

Applicability of the Federal Truth in Lending Act to Rental Purchase Contracts

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NOTES

THE APPLICABILITY OF THE FEDERAL TRUTH IN LENDING ACT TO RENTAL PURCHASE CONTRACTS

Since its enactment by Congress in 1968, the Truth In Lending Act¹ has been an important, if controversial, attempt to protect consumers using credit.² Requiring uniform disclosure of all

¹ Consumer Credit Protection Act of 1968, Pub. L. No. 90-321, 82 Stat. 146 (codified at 15 U.S.C. §§ 1601-1667e (1976)).

² Commentators vigorously debate the Act's impact on consumer credit transactions. Supporters of the Act emphasize its beneficial effects. First, the percentage of consumers aware of prevailing annual percentage rates (APR) for ordinary loans increased significantly between 1969 and 1977. [1977] FRB Truth-In-Lending Ann. Rep. reprinted in [1978] INVEST. CRED. GUIDE (CCH) app. A, at 21 [hereinafter cited as 1977 ANN. REP.]; *Truth In Lending Simplification and Reform Act: Hearings on S. 108 and S. 37 Before the Senate Comm. on Banking, Housing, and Urban Affairs*, 96th Cong., 1st Sess. 1 (1979) (statement of Senator Proxmire) [hereinafter cited as 1979 TIL SIMPLIFICATION HEARINGS]. Second, despite the "inherent limitations" of the benefits of disclosure for "high risk" credit users, many of whom lack formal education, disclosure has made relatively well-educated and moderately affluent consumers sufficiently aware of credit costs "to bring about effective rate (price) competition . . . in the general market." NATIONAL COMMISSION ON CONSUMER FINANCE, CONSUMER CREDIT IN THE UNITED STATES 177-78 (1972) [hereinafter cited as NCCF REPORT]. Third, disclosure of the "fluctuating cost of closed end credit" to consumer credit users enhances overall "economic stabilization" by enabling consumers to "observe and react" to changing credit costs and adjust their uses of credit by taking into account APR variations. *Id.* at 184. See 1977 ANN. REP., *supra*, at 23-24. See generally Garwood, *A Look At Truth In Lending—Five Years After*, 14 SANTA CLARA LAW. 491 (1974).

Critics of the Act dispute these assertions and contend that Truth In Lending disclosures have had a minimal effect on consumer behavior in credit transactions. See Kripke, *Gesture and Reality in Consumer Credit Reform*, 44 N.Y.U. L. REV. 1, 1-11 (1969); Note, *Truth In Lending: The Impossible Dream*, 22 CASE W. RES. L. REV. 89 (1970); Note, *The Impact of Truth In Lending on Automobile Financing—An Empirical Study*, 4 U. CALIF. D. L. REV. 179 (1971). They argue that disclosure has proved particularly ineffective for the low-income consumer. See NCCF REPORT, *supra*, at 179; Harrison, *The Consumer Credit System and the Low-Income Consumer*, 13 J. FAM. L. 1, 7 (1973-74) ("While the need for [disclosure] would not be questioned, its effectiveness would appear to be somewhat diminished where the lowest socio-economic groups are involved.") (citing D. CAPLOVITZ, *DEBTORS IN DEFAULT* (1970)); Note, *Consumer Legislation and the Poor*, 76 YALE L.J. 745 (1967). See also COMMISSION ON FEDERAL PAPERWORK, CONSUMER CREDIT PROTECTION 13 (1977) (asserting inadequacy of increases in consumer awareness of APRs) (citing Mandell, *Consumer Perception of Incurred Interest Rates: An Empirical Test of the Efficacy of Truth-In-Lending*, 26 J. FINANCE 1143 (1971)).

