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CONSUMER LAW

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GOOD FAITH VIOLATIONS OF THE TRUTH IN LENDING ACT

When in 1969 the plaintiff-creditor in *Thrift Funds of Baton Rouge, Inc. v. Jones*[1] refinanced the original 1967 consumer credit loan indebtedness of the defendant-debtor, the then recently enacted Consumer Credit Protection Act[2] required that various specified disclosures regarding the cost of that credit be made to the debtor.[3] In apparent compliance with that federal legislation certain disclosures were made to the debtor prior to consumation of the 1969 extension of credit, but as the Louisiana supreme court was subsequently to point out, the creditor was at that time laboring under an erroneous belief as to the effect of the Louisiana usury laws. Thus, when it disclosed to the debtor that the "amount financed"[4] was $627 it made

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1. 274 So. 2d 150 (La. 1973). For a discussion of the facts of the case and of the court's decision on the usury issue, see *The Work of the Louisiana Appellate Courts for the 1972-1973 Term—Obligations*, 34 LA. L. REV. 231, 238 (1974).

2. Act of May 29, 1968, Pub. L. No. 90-321; 82 Stat. 146 *et seq.*; codified in 15 U.S.C. §§ 1601-1681 (1968). The act contains six titles: Title I, which pertains to consumer credit cost disclosure is popularly referred to as the "Truth in Lending Act"; Title II deals with "extortionate credit transactions" and is essentially aimed at loan sharking; Title III sets wage garnishment limits and restricts the discharge of employees whose wages have been garnished; Title IV established the National Commission on Consumer Finance which through its recent report has recommended to Congress numerous and far-reaching changes in the structure and functioning of the consumer credit industry (U.S. Government Printing Office, Stock No. 5200-00005, December 1972); Title V sets restrictions on the issuance of credit cards and the liability of cardholders; Title VI is the "Fair Credit Reporting Act."

Congress delegated to the Board of Governors of the Federal Reserve System the duty of prescribing such regulations as in the Board's judgment are "necessary and proper" to carry out the purposes of the Act, and to prevent evasion of it, or to facilitate compliance therewith. This the Board has done in "Regulation Z" [12 C.F.R. §§ 226.1 *et seq.* (1973)]. The purpose of Title I is to arm the consumer through disclosure statements with cost of credit information so that he may meaningfully compare or "shop" for the various credit terms available to him and thus avoid the uninformed use of credit. The consumer will then theoretically choose the least expensive credit, thus promoting competition which in turn leads to enhanced economic stabilization. 15 U.S.C. § 1601 (1970).

3. The disclosure requirements vary somewhat depending on whether the credit extended is open end or non-open end, and whether it is sale or loan credit. *See* 15 U.S.C. §§ 1631-39 (1970); 12 C.F.R. §§ 226.6-.8 (1971). For the credit extended in the principal case 12 C.F.R. § 226.8(j) (1973) required the creditor to make the disclosure set forth in 15 U.S.C. § 1639 (1970) and 12 C.F.R. § 226.8(b), (d) (1973).

4. 15 U.S.C. § 1639(a)(3) (1970); 12 C.F.R. § 226.8(d)(1) (1973).

an incorrect disclosure since the balance due on the 1967 indebtedness should have been $128 rather than $522, the difference being ascribable to the omission of "capitalized" interest forfeited—under the court's view—by usurious delinquency charges.[5] So erroneously informed, a debtor such as Mr. Jones is theoretically prevented from exercising what is the underlying basis of the federal requirement of credit cost disclosure—the opportunity to meaningfully and intelligently "shop" for credit by comparing via disclosure statements the terms, rates and charges of competing credit grantors.[6] To promote that end, Congress provided civil liability of twice the amount of the finance charge,[7] the costs of the action and a reasonable attorney's fee,[8] against creditors who violate the act's disclosure requirements. The act expressly provides in § 1640(c), however, that a creditor may not be held liable for violations which the creditor shows by a preponderance of evidence were "not intentional and resulted from a bona fide *error* notwithstanding the maintenance of procedures reasonably adapted" to avoid any such errors.[9]

In *Thrift Funds* the debtor alleged in his reconventional demand that the plaintiff-creditor's erroneous disclosures violated the federal disclosure requirements, thus entitling him to the recovery provided in § 1640(a). The supreme court, expressly taking into consideration the fact that prior interpretations of the usury laws were at the time

5. The Federal Reserve Board has taken the view that the word "error" in 15 U.S.C. § 1640(b) (1970) includes overstatement, understatement, or discrepancy. *See* FRB Letter of April 17, 1970, by Milton W. Schober in 4 CCH CONS. CRED. GUIDE ¶ 30,352. The "error" occurring in the principal case would normally produce "spin-off" errors in other required disclosures such as the amount of the finance charge, the annual percentage rate, and the amount and due dates of payments scheduled to repay the indebtedness. *See* 12 C.F.R. § 226.8(b) (1973).

6. *See* note 2 *supra*, and Mourning v. Family Publications Service, 93 S. Ct. 1652, 1658 (1973).

7. 15 U.S.C. § 1640(a)(1) (1970). The term "finance charge" is defined in 15 U.S.C. § 1605 (1970) and 12 C.F.R. §§ 226.2(q), 226.4 (1973). 15 U.S.C. § 1640(a) (1970) provides that the doubled finance charge cannot exceed $1000 but it also provides a minimum recovery of $100. The recovery is probably more accurately categorized as a *penalty* to promote compliance. *But see* Bostwick v. Cohen, 319 F. Supp. 875 (N.D. Ohio 1970).

8. 15 U.S.C. § 1640(a)(2) (1970). Trial courts are generally considered to be experts in the matter of setting reasonable attorney's fees. *See* Wegmann v. Suggs, 147 So. 2d 263 (La. App. 4th Cir. 1962).

9. 15 U.S.C. § 1640(c) (1970) (Emphasis added.) Given a disclosure violation, there are at least five other defenses to the liability created by § 1640(a), including the discovery and notification to the consumer of the error under § 1640(b). Avoidance of liability under the act is discussed in this writer's article, *Representing the Creditor: A Guide to the New Ground Rules of Extending and Collecting Credit*, 21 DRAKE L. REV. 381, 412-15 (1972).

the disclosures were made uncertain and even conflicting,[10] and failing to find any bad faith or fraudulent or even careless attempt to misinform the debtor, found no error in the district court's dismissal of the debtor's reconventional demand. Thus, the supreme court holds that where a creditor discloses information based on a bona fide and reasonable misinterpretation of law, the resulting error is a violation which is "not intentional" and which is the result of a "bona fide error" under the meaning of § 1640(c).

While under the facts and circumstances of the case the court's ruling that a "reasonable" misinterpretation of law can constitute an unintentional and bona fide error seems unimpeachably sound, a caveat is warranted lest creditors place total and uninformed reliance on the court's interpretation of the federal law. Beyond the fact that the court was understandably hesitant to add up to $2500[11] to the consequences of Thrift Funds' misinterpretation of law, the Consumer Credit Protection Act does not define the key phrase "bona fide error." The Federal Reserve Board, in carrying out its delegated duty to issue regulations and interpretations of the act,[12] has declined to interpret § 1640, taking the position that Congress intended that the matter be left for judicial interpretation.[13] Though few in number, the decisions on the point appear to favor a construction of § 1640(c) contrary to that announced by the Louisiana supreme court. In *Ratner v. Chemical Bank New York Trust Company*,[14] the bank failed to disclose the nominal annual percentage rate on monthly statements to its open end revolving loan account ("Master Charge") customers who had incurred no finance charges during the particular billing period.[15] The bank's computers were intentionally programmed to omit that disclosure in reliance on the advice of counsel and on that of a Federal Reserve Board attorney[16] that neither the act

10. 274 So. 2d 150, 161 (La. 1973). See Professor Johnson's discussion of this aspect of the case in *The Work of the Louisiana Appellate Courts for the 1972-1973 Term—Obligations*, 34 LA. L. REV. 231, 241 (1974).

11. Defendant sought $1000 under 15 U.S.C. § 1640(a)(1) (1970) and $1500 as attorney's fees under 15 U.S.C. § 1640(a)(2).

12. *See* note 2 *supra*.

13. *See* FRB Letter of October 22, 1970, by Griffith L. Garwood in 4 CCH CONS. CRED. GUIDE ¶ 30,596; FRB Letter of January 9, 1970 by J.L. Robertson in 4 CCH CONS. CRED. GUIDE ¶ 30,261.

14. 329 F. Supp. 270 (S.D.N.Y. 1971).

15. That is, those customers who paid in full during the 25-day "free ride" or grace period incident to the Master Charge billing plan.

16. The Federal Reserve Board has taken the position that opinion or advisory letters written by FRB Staff members in response to inquiries from creditors or members of the general public only represent "the informed view of the particular official

nor Regulation Z required such a disclosure for billing cycles in which no finance charges were imposed.[17] This the New York federal district court held to be a mistaken interpretation of the requirements of the law and *not* a "bona fide error" for which liability could be avoided under § 1640(c):

> It is undisputed that defendant carefully, deliberately—intentionally—omitted the disclosure in question. That defendant, in this court's view, mistook the law does not make its action any less intentional . . . .
>
> This conclusion is buttressed when we note the requirement . . . that the error be shown to have been both 'not intentional *and* [the result of] a bona fide error notwithstanding the maintenance of procedures reasonably adapted to avoid any such error.' The sparse legislative history on this reinforces what the language shows amply by itself—that the absolution was meant for *clerical errors.*[18] A defendant invoking this excuse is required not merely

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responding to the inquiry, who is authorized by the Board to express opinions on the particular subject," and does not necessarily represent "the position the Board members themselves would take if they formally considered the issue." FRB Letter of March 1, 1971, No. 444, by Kenneth A. Keynon, Deputy Secretary, in 4 CCH CONS. CRED. GUIDE ¶ 30,640; FRB Letter of December 2, 1969, No. 198, By J.L. Robertson in 4 CCH CONS. CRED. GUIDE ¶ 30,505. In *Stefanski v. Mainway Budget Plan, Inc.*, 326 F. Supp. 138 (S.D. Fla. 1971), *rev'd on other grounds*, 456 F.2d 211 (5th Cir. 1972), the court characterized such correspondence releases as "persuasive . . . [but] not binding authority as to questions of interpretation of federal law." *Id.* at 142. From the Board's standpoint, however, "the public is entitled to rely on [an informal] staff opinion unless and until it is altered by the Board after formal consideration." Kenyon Letter, ¶ 30,640 *supra*.

17. FRB Letter of November 28, 1969, No. 190, by Griffith L. Garwood in 4 CCH CONS. CRED. GUIDE ¶ 30,220.

18. The court added this footnote discussion: "The original version of the Senate bill contained no exemption for unintentional or bona fide violations. After businessmen and others complained during the Senate hearings that mathematical and clerical errors would be inevitable because of the complexity of annual rate computations, Hearings on S. 5 Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking and Currency, 90th Cong., 1st Sess. 64 ff., 226, 374, 426-27, 529, 584, 698 (1967), and should not subject creditors to liability, *id.* at 374, the bill was changed to include the language of the present exemption—with additional provision for exemption where the error is corrected and adjustments made 'within fifteen days after discovering the error, and prior to the institution of an action hereunder or the receipt of written notice of the error. The House bill originally required proof of a 'knowing' violation to establish civil liability. This was omitted in the final House version, apparently in response to objections by the Justice Department that to require proof of 'specific knowledge' might 'frustrate prospective plaintiffs, and thereby weaken the enforcement provisions of the act.' Hearings on H.R. 11601 Before the Subcomm. on Consumer Affairs of the House Comm. on Banking and Currency, 90th Cong., 1st Sess., pt. 1, 903 (1967)." 329 F. Supp. at 281, n.17.

> to show the clerical error was unintentional, but also that due care has been taken to set up *procedures* to avoid it. The provision is wholly inapposite to deal with errors of law like defendant's, though made in entire 'good faith.' However much clients and others might wish it, nobody has devised . . . 'procedures' Congress could have envisaged to cover such errors of law.[19]

The decision in *Ratner* also rendered irrelevant defendant's claim that its interpretation of the act's requirements was "reasonable" by ruling that the paramount aim of the act to protect consumers would be "grossly subverted" by countenancing "reasonable" violations.[20] This construction of § 1640(c) by the New York court has been adopted in three subsequent federal court decisions,[21] and because a question of interpretation of federal law is involved, the resulting "majority" view may be deemed persuasive by a federal court in Louisiana, the Louisiana supreme court's "minority" view of that section notwithstanding.[22]

The *Ratner* case has, on the other hand, been equally persuasive in its holding that class actions are inappropriate in private civil actions under the Consumer Credit Protection Act,[23] and at least one

19. 329 F. Supp. at 281-82. (Emphasis added in part.)

20. *Id.* at 282.

21. *See* Buford v. American Finance Co., 333 F. Supp. 1243, 1247 (N.D. Ga. 1971) (failure to include notary fees within the "finance charge" held a violation, creditor's good faith belief that such was not required under the act notwithstanding, since § 1640(c) exempts only clerical errors); Douglas v. Beneficial Finance Co. of Anchorage, 334 F. Supp. 1166, 1178 (D.C. Alaska 1971), *rev'd on other grounds*, 469 F.2d 453 (9th Cir. 1972) (creditor's intentional failure to disclose a confession of judgment clause under the erroneous belief that the act did not require such a disclosure held to be violative of the act and not an exempt clerical error); Palmer v. Wilson, 359 F. Supp. 1099 (N.D. Ca. 1973) (defense under § 1640(c) applies only to clerical errors). Prior to *Ratner*, the court in *Stefanski v. Mainway Budget Plan, Inc.*, 326 F. Supp. 138 (S.D. Fla. 1971), held violative of the act a creditor's disclosures premised on the erroneous belief that the transaction constituted sale credit rather than loan credit. Under 15 U.S.C. § 1640(e) (1970), a § 1640(a) action may be brought in any court of competent jurisdiction.

22. The United States Supreme Court denied certiorari on this aspect of the *Thrift Funds* case. 42 U.S.L.W. 3187 (U.S. Oct. 9, 1973).

23. Ratner v. Chemical Bank New York Trust Co., 54 F.R.D. 412 (S.D.N.Y. 1972). In its Annual Report to Congress on Truth in Lending for the year 1972, the FRB states that "while the cases are split, the clear trend appears to be against the allowance of class actions." The Report cites nine cases permitting class actions and twelve cases denying class action status. *See, e.g.*, Buford v. American Finance Co., 333 F. Supp. 1243, 1249-51 (N.D. Ga. 1971); Rogers v. Coburn Finance Corp. of De Kalb, 54 F.R.D. 417 (N.D. Ga. 1972); Kenney v. Landis Financial Group, Inc., 349 F. Supp. 939 (N.D. Iowa 1972) (class actions disallowed). In *Wilcox v. Commerce Bank of Kansas City*, 474 F.2d 336 (10th Cir. 1973), the court's opinion lists in footnote 13, at page 340 of

federal district court has interpreted § 1640(c) as "clearly contemplating" and thus exempting from liability "de minimus" violations of terminology requirements such as "total balance due" instead of the required phrase "total of payments," and "amount to be financed" instead of "amount financed."[24] In addition, the Board of Governors has recommended to Congress that the act be amended to provide for a "good faith" provision such as is contained in the Securities and Exchange Act of 1934.[25] Finally, mention should be made of the fact that the act arguably provides a defense for the kind of error involved in *Thrift Funds.* Under § 1634 if information "accurate" when disclosed is "subsequently rendered inaccurate as the result of *any* act, occurrence, or agreement subsequent to the delivery of the required disclosures, the inaccuracy resulting therefrom does not constitute a violation. . . ."[26] A decision of a state's highest court which in effect reverses existing practice among creditors arguably comes within the broad phrase "any . . . occurrence."[27]

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the opinion, twenty-one cases denying class actions and eleven permitting them. The FRB Report cites no cases allowing class actions subsequent to the *Ratner* ruling. The FRB recommends that the act be amended so as to permit class actions, but carrying an upper limit on the aggregate amount of class recovery of the greater of $50,000 or 1% of the creditor's net worth.

24. *See* Richardson v. Time Premium Co., 4 CCH CONS. CRED. GUIDE ¶ 99,272 (D.C. Fla. 1971); 12 C.F.R. § 226.8(b)(3) (1973).

25. *See* FRB Letter of February 28, 1972, by J.L. Robertson, FRB Vice Chairman, to Senator William Proxmire in 4 CCH CONS. CRED. GUIDE ¶ 30,811. The FRB proposal was made in its 1971 Annual Report to Congress on Truth in Lending.

26. 15 U.S.C. § 1634 (1970).

27. Such a disposition would appear to have more clearly complimented the supreme court's concern regarding the effect of its decision on the usury issue. The "subsequent occurrence" defense, however, was argued unsuccessfully by the writer in a similar case. *See* Kenney v. Landis Financial Group, Inc., 349 F. Supp. 939 (N.D. Iowa 1972). *Cf.* Douglas v. Beneficial Finance Co. of Anchorage, 469 F.2d 453, 456 (9th Cir. 1972).