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Statement on
Truth in Lending Simplification Bills
(S. 1312, S. 1501, S. 1653 and Federal Reserve Board Staff Proposal)

Presented to the
Subcommittee on Consumer Affairs
Senate Committee on Banking, Housing and Urban Affairs

United States Senate

by

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Mr. Chairman, we greatly appreciate this opportunity to appear this morning before your Subcommittee to testify in support of Truth in Lending simplification. The four proposals before us are Senator Proxmire's S. 1312, Senator Garn's S. 1501, your S. 1653 and a Federal Reserve Board staff proposal.

As you know, the FDIC has enforcement responsibility under the Truth in Lending Act with respect to insured banks which are not members of the Federal Reserve System. Since the law became effective in 1969, FDIC field examiners have checked for compliance with the Act as part of our routine bank examinations for safety and soundness. As an outgrowth of an experimental program involving the reliance on State examinations for safety and soundness in three states, the Corporation developed and in 1974 began using on a nationwide scale separate compliance examination reports designed to focus more attention on consumer matters. Furthermore, on June 3 of this year, we announced a new program of separate compliance examinations to assess compliance with various consumer protection laws and regulations including Truth in Lending. These separate compliance examinations will be conducted at least once every 15 months by examiners having special expertise in consumer protection matters, who will also, as appropriate, provide advice and guidance to bank managements on consumer protection laws and regulations.

While we believe that this new program of separate compliance examination by examiners specially trained in consumer protection matters will help bank managements establish effective procedures to assure compliance with consumer protection requirements, it is nevertheless imperative in our judgment that the basic framework of consumer legislation be structured to make it both comprehensible to consumers and enforceable at a reasonable cost to the public and to regulated institutions. Truth in Lending is a prime example of the need to simplify consumer legislation.

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The need for Truth in Lending simplification has been abundantly documented elsewhere. I will not, therefore, belabor the point with you here today. A simple glance at the length and complexity of the Act itself and of its implementing Regulation Z, at the more than 1,200 interpretations and staff opinion letters published by the Federal Reserve, and at the many thousands of law suits this legislation has spawned should suffice to make the case for simplification.

Clearly, it is unduly burdensome for creditors, especially smaller lending institutions, to have to comply with this enormous volume of regulatory requirements. In fact, the sheer volume and complexity of required disclosures renders full compliance very difficult. In our opinion, the amount of detailed, complex information that must be disclosed has increased the cost of credit to the consumer. At the same time, some believe that there has been no corresponding increase in benefit to the consumer because of a so-called "information overload" which taxes his ability to assimilate and utilize the information made available to him. Therefore, simplification legislation would substantially benefit both consumers and creditors. Similarly, there would undoubtedly be cost savings to the regulatory agencies as well.

Of course, simplification can mean different things to different people. To some it means eliminating unnecessary disclosures. To others it means limiting creditor liability. To still others it means providing borrowers and creditors with model forms in simple layman's language. Finally, there are those who advocate strengthening the administrative enforcement machinery for Truth in Lending violations. We believe that all of these are legitimate objectives of Truth in Lending simplification and that they all should be pursued simultaneously.

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S. 1312

As you indicated when you introduced your bill, Mr. Chairman, Senator Proxmire's S. 1312 provides a basic framework for comprehensive revision of the Truth in Lending Act. In addition to a number of largely technical changes recommended by the Federal Reserve Board, the bill would --

(a) exclude agricultural credit from Truth in Lending coverage;

(b) permit State officials to enforce State Truth in Lending laws as to federally chartered institutions in those States which are exempted by the Federal Reserve from Federal Truth in Lending requirements;

(c) require the enforcement agencies to order creditors to reimburse borrowers for any charges in excess of the stated finance charge or annual percentage rate unless the enforcing agency finds such restitution to be unreasonably burdensome; S. 1312 would also require such agencies to notify borrowers of any failure to reimburse them as ordered and of their consequent rights under the Act and would authorize the enforcement agencies to publicize the name and other details regarding a creditor who has engaged in repeated and substantial Truth in Lending violations;

(d) permit borrowers who are notified of a violation by an enforcement agency to file a civil action for damages within 90 days of such notification, but not more than 3 years after the transaction date;

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(e) require the Federal Reserve Board to issue model disclosure forms for common credit transactions phrased in understandable language which, if properly used, would relieve creditors from civil liability for alleged inadequate disclosures;

(f) limit civil liability in closed-end transactions to the following seven types of disclosure violations: (1) amount financed, (2) finance charge, (3) annual percentage rate, (4) repayment schedule, (5) late payment charges, (6) security interest, and (7) the right of rescission; and

(g) require the Federal Reserve Board to publish semiannually the annual percentage rates charged by creditors for various types of closed-end credit in urban areas exceeding 500,000 population.