Both advocates and critics claim that independent studies evaluating the effectiveness of the Truth In Lending Act support their positions. For example, after an extensive reevaluation of several empirical studies, one commentator concludes that there is "considerable evidence to support the contention of the critics of disclosure regulation[s] . . . [that] truth-in-lending, has had little impact on consumer purchasing behavior." Whitford, *The Functions of Disclosure Regulation in Consumer Transactions*, 1973 WIS. L. REV. 400, 469. He notes, however, that the benefits of truth in lending disclosure regulation "may marginally exceed its costs." *Id.* at 435. The Act's impact is limited, Professor Whitford suggests, because retailers use inadequate methods to communicate disclosed information to consum-

charges associated with the extension of consumer credit, the Act seeks to promote informed consumer use of credit and price competition in the consumer credit industry. Rental purchase contracts, however, threaten to undercut the Act's effectiveness. By dividing a lease into a series of short-term rental contracts with an option to purchase, merchants exploit the Act's literal language and evade the provisions regulating credit sales. The Federal Reserve Board, which is responsible for administering the Act,³ maintains that rental purchase contracts are beyond the scope of the Act. Most courts have deferred to the Board's position. This Note argues that both the Federal Reserve Board and the courts construe the Truth In Lending Act too narrowly. Because they are unlikely to abandon this restrictive construction, Congress should amend the Act's definition of "credit sale" so that it unambiguously encompasses rental purchase contracts and subjects them to the Truth In Lending Act's credit sale provisions.

I

THE TRUTH IN LENDING ACT

Prior to the enactment of the Truth In Lending Act, confusion prevailed in the consumer credit field.⁴ Creditors expressed finance charge rates and total sales amounts in different, incomparable ways;⁵ some, simply quoting monthly dollar payments,

ers. *Id.* at 469-70. Some commentators, however, challenge the methodology and interpretations of empirical research. See, e.g., NATIONAL CONSUMER LAW CENTER, S. 108: THE FRB'S 1977 CONSUMER CREDIT SURVEY DOES NOT SUPPORT S. 108 OR YOU ASK A STUPID QUESTION YOU GET A STUPID ANSWER (1979) (criticizing Federal Reserve Board's 1977 consumer awareness survey), reprinted in 1979 TIL SIMPLIFICATION HEARINGS, *supra*, at 44-47.

³ See note 36 and accompanying text *infra*.

⁴ See *Truth In Lending—1967: Hearings on S. 5 Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking and Currency*, 90th Cong., 1st Sess. 41-42 (1967) (statement of Senator Douglas, chairman of the National Commission on Urban Affairs) [hereinafter cited as 1967 SEN. TIL HEARINGS] Congressman Halpern noted that "[t]he loan shark and the credit deceiver have always had the benefit of complexity and confusion." *Id.* at 444. For an account of the development of the American consumer credit industry and the movement towards requiring credit cost disclosure, see NCCF REPORT, *supra* note 2, at 5-21. For a review of state consumer credit legislation schemes prior to the Truth In Lending Act, see Curran, *Legislative Controls as a Response to Consumer-Credit Problems*, 8 B.C. INDUS. & COM. L. REV. 409 (1967); Jordan & Warren, *A Proposed Uniform Code for Consumer Credit*, 8 B.C. INDUS. & COM. L. REV. 441, 441-49 (1967).

⁵ Creditors have employed several different methods of calculating finance charges. (1) The "add-on" rate is an expression of the finance charge as a dollar amount per year, calculated with respect to the unpaid balance *at the outset*. For example, the creditor might have stated the charge on a four-year, \$3,000 loan as "\$6.00 per \$100," indicating a total charge of \$720 (\$180/yr. x 4 yrs). The APR on this loan would be 12.5%. See NCCF

made no rate disclosures at all.⁶ Such inconsistent practices precluded consumers from comparison shopping for credit terms.⁷ As the credit industry expanded rapidly⁸ and the number of personal bankruptcies increased,⁹ the need for complete and uniform disclosure of credit information became pressing. Consumers needed information to enable them to compare credit costs.

REPORT, *supra* note 2, at 169. (2) The "discount" rate expresses the periodic charge in dollars per \$100 of unpaid balance, and is calculated *after deducting* the entire credit fee from the note's initial face amount. The APR on the "\$6.00 per \$100" charge in the above example would be 19.5%. (3) The "monthly" rate states a monthly percentage calculated on a defined balance. The APR, not compounded, would be 12 times the quoted figure. At a monthly rate of 1.25%, for example, the APR would be 15%. Some retailers employ a combination of rate charge methods. Such "fragmentation" involves separating the total finance charge "so that part appeared as an add-on or discount rate and part as a flat fee or extra charge." A retailer, for example, might charge "8 percent a year discount (to 18 months)" plus a predetermined fee of "8 percent on the first \$600 of initial unpaid balance." A \$500 loan for six months would result in a charge of \$68.14, reflecting an APR of 46.33%. *Id.* See AMERICAN ENTERPRISE INSTITUTE, THE "TRUTH-IN-LENDING" BILL 2-3 (1967) [hereinafter cited as AEI LEGISLATIVE ANALYSIS]; 113 CONG. REC. 18400 (1967) (statement of Senator Proxmire).

⁶ See NCCF REPORT, *supra* note 2, at 169.

⁷ Consumers' inability to shop comparatively for credit resulted from a lack of knowledge about finance charges and interest rates. Before the Truth In Lending Act became effective in 1969, the Board of Governors of the Federal Reserve System conducted a survey to determine levels of consumer awareness of finance charges and interest rates on their personal debts. Of the households surveyed, less than one-half of consumers with appliance and furniture loans claimed to know the interest rates on their debts. Consumers with low incomes or low education levels were even less aware. Of respondents with annual incomes under \$5,000, more than three-fourths did not know the annual percentage rates of interest on their loans. Of those with incomes under \$5,000 claiming knowledge of their interest rates, more than half unrealistically estimated the annual percentage rates on their credit use to be 7% or less. See [1969] FRB Truth-In-Lending Ann. Rep. reprinted in [1970] INV. CRED. GUIDE (CCH) app. B, at 1-13 (CCH 1970). For a review of surveys documenting the difficulties consumers faced in comparing finance charges, see NCCF REPORT, *supra* note 2, at 170.

⁸ In 1945, the total consumer credit debt was \$5.5 billion. By March 1967, consumers owed \$92.5 billion in short-term and immediate debt. See 113 CONG. REC. 18423 (1967) (remarks of Senator Morse). In 1967, \$73.6 billion represented installment credit held by financial institutions and retail outlets. 53 FED. RES. BULL. 834 (1967). See also S. REP. NO. 392, 90th Cong., 1st Sess. 1-6 (1967). According to the National Commission on Consumer Finance, this extraordinary growth was a result of

rising discretionary income, the urbanization of the population, and the influx of younger consumers into the market. A particularly important influence has been the trend to home ownership and its accompanying shift to owned durable goods in substitution for purchased services. The growth of asset ownership has also been stimulated by the increased number of women in the work force.

NCCF REPORT, *supra* note 2, at 21.

⁹ In the early 1960's, the rate of nonbusiness bankruptcies rose from 73 per 100,000 persons to 85 per 100,000. In 1967, nonbusiness bankruptcies reached a high of 98 per 100,000 population. In 1968, the rate dropped to 92 per 100,000, and declined again in 1969 to 85 per 100,000. See NCCF REPORT, *supra* note 2, at 19.

Few lenders, however, disclosed a simple annual percentage rate for fear of suffering a competitive disadvantage.

Legislators recognized the need for reform to protect consumers. Eight years after the introduction of the first legislation requiring full disclosure of credit costs,¹⁰ Congress enacted the Truth In Lending Act as Title I of the 1968 Consumer Credit Protection Act.¹¹ The Act requires that prior to extending credit, a lender must disclose information¹² that Congress has deemed relevant to the particular type of credit transaction.¹³ These re-

¹⁰ See S. 2755, 86th Cong., 2d Sess., 106 CONG. REC. 97 (1960). When Senator Douglas introduced the bill—popularly known as the “interest-rate labelling bill”—he remarked: “This bill would require that [the consumer] be given, in writing, two vital pieces of information: First, the total amount of the finance charges he is contracting to pay; and, second, the percentage that such an amount bears to the outstanding balance expressed in simple annual interest.” *Id.* The Subcommittee on Production and Stabilization of the Senate Committee on Banking and Currency, chaired by Senator Douglas, conducted hearings on the bill and reported it to the full Committee, which took no action. The bill died upon adjournment of the 86th Congress.

In succeeding years credit disclosure legislation received similar treatment. After Massachusetts’ enactment of a truth in lending bill and pressure from the Johnson Administration for a similar federal enactment, the Senate in 1967 passed S. 5, adapted and derived from Senator Douglas’ 1960 proposal. See S. 5, 90th Cong., 1st Sess., 113 CONG. REC. 18424 (1967). The House, which was also actively considering comprehensive consumer protection legislation in 1967, see H.R. 11601, 86th Cong., 2d Sess., reprinted in *Consumer Credit Protection Act: Hearings on H.R. 11601 Before the Subcomm. on Consumer Affairs of the House Comm. on Banking and Currency*, 90th Cong., 1st Sess. (1967), deleted all language of S. 5 after the enacting clause, inserted the text of the House bill, and returned it to the Senate. On May 20, 1968, the Conference Committee accepted a compromise S. 5, which Congress enacted into law nine days later. See CONF. COMM. REP. NO. 1397, 90th Cong., 2d Sess., reprinted in [1968] U.S. CODE CONG. & AD. NEWS 1962, 2021. For the legislative history of S. 5 and a synopsis of the major issues, see AEI LEGISLATIVE ANALYSIS, *supra* note 5, at 1-5, 8-44.

¹¹ Consumer Credit Protection Act of 1968, Pub. L. No. 90-321, 82 Stat. 146 (codified at 15 U.S.C. §§ 1601-1667e (1976)).

¹² The Act requires, prior to extension of consumer credit, complete and conspicuous disclosure of finance charges, expressed both in dollar amount and as an annual percentage rate. 15 U.S.C. § 1631 (1976). “Credit” means the right that a creditor gives a debtor to incur debt and defer its payment. 15 U.S.C. § 1602(e) (1976). The finance charge is the sum of most charges payable by the debtor—whether the creditor imposes them directly or indirectly—as an incident of credit extension. 15 U.S.C. § 1605(a) (1976). In addition to these general requirements, the creditor must satisfy the disclosure requirements applicable to his credit plan. See note 13 and accompanying text *infra*.

¹³ The Act divides credit plans into three categories: (1) open end credit plans, 15 U.S.C. § 1637 (1976); (2) sales not under open end credit plans, 15 U.S.C. § 1638 (1976); and (3) consumer loans not under open end credit plans, 15 U.S.C. § 1639 (1976). An open end or “revolving credit” plan allows a debtor to maintain an account with a creditor, who may extend credit repeatedly. Under a closed end credit plan the creditor extends credit in a single transaction. The debtor pays the total debt over a fixed period of time. See Davis, *Protecting Consumers From Overdisclosure and Gobbledygook: An Empirical Look at the Simplification of Consumer-Credit Contracts*, 63 VA. L. REV. 841, 845 n.17 (1977).

quirements vary, but generally include disclosure of the amount financed, the finance charge, the annual percentage rate, time-sale price and time balance, prepayment procedures, rebates, delinquency charges, and any security interests.¹⁴ Because certain requirements apply only to "credit sales", the Act's definition of "credit sale" significantly restricts the scope of the statute.

Section 103(g) of the Truth In Lending Act defines a "credit sale" as:

any sale with respect to which credit is extended or arranged by the seller. The term includes any contract in the form of a bailment or lease if the bailee or lessee contracts to pay as compensation for use a sum substantially equivalent to or in excess of the aggregate value of the property and services involved and it is agreed that the bailee or lessee will become, or for no other or a nominal consideration has the option to become, the owner of the property upon full compliance with his obligations under the contract.¹⁵

Thus, any lease is a credit sale if the lessee: (1) "contracts to pay" a sum substantially equivalent to, or in excess of, the aggregate value of the lease-property, and (2) has the option to purchase the property for no more than a nominal sum.¹⁶

Congress believed that more knowledgeable use of credit would promote economic stability and competition within the credit industry.¹⁷ It expressly designed the Act "to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit."¹⁸ An implied purpose of the Truth In Lending Act was to expose and thereby eliminate

¹⁴ See 15 U.S.C. §§ 1637-1639 (1976). Separate disclosure requirements apply to each credit plan category. See note 13 *supra*.

¹⁵ 15 U.S.C. § 1602(g) (1976).

¹⁶ *Id.*

¹⁷ See *id.* § 1601(a).

¹⁸ *Id.* According to the National Commission on Consumer Finance, Congress designed the Truth In Lending Act to serve three functions: a shopping function, a descriptive function, and an economic stabilization function. See NCCF REPORT, *supra* note 2, at 171-74. The Act serves the shopping function by enabling consumers to shop comparatively for credit prices. Comparison shopping should help consumers avoid high-cost credit and stimulate price competition among creditors. *Id.* at 172. The object of the descriptive function is to assist consumers in choosing whether to use credit, use liquid assets, or delay consumption. *Id.* The economic stabilization function serves the dual purposes of preventing consumers from incurring excessive indebtedness and regulating credit use during fluctuations in the economy. *Id.* at 174.

unscrupulous credit practices.¹⁹ Drafting legislation to effectuate this purpose was difficult because, as the Supreme Court has noted, "some creditors would attempt to characterize their transactions so as to fall one step outside whatever boundary Congress attempted to establish."²⁰ Such attempts to circumvent the Act, if successful, subvert its effectiveness and leave consumers without the protection envisioned by Congress.

II

THE EXCLUSION OF RENTAL PURCHASE CONTRACTS

A. *Rental Purchase Contracts as Unregulated Merchandising Devices*

In recent years, retailers of consumer durable goods have introduced a novel merchandising device—the rental purchase contract—into the highly competitive consumer credit market.²¹

¹⁹ Proponents of the Act were aware that strong opposition within the credit industry had hampered credit regulation efforts in the past. To avoid antagonizing the credit industry unnecessarily, the Act's proponents may have strategically refrained from emphasizing, as one of their goals, the policing of creditors' practices: "The bill contains no assumptions that consumer credit is bad or that the vast majority of those who extend consumer credit are engaged in deceitful practices. The bill contains no indictment of the credit industry as a whole." S. REP. NO. 392, 90th Cong., 1st Sess. 2 (1967).

²⁰ *Mourning v. Family Publications Serv.*, 411 U.S. 356, 365 (1973). Congress was acutely aware that creditors might attempt to avoid the Truth In Lending Act's disclosure requirements by manipulating the forms of their transactions. See, e.g., *Truth In Lending Bill: Hearings on S. 1740 Before the Subcomm. on Production and Stabilization of the Senate Comm. on Banking and Currency*, 87th Cong., 1st Sess. 49, 56-57 (1961) (statement and testimony of J. Tohin, Council of Economic Advisers); *id.* at 389-90 (testimony of A. Haring, consultant, National Retail Furniture Association); *id.* at 447-48 (testimony of Andrew Bumiller, Director, Department of Legislation, AFL-CIO); *id.* at 563-64 (remarks of Senator Bennett); 1155-56 (remarks of Senator Douglas); *Truth In Lending Bill: Hearings on S. 1740 Before the Subcomm. on Production and Stabilization of the Senate Comm. on Banking and Currency*, 87th Cong., 2d Sess., Pt. 2, at 296 (statement of L. Rothschild, Executive Director, Menswear Retailers of America); 1967 SEN. TIL HEARINGS, *supra* note 4, at 702-03 (statement of D. Marlin, Neighborhood Legal Services Project of Washington, D.C.).

In 1979, the Senate Committee on Banking, Housing and Urban Affairs recommended amending the definition of open end credit plans (15 U.S.C. § 1637 (1976)) to curb the use of "spurious" open end credit (characterization of a one-time credit extension as a purchase on an "open end" or "revolving charge" plan). See S. REP. NO. 73, 96th Cong., 1st Sess. 10 (1979).

²¹ The advantages of consumer credit for retailers derive from the purchasing incentives that credit availability gives to customers. To promote these incentives, many creditors in the early 1960s focused sales efforts on consumers with low incomes. See FEDERAL TRADE COMM'N, ECONOMIC REPORT ON INSTALLMENT CREDIT AND RETAIL SALES PRACTICES OF DISTRICT OF COLUMBIA RETAILERS, MARCH 1968, reprinted in *Consumer Credit and the Poor: Hearings Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking and Currency*, 90th Cong., 2d Sess. 37, 51 (1968) [hereinafter cited as FTC CREDIT PRACTICES REPORT (1968 HEARINGS)]. Such creditors, however, typically sold goods at prices far in excess of market value, *id.* at 39, 107, and disguised total credit charges and credit rates

Rental purchase contracts are short term leases that give the lessee the option to purchase the merchandise.²² They bind consumers to pay short-term rental fees. At the end of a rental term, the agreement automatically terminates and the customer must return the property, unless he renews the contract by paying the fee for another term.²³ The retailer has the right to collect rent while the consumer possesses the goods, and to recover the goods, plus damages for diminished value, excepting normal wear and tear, at the end of the term. The retailer retains title to the goods but must provide maintenance and pay any property taxes.²⁴

The central feature of the rental purchase contract, however, is the option it gives the consumer to purchase the property by simply renewing the agreement for a specified number of successive terms. This purchase option,²⁵ along with low weekly payments and the lack of an initial down payment, makes the rental purchase contract particularly attractive to low-income consumers²⁶ who have been closed out of more traditional credit mar-

as "fees, charges, discounts, and the like. . ." 106 CONG. REC. 97 (1960) (statement of Senator Douglas). See, e.g., FTC CREDIT PRACTICES REPORT (1968 HEARINGS), *supra*, at 99; 1967 SEN. TIL HEARINGS, *supra* note 4, at 700-02.

²² See SAMPLE RENTAL PURCHASE CONTRACT at Appendix *infra*. The reprinted sample is the form contract at issue in *Johnson v. McNamara*, No. H-78-238 (D. Conn. Apr. 12, 1979). The lessor in *Johnson* asserted that the rental agreement typified those used in other transactions. See Ruling on Motions for Summary Judgment and To Dismiss, *Johnson v. McNamara*, No. H-78-238 (D. Conn. Apr. 12, 1979). Similarly, several courts have noted that the terms of the contracts they construed contained contractual terms resembling those that the Federal Reserve Board described in its staff opinion letters. See note 37 *infra*.

Further highlighting the general similarity between rental purchase contracts employed by different retailers is the fact that a national manufacturer of televisions and stereos provides franchised dealers with a form rental purchase contract that the dealers may use at their option. Moreover, there is notable similarity among rental purchase contracts that have been the subject of disputes resulting in litigation. For example, the plaintiff's attorney in *Turner v. Curtis Mathes Centers, Inc.*, No. 3-78-1135 (D. Minn. Mar. 1979), commented that the disputed rental agreement was identical to the contract that another court construed in *Johnson v. McNamara*, No. H-78-238 (D. Conn. Apr. 12, 1979). Telephone interview with Jerry Lane, Esq., Minnesota Legal Services (Oct. 15, 1979).

²³ See SAMPLE RENTAL PURCHASE CONTRACT at Appendix *infra*.

²⁴ *Id.*

²⁵ Rental purchase contracts specify the number of successive renewals required before exercising the purchase option. A standard form rental purchase contract may indicate, for example, that "[i]n the event renter at his sole election renews this rental agreement for one hundred four successive one-week terms, owner will transfer the property to renter." See SAMPLE RENTAL PURCHASE CONTRACT at Appendix *infra* (emphasis added). Such language clarifies that the lessee retains power to avoid a complete transfer of title.

²⁶ See notes 27-28 and accompanying text *infra*. One commentator has noted that "[r]etailers who sell to lower-income consumers use installment credit in a much higher percentage of their sales than do retailers selling to the general public." Harrison, *supra*

kets.²⁷ Without other sources of credit, the low income consumer may view the rental purchase contract as his only means of obtaining certain household goods.²⁸ Because they provide a convenient means to finance the purchase of consumer goods, rental purchase contracts are functionally equivalent to credit sales.²⁹

Despite their similarity to credit sales, rental purchase contracts are not currently regulated under the Truth In Lending Act.³⁰ Retailers employing rental purchase contracts can keep transactions beyond the Act's scope by literally interpreting the Act's "credit sale" definition. They argue that rental purchase contracts do not meet the definition's first condition, which requires that the lessee be contractually bound to pay a sum equal to or greater than the value of the property.³¹ On their face they ap-

note 2, at 3. A Federal Trade Commission study of credit use found that installment credit was widely used to market appliances and home furnishings to low-income families and that, as a group, retailers selling to a low-income market made about 93% of their sales through installment credit. See FTC CREDIT PRACTICES REPORT (1968 HEARINGS), *supra* note 21, at 40. The study concluded that "[w]hat competition there is among low-income market retailers apparently takes the form of easier credit availability, rather than of lower prices." *Id.* at 41. See generally D. CAPLOVITZ, THE POOR PAY MORE: CONSUMER PRACTICES OF LOW-INCOME FAMILIES (1963) (case study of low-income market retailers in New York).

Low-income consumers seeking credit typically rely on retail stores to make the arrangements. A study of consumer awareness of annual percentage rates revealed that "just over half of middle and upper income whites relied on the retailer to provide or arrange credit." NCCF REPORT, *supra* note 2, at 180. However, "[i]n contrast, four-fifths of minority customers depended on the dealer, and about seven-tenths of low-income (under \$7,500) whites" either used the retailer's installment charge plan or let the dealer make other arrangements. *Id.*

²⁷ According to the National Commission on Consumer Finance, the low-income consumer's heavy dependence on dealers for credit results from a paucity of other legal credit sources. See NCCF REPORT, *supra* note 2, at 180. As the Commission observed, "[t]here are no small loan offices in Harlem or the District of Columbia. There are relatively few low-income members of credit unions. . . . Direct bank credit is also generally less available in the high-risk market." *Id.* at 180-81. See 1967 SEN. TIL HEARINGS, *supra* note 4, at 699, 702 (statement of David H. Marlin, Deputy Director for Law Reform and Education, Neighborhood Legal Services Project of Washington, D.C.).

²⁸ See note 27 and accompanying text *supra*. The absence of alternative credit sources prompts low-income consumers to endure the disadvantageous aspects of rental purchase contracts. See note 33 *infra*.

²⁹ Retailers typically seek to avoid the characterization of the rental purchase contract arrangement as a "credit sale" by including bold-faced provisions such as the caption "This is a Rental Agreement Only." See, e.g., SAMPLE RENTAL PURCHASE CONTRACT at Appendix *infra*. The appropriate characterization of such arrangements, however, remains unclear, because legislative, administrative, