Uniform Consumer Credit Code and National Consumer Act: Some Objective Comparisons

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The Uniform Consumer Credit Code[1] was approved by the National Conference of Commissioners on Uniform State Laws on July 30, 1968, and by the American Bar Association on August 7, 1968. Many state legislatures are today actively considering the measure, with Utah and Oklahoma having already enacted it.

The National Consumer Act[2] was promulgated in 1969 by the National Consumer Law Center, an Office of Economic Opportunity funded project at Boston College Law School. It too, is under active consideration around the country.

Both Acts are comprehensive revisions of the hodge-podge of consumer credit state laws that are on the statute books today. In some respects, the two Acts are similar; in many ways, however, they differ. Both Acts are quite lengthy and complex, and contain

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1. Hereinafter cited as U.C.C.C.
2. Hereinafter cited as N.C.A.

many provisions on a number of subjects. The purpose of this material is not to examine in detail each section of both Acts, but rather to highlight the coverage of the two Acts, comparing their differences where important.

I. General Observations

A. Disclosure. The Federal Consumer Credit Protection Act of 1968, of which part I is Truth in Lending, requires certain basic disclosures under certain credit conditions. Section 123 of that Act provides that the Federal Reserve Board should exempt from the requirements of Chapter 2 of Truth in Lending:

> Any class of credit transactions within any State if it determines that under the law of that State that class of transactions is subject to requirements substantially similar to those imposed under this Chapter, and that there is adequate provision for enforcement.

Accordingly, in order to obtain the authorized exemption, the U.C.C.C. contains disclosure language throughout its sections, language which the Federal Reserve Board has already determined to be "substantially similar" to federal law. Accordingly, on May 5, 1970, the Federal Reserve Board granted the State of Oklahoma—a Uniform Consumer Credit Code state—a section 123 exemption.

The N.C.A., on the other hand, would incorporate the provisions of the Federal Act as part of any state statute (N.C.A. § 2.306). Through this device, the State Administrator created under Article 6 is given enforcement powers within the state even under the Federal Act.

There are some additional disclosures required under N.C.A., however, such as:

(1) disclosure of annual percentage rate and dollar finance charge must be made in all transactions; the Federal Act exempts transactions where only a statutory minimum charge is made;

(2) the Federal Act, and thus U.C.C.C., deals solely with disclosure of credit cost and other terms; the N.C.A. goes beyond this and deals with problems of the transaction itself. For example, N.C.A. prescribes what must be contained in the contract itself.

(a) N.C.A. § 2.302—requirements of a single writing;

(b) N.C.A. § 2.303—prohibits signing in blank.

B. Maximum Interest Rates. Neither the U.C.C.C. nor the

N.C.A. fixes rates. Both are designed only to set ceilings on interest rates, although the N.C.A. does not propose any specific ceilings in its text.

1. The U.C.C.C. would set the following ceilings on interest rates:

a. revolving charge accounts—24% per/year to $500; 18% over $500. (§ 2.207)

b. other consumer credit sales—36% to $300; 21% to $1,000; or 18% per/year on the unpaid balances of the amount financed. (§ 2.201)

c. supervised loans—same as for consumer credit sales (§ 3.508)

d. other loan finance charges—for all other consumer loans, the ceiling is set at 18% on the unpaid balance. This applies to both closed end credit as well as revolving credit. (§ 3.201)

2. N.C.A. provides three alternatives: a flat rate ceiling, graduated rates, or graduated or flat rates (as provided in U.C.C.C.). No position was taken by N.C.A. draftsmen as to what the rate ceiling should be, and in fact blank spaces are provided. The following comments were offered, however:

> No available data adequately supports the need for the high rates ceilings proposed in the Uniform Consumer Credit Code, although such ceilings do exist in some states. The important matter is that a state adopt a unified and consistent rate ceiling statute which applies across the board to all creditors . . . . This section (N.C.A. § 2.201) applies the same rate ceiling or ceilings to all kinds of credit, whether open-end or otherwise and whether sale or loan credit. (comment to N.C.A. § 2.201)

C. SALES VS. LOANS. The U.C.C.C. treats sales transactions and loan transactions separately. Article 2 covers credit sales, including home solicitation sales, and Article 3 covers loans. The only explanation for this treatment can be found in the Prefatory Note to Working Draft No. 6 of the U.C.C.C.:

> [T]he Committee was and is aware that, sociologically and economically, sales credit and loan credit are alike and that their separate treatment results in much duplication in drafting. Nevertheless, we are mindful of the weight given to Uniform Acts by Courts of States which have not enacted them. Thus, long before the Uniform Commercial Code was enacted or even introduced in New York, the New York Court of Appeals relied in part on a provision of the Uniform Commercial Code in overruling the Court's prior decisions on privity of contract and determining who may recover upon a breach of warranty in a sale of goods. The Committee believes that any encouragement to the Courts of a State which has not enacted the Uniform Consumer Credit Code to rely on the Code's

> provisions in rejecting the time sale price doctrine would have most unfortunate social and economic consequences.

The National Consumer Act combines Articles 2 and 3 and treats them both in N.C.A. Article 2, entitled "Consumer Credit Transactions."

II. Limitations on Agreements and Practices

Although the language and intent may differ, both the U.C.C.C. and N.C.A. prohibit some of the most abusive consumer practices, and restrict many others. A few are highlighted here:

A. Prohibited Agreements:

1. Confession of judgment clauses are prohibited by both Acts. (U.C.C.C. § 2.415; N.C.A. § 2.404).

2. Use of negotiable instruments is prohibited by both Acts. Significant differences must be noted, however:

   a. U.C.C.C. § 2.403 restricts negotiable instruments (other than checks), and states that a holder ". . . is not in good faith if he takes a negotiable instrument with notice that it is issued in violation of this section." The Code does concede the holder in due course concept, however, since such instruments can be used in violation of the Code. The rationale behind this is explained in a comment following § 2.403:

      > [I]t is possible that in rare cases second or third takers may not know of an instrument's consumer origin; in this unusual situation the policy favoring negotiability is upheld in order not to cast a cloud over negotiable instruments generally.

   b. N.C.A. § 2.405 prohibits the taking of instruments payable "to order or to bearer" in any consumer credit transaction or consumer lease. Thus, under Article 3 of the Uniform Commercial Code, the negotiability of such instruments is destroyed.[3] It should be noted that the N.C.A. provisions apply to both sales and loans, whereas U.C.C.C. applies only to consumer sales.

3. Assignee subject to Defenses. Herein lies perhaps one of the

3. They are, of course, still subject to other provisions of U.C.C.C. Article 3.

most controversial issues among proponents of both measures.

a. U.C.C.C. (§ 2.404) provides two alternative methods of attacking this problem:
   (1) Alternative A[4]—the assignee of the rights of a seller in a consumer sale is subject to *all* claims and defenses of the buyer against the seller arising out of that sale. This section does not apply to sales which are "primarily for an agricultural purpose," and limits the assignee's liability to "the amount owing to the assignee at the time the claim or defense is asserted." Furthermore, the rights of the consumer can only be asserted "as a matter of defense to or set-off against a claim by the assignee."
   (2) Alternative B—provides that where a sales contract contains waiver of defenses against assignees, the assignee must notify the buyer of assignment, and the buyer then has three months in which to notify the assignee of any defenses which have arisen. If he fails to notify, he may not assert his defenses against the assignee although the buyer would still be free to raise real defenses arising after the expiration of the three-month period.

b. N.C.A.—§ 2.406 makes ineffective and unenforceable agreements of consumers which waive any of their defenses against assignees. Thus, for all practical purposes the holder in due course doctrine is repealed in consumer credit transactions.

4. Assignments of earnings is prohibited by both Acts. (U.C.C.C. § 2.410, § 3.403; N.C.A. § 2.403). The Code comments that this prohibition is a recognition of the ". . . potential for hardship for a consumer and his dependents which may result from a disruption of the steady flow of family income." Thus, both Acts would preclude a creditor from reaching a debtor's earnings pursuant to an irrevocable wage assignment obtained from the debtor.

5. Waivers, or agreements to forego rights or benefits conferred by the Consumer Act, are prohibited by both U.C.C.C. (§ 1.107) and N.C.A. (§ 1.106).

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4. This section codifies a growing body of decisions in connection with U.C.C. § 9-206. *See, e.g.*, Unico v. Owens, 50 N.J. 101, 232 A.2d 405 (1967).

B. OTHER LIMITATIONS

1. Balloon payments.

a. U.C.C.C. (§ 2.405, § 3.402) provides that for sales and loans, if any scheduled payment is more than twice as large as the average of earlier scheduled payments, the consumer has the right to refinance the amount of that payment at the time it is due without penalty. The terms of the refinancing shall be no less favorable to the buyer than the terms of the original sale. This refinancing does not apply to transactions:

(1) primarily for an agricultural purpose;

(2) pursuant to a revolving charge or loan account;

(3) where the payment schedule is adjusted to the seasonal or irregular income of the buyer.

b. N.C.A. (§ 2.402) prohibits all balloon payments for irregular payment intervals unless they expressly relate to the consumer's income.

2. Referral Sales. Both Acts prohibit the practice whereby the consumer—as an inducement to buy—is offered a rebate or discount for every other prospective purchaser's name given by the consumer. (U.C.C.C. § 2.411; N.C.A. § 2.415). A comment to the U.C.C.C. states:

> The evil this section is aimed at is the raising of expectations in a buyer of benefits to accrue to him from events which are to occur in the future.

3. Attorney's fees.

a. The U.C.C.C. provides alternative sections to cover the problem of who pays the creditor's lawyer (§ 2.413):

(1) Alternative A—prohibits a charge on the consumer for the payment of attorney's fees. According to the Code's draftsmen, this section ". . . reflects a policy decision to follow some small loan acts in treating this expense, like other collection costs, as part of the seller's cost of doing business, rather than a charge to be imposed on the defaulting buyer."

(2) Alternative B—permits an agreement whereby

the consumer pays reasonable attorney's fees not in excess of 15 percent of the unpaid debt after default. According to the Code's draftsmen, this alternative reflects a policy to treat attorney's fees ". . . not as part of the seller's general overhead to be indirectly borne by all his customers but as a charge to be imposed, at least in part, on the defaulting buyer who gives rise to the expense."

b. N.C.A., in § 2.410 prohibits payment by the consumer of attorney fees, thus reflecting the policy incorporated in Alternative A, U.C.C.C., § 2.413.

4. Security interest.

a. U.C.C.C. § 2.407 is the applicable section, and governs the following types of transactions:

(1) sale of goods—a seller may take a security interest in the goods sold but not in other goods or land of the buyer unless;

(a) the goods sold become closely connected with the goods or land in which the security interest is taken, and

(b) in the case of a security interest in land the debt secured is $1,000 or more, or, in the case of a security interest in goods the debt secured is $300 or more.

(2) sale of land—the seller can retain a security interest only in the land sold, and not in other goods or land of the buyer. This applies only to "consumer credit sales," and (according to § 2.104(2)) a sale of an interest in land in which the finance charge is 10% or less is not such a sale.

(3) loans—U.C.C.C. § 3.510 prohibits a lender from contracting for an interest in land as security, if he makes a supervised loan (*i.e.*, finance charge exceeds 18%) in which the principle is $1,000 or less.

b. N.C.A. § 2.416 is the applicable section, and governs the following types of transactions:

(1) there is a general exemption in that no security, other than a purchase money security interest, may be taken for household furnishings, appliances and clothing of the consumer and his dependents.

(2) sale of goods—a seller may take a security interest in the goods sold, but not in other goods or land of the buyer unless;
   (a) the goods sold become closely connected with the goods or land in which the security interest is taken, and
   (b) in the case of a security interest in land, the obligation secured is $3,000 or more, or, in the case of a security interest in goods the obligation secured is $500 or more.

(3) sale of land—the seller can retain a security interest only in the land sold, and not in other goods or land of the buyer.

(4) loans—N.C.A. § 2.416(3) prohibits a lender from securing the obligation:
   (a) with an interest in real property where the amount financed is $3,000 or less, or
   (b) with an interest in personal property the fair market value of which exceeds one and one half times the amount financed.

III. Limitations on Creditors Remedies

A. Restrictions on Deficiency Judgments:

1. U.C.C.C. (§ 5.103) applies to consumer credit sales or goods or services. Under such sales, if the *cash price* is $1,000 or less, a seller who repossesses or voluntarily accepts surrender of goods sold in which he has a security interest may not obtain a deficiency judgment against the buyer if the proceeds on disposition of the goods are insufficient to pay the indebtedness and the expenses of the seller. The seller need not resell the goods. Thus, the Code gives the seller, in cases of sales of $1,000 or less, the option of either sueing for the unpaid balance or repossessing; he may not do both.

2. N.C.A. (§ 5.211) applies to both secured loans as well as credit sales. A creditor who repossesses is entitled to a deficiency only if the *unpaid balance* at the time of default was $2,000 or more. Thus, under $2,000, a creditor has an election between repossession and a suit for deficiency.

B. UNCONSCIONABILITY:

1. U.C.C.C. (§ 5.108, § 6.111)
   a. If the court, as a matter of *law*, finds an agreement or any clause of an agreement, to have been unconscionable at the time it was made, the court may refuse to enforce it or any part of it. The basic test is whether, in the light of the background and setting of the market, the commercial needs of the particular trade or case, and the condition of the particular parties to the contract, the contract or clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract.
   b. Section 6.111 gives the Administrator of the Code power to bring a civil action to restrain a creditor from engaging in fraudulent or unconscionable conduct. Section 6.111 (3) sets out guidelines for the Court to apply in determining whether such conduct exists.
   c. The Administrator's powers under § 6.111 covers three different areas of unconscionable conduct:
      (1) unconscionable contract terms;
      (2) fraudulent or unconscionable conduct in inducing consumers to enter into consumer credit transactions; and
      (3) fraudulent or unconscionable conduct in the collection of consumer credit debts.
2. N.C.A. (§ 1.106 (4); § 3.201 (2); § 5.107; § 6.109, and § 7.206).
   a. Under the N.C.A., unconscionability is found as a matter of *fact*.
   b. Whereas the U.C.C.C. provides for either a reformation or cancellation of a contract where found unconscionable, N.C.A. permits reformation or cancellation as well as a provision for actual and punitive damages.
   c. Unlike the Uniform Commercial Code (U.C.C. § 2-302) which limits the concept of unconscionability to terms or clauses in the contractual agreement, the N.C.A. includes any conduct pursuant to a transaction.

IV. CONCLUSION

It was not the objective of this paper to reach a conclusion. Its sole purpose is to assist those who are considering the enactment of

consumer credit legislation in understanding some of the highlights —whether controversial or not. If a conclusion must be drawn, it is that there is a strong need in most of the states for modern consumer credit legislation. And those considering this legislation must see to it that their approach is a positive one, so that legislation can indeed be enacted.