We generally support the provisions in S. 1312, particularly the exemption for agricultural credit, requirements as to model disclosure forms and publication of annual percentage rates in large urban areas and the limitation of civil liability in closed-end credit transactions to certain specified disclosure violations. Including agricultural credit in the Act has resulted in numerous complexities and has been of little value to consumers. The FDIC has recommended on several occassions in the past that agricultural credit be excluded from the Act.

As to preparing model disclosure forms, the Federal Reserve Board is already doing this in the consumer leasing area and for credit application forms under the Equal Credit Opportunity Act. If the Board could draft simple, easy to read, and understandable disclosure forms, we believe this would be one

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of the more significant steps forward in consumer credit transactions that has ever been taken. Coupled with readily available information on rates being charged by various creditors in the locality, a consumer would be in a much better position to understand the terms of consumer credit transactions and to shop for the best rate available to him. While we strongly endorse this concept of publishing consumer loan rates in large urban localities, some have questioned the practicability of such an effort. Because of the obvious benefits to consumers, we would favor making every effort to provide such rate information to the public.

In the area of civil liability for disclosure violations, present law requires as many as twenty or more Truth in Lending disclosures in connection with a closed-end transaction. Civil liability may currently be imposed upon a creditor for very technical violations of Truth in Lending requirements. The amendment in S. 1312 would eliminate technical disclosures and require disclosure of information which is material to the borrower's credit decision. From the creditor's viewpoint, we believe that this could be one of the more important sections of the bill and should significantly reduce the amount of litigation.

We also favor some form of restitution to borrowers in cases involving an erroneously stated finance charge or annual percentage rate. While in our opinion the financial institution regulatory agencies presently have authority to order affirmative remedial action generally in enforcing the Truth in Lending Act, and to publish the results of examinations, we believe there is merit in the S. 1312 proposal to specifically provide for restitution, for notification to borrowers, and for public reporting of repeated and substantial violations. We would recommend amending these provisions in two respects, however.

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First, we believe that the bill should provide that, in the first instance, a violating bank should be required to notify individual borrowers of violations on standard forms prescribed by the enforcement agencies and that the agencies have this responsibility only if the bank refuses to do so. Secondly, we recommend that in the case of substantial and repeated violations, the agencies should be mandated either to publish the details of such violations as the bill presently provides or to proceed administratively against the bank by cease-and-desist action.

We favor extending the statute of limitations for civil damage actions. The present limitations period of one year from the transaction date effectively deprives many borrowers of legal redress. The one year period is inadvisable because examinations often uncover errors after one year from the transaction date. The new statute of limitations proposal in S. 1312 would solve this problem and would mesh with the disclosure procedures contemplated in the bill.

We have no comment on the S. 1312 provision which would permit State officials to examine federally chartered financial institutions for compliance with State Truth in Lending requirements except to note that it has been our experience that State authorities are capable of effectively enforcing State consumer protection laws as to State banks regularly examined by FDIC. Accordingly, there seems to us to be considerable merit in considering Federal withdrawal from enforcement of these laws where State enforcement methods meet necessary minimum standards. We assume that Congress will also want to resolve this problem without imposing duplicative and costly enforcement procedures on federally chartered institutions.

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S. 1653

In introducing S. 1653, Mr. Chairman, you stated that it was not intended to be a comprehensive revision of the Truth in Lending Act like Senator Proxmire's S. 1312. Instead, you indicated that S. 1653 was designed to address certain specific problems which have arisen in implementing the Act. Essentially, S. 1653 would authorize the Federal Trade Commission, which enforces the Act with respect to about 90 percent of the Nation's creditors, to obtain restraining orders in U.S. district courts and seek civil penalties and restitution to enforce compliance with Truth in Lending requirements. S. 1653 would also make several other amendments to the Act recommended by the FTC. The FTC amendments would, for example, provide (1) that assignees are liable for violations on the face of disclosure statements and that an obligor's exercise of the right of rescission is effective as to any assignee, (2) that a consumer's right to rescind is not cut off by a creditor's foreclosure sale of the consumer's home, (3) that the notice of billing rights mailed to consumers under the Fair Credit Billing Act should list the types of errors to which the Act applies, and (4) that creditors should credit to the accounts of customers any balances over $1.00 resulting from excess payments or rebates.

We have no objection to any of the provisions in S. 1653. As noted above, the financial institution regulatory agencies already have administrative cease-and-desist authority to enforce Truth in Lending requirements (including power to order affirmative remedial action by creditors). Therefore, the authority sought by the FTC to seek immediate judicial enforcement would seem unnecessary in the case of the financial agencies.

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S. 1501

S. 1501 contains some of the same provisions as S. 1312 but it goes much further in many respects. Generally speaking, we have no problems with those provisions of S. 1501 which implement Federal Reserve Board recommendations. Your Subcommittee may want to consider whether other provisions of the bill would enhance the consumer protection goals of the Truth in Lending Act.

For example, S. 1501 provides that a creditor would not be civilly liable if the failure to disclose was not material to the consumer's awareness of the cost of credit. The bill would relieve creditors of the duty to make disclosures with respect to late payment penalties, the existence of a security interest and identification of the property subject thereto, and the borrower's right of rescission. We believe these matters should properly be disclosed as required under present law and S. 1312.

S. 1501 would also establish a general principle of preempting all similar State laws except those that are identical to the federal law or those that are both more protective of consumers and necessary because of special local circumstances. While we agree the preemption area needs clarification, we question whether State authority in this area should be so severely curtailed as S. 1501 would do. We would prefer the provision in the Federal Reserve Staff proposal which permits the Federal Reserve Board to exempt credit transactions in any State which imposes substantially similar requirements as under Federal law and where there is adequate provision for enforcing such State requirements.

In order to limit form changes to once a year and give lead time for necessary printing and programming, another provision in S. 1501 would provide generally that the effective date of any statutory, regulatory, or interpretive

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change requiring a change in a disclosure form would be October 1 of the following year, unless the Federal Reserve Board determines that an earlier effective date is necessary to prevent unfair or deceptive practices. Although such a provision would certainly be helpful to creditors in adjusting to new requirements, we do not believe the Federal Reserve has been unreasonable about providing lead time and would therefore defer to them as to the workability of such a deferred effected date in achieving the purposes of the Act.

Federal Reserve Proposal

The Federal Reserve draft bill contains several provisions quite similar to comparable provisions in S. 1312. It provides, for example, for issuance by the Federal Reserve of model disclosure forms in everyday language, for the exemption of agricultural credit from Truth in Lending coverage, and for a substantial reduction in the number of items which need to be disclosed in a Truth in Lending statement. Also, as alluded to above, the Federal Reserve draft bill would substantially revise the definition of finance charge in Section 106 of the Act to include a number of items previously excluded, such as fees for credit reports and appraisals, for the preparation of deeds and other documents (except in residential mortgage transactions), and for perfecting security interests. All these changes are intended to reinforce the notion that the finance charge should contain all those charges which are unique to a credit transaction.

In residential mortgage transactions, the creditor would be permitted to exclude from the finance charge fees for title examination, surveys and mortgagor's title insurance. With the exception of mortgagor's title insurance,

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such fees should not be excluded from the finance charge if required by the lender as a condition of the credit. Other changes are also recommended in the Federal Reserve proposal to conform disclosure requirements in residential mortgage transactions to those contained in the Real Estate Settlement Procedures Act.

Under present law credit life, health and accident insurance premiums need not be included in the finance charge if its purchase is at the borrower's option. The Federal Reserve draft bill presents two alternatives on this controversial issue. One alternative would include such premiums in the finance charge on the rationale that in some localities such insurance is traditional despite its ostensible voluntariness. The other would require inclusion unless the consumer has an absolute right to cancel the insurance in a reasonable time period. We favor inclusion of such premiums in the finance charge in all cases. This we believe is the simpler approach. Moreover, it should be noted that credit life, accident or health insurance is unique to a credit transaction and is not present in a cash transaction. Therefore, where insurance is to be purchased, whether or not voluntarily, its cost should be included as a cost of credit. In our view, this change would reflect the reality that, in many cases, borrowers are lead to believe credit insurance is mandatory despite representations or written disclosures to the contrary. In these cases, it is difficult, if not impossible, to prove that the required representations or disclosures of voluntariness were overridden by by other statements of the creditor. Consequently, the issue of including or excluding the cost should not be made to turn upon the supposed "voluntariness" of the insurance.

We fully support the simplification provisions contained in the Federal

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Reserve draft proposal and would urge that its elements be combined with those of S. 1312 and S. 1653, and perhaps certain portions of S. 1501, to produce a composite simplification bill. This would be a major step in the direction of making the consumer protection provisions of the Truth in Lending Act more effective. We believe that in these pending proposals your Subcommittee has before it all the elements necessary to make a very significant contribution to better implementation of Truth in Lending objectives and we would be happy to work with your Subcommittee in any effort to combine the best elements of these bills to achieve this objective.

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