of monies	<u>-400.00</u>
paid	
	3050.00
Damages	<u>-1000.00</u>
Debtor Owes	<u>\$ 2050.00</u>
Attorney's Fees	
Creditor Owes	\$ 750.00

108. 393 F. Supp. 315 (N.D. Cal. 1975) (plaintiff brought action against broker for failure to disclose identity of the lender).

109. "Since plaintiff does not contend that Pacific Plan has practiced any fraud or unconscionable conduct, the Court concludes that plaintiff had an equitable duty to restore the net amount she received." *Id.* at 324.

110. 411 F. Supp. 176 (E.D. La. 1976).

111. *Id.* at 192.

112. See notes 101 and 107 *supra*. The results are the same as in the second alternative as set forth in note 107 *supra*, but here rescission is predicated on repayment of the principal with the security interest staying in effect.

113. 502 F.2d 860 (9th Cir. 1974). See also *Rachbach v. Cogswell*, 547 F.2d 502 (10th Cir. 1976) (imposition of interest as condition to right of rescission); *LaGrone v.*

creditor's ability to recover the amount advanced. The retention of the security interest protects the creditor if the borrower is incapable of restoration.¹¹⁴ This approach is inconsistent with the Act's language which stipulates that the creditor must remove any lien prior to tender by the debtor.¹¹⁵ The retention of the security interest on the debtor's property seems contrary to the legislative purpose of protecting homes.¹¹⁶ The apparent harshness of conditional rescission on consumers, however, is mitigated when the judgment lien is distinguished from the original security interest. State statutes usually provide certain exemption rights regarding the real property of a judgment debtor. Thus, the creditor may reach less of the debtor's property under a lien than under a security interest. The creditor may also lose priority to other intervening creditors.¹¹⁷

Johnson, 534 F.2d 1360 (9th Cir. 1976) (damages precluded by statute of limitations); Ljepava v. M.L.S.C. Properties, Inc., 511 F.2d 935 (9th Cir. 1975).

114. See note 96 *supra*.

The result is that the creditor, having been stripped of his security interest by rescission, finds that the debtor is judgment-proof. The creditor may lose not only the investment value of the loan but also the principal, in addition to the administrative costs of the loan, a civil penalty, attorneys' fees and costs of the truth in lending action.

Note, *supra* note 31, at 879 (1975). The *Palmer* court held that on remand the lower court could require defendants to submit a proposed plan of repayment to accommodate defendants' desire for recovery that was consistent with the Palmers' financial situation. 502 F.2d at 862-63.

115. Reg. Z § 226.9(d) in pertinent part reads:

Within 10 days after receipt of a notice of rescission, the creditor shall return to the customer any money or property given as earnest money, down-payment, or otherwise, and shall take any action necessary or appropriate to reflect the termination of any security interest created under the transaction. If the creditor has delivered any property to the customer, the customer may retain possession of it. Upon the performance of the creditor's obligations under this section, the customer shall tender the property to the creditor, except that if return of the property in kind would be impracticable or inequitable, the customer shall tender its reasonable value.

12 C.F.R. § 226.9(d) (1980). (Emphasis added.)

116. See note 34 *supra*. "Under the Act a court should be concerned that defendants ultimately receive the money they advance under a loan agreement, but it must be careful that such concern does not provide lenders with a method of frustrating the main purpose of the Act, which is to allow rescission." Ljepava v. M.L.S.C. Properties, Inc. 511 F.2d 935, 944 (9th Cir. 1975). See Case Note, 1975 B.Y.U. L. Rev. 211, 221.

117. These state statutes grant homestead exemptions and can reduce the creditor's status from a holder of a security interest in property to a judgment creditor and thus protect the debtor. See Note, *Truth in Lending—Right of Rescission*, 1975 Wis. L. Rev. 192, 198-99.

A more severe determination from a debtor's viewpoint would be the award of damages and attorney's fees without rescission. Thus, the consumer would owe the balance of the note, including the finance charge, reduced by the amount of damages awarded. The creditor would still be liable for attorney's fees.¹¹⁸ In *Powers v. Sims and Levin*,¹¹⁹ plaintiffs attempted to rescind and offered to deliver the transaction's partial value. The court found anticipatory breach by the debtor and held there is no condition precedent to clear title when it is evident that the borrower does not intend to repay.¹²⁰ Thus, under *Powers*, debtors must give an unqualified notice of exercise of the rescission right.

In Regulation Z, the Federal Reserve Board accounted for another potentially inequitable situation by enacting the section 226.9(c) delay of performance provision. That provision forbids certain acts¹²¹ by a creditor before "the rescission period has expired and he has reasonably satisfied himself that the customer has not exercised his right of rescission."¹²² Since there should be no performance in the three-day rescission period after the transaction's consummation, the debtor will not receive any unjust benefits. The only time the consumer can rescind after the creditor has performed some service is

118. See notes 101, 107 and 112 *supra*. Under the *Powers* scheme the results would be:

Amount of Note	\$ 5000.00
Monies paid	<u>- 400.00</u>
	4600.00
Damages	<u>-1000.00</u>
Debtor Owes	\$ 3600.00
Attorney's Fees	
Creditor Owes	\$ 750.00

119. 542 F.2d 1216 (4th Cir. 1976). At the time of the home improvement transaction with Sims and Levin, Powers owed the First & Merchants Bank \$2,758.13, which was secured by a first mortgage. Defendant satisfied plaintiff's debt and that mortgage was canceled.

120. The court found that rescission absolves the borrower of the obligation to pay finance or other charges, but does not relieve him of the duty to restore. *Id.* at 1220-22.

121. The creditor is prohibited from disbursing any money other than in escrow; making any physical changes in the customer's property; performing any work or service or making any deliveries to the customer's residence if the security interest is other than one arising by operation of law. 12 C.F.R. § 226.9(c) (1980).

122. *Id.*

upon the creditor's nondisclosure.¹²³

IV. CONCLUSION

It is crucial to keep in mind the TILA's purpose of compelling creditor disclosures to facilitate consumer comparison between available sources and to encourage competition among lenders.¹²⁴ Through the Truth-in-Lending Act, Congress also hoped to promote private litigation by consumers. In light of these objectives, the rescission and civil liability sections should be construed as penal as well as remedial provisions. Courts should therefore award conjunctive relief.

Influenced by the possibility of inequitable results, some courts resort to a balancing approach. In many cases, however, creditors could avoid imposition of harsh penalties by compliance with the disclosure requirements. Creditor contentions that TILA's requirements are difficult to implement may well be valid, but these ambiguities should be remedied through Congressional amendment¹²⁵ or by explanatory regulations promulgated by the Federal Reserve Board.

Congress sought to clarify the parties' obligations in consumer credit transactions by enacting the Truth-in-Lending legislation. Yet, the increased use of judicial discretion creates uncertainty for both creditors and debtors. An approach that appears consistent with Congressional intent and equitable to all parties is the incorporation of the debtor's obligation¹²⁶ into the court's judgment. A court achieves mutual restoration by ordering rescission, voiding the secur-

123. To distinguish the two three-day periods when rescission is permissible, see note 44 *supra*.

124. The Act's effectiveness in achieving its goals has been frequently questioned. See Landers & Rohner, *A Functional Analysis of Truth in Lending*, 26 U.C.L.A. L. REV. 711 (1979). Landers and Rohner contend that consumer behavior is not affected by disclosure statements, regardless of the quality of the statement. *Id.* at 715. They cite several reasons supporting their conclusion, amongst them that disclosures are made after a preliminary agreement has been reached and the consumer is "verbally and psychologically committed." *Id.* at 715-16. Also, most credit sales occur when the consumer needs the good or service on credit terms and thus must seek "the best terms offered by a creditor who will approve his credit." *Id.* at 716. Landers and Rohner state that shopping for credit terms after disclosure is not cost effective. *Id.* at 717-18.

125. Congress is considering simplifying and reforming the Act, as evidenced by S. 108. See note 18 *supra*. The proposed amendments, if approved, will directly affect and clarify issues now being litigated.

126. This is similar to the second alternative discussed. See note 107 *supra*.

ity interest and giving the creditor the principal balance due him. By comparison, the conditional rescission approach¹²⁷ threatens the debtor with the loss of his home. Incorporation of the debtor's obligation encourages consumer suits that may help compel creditor compliance and yet dissuade frivolous or malicious legal actions.

127. *See* note 112 *supra*.

COMMENTS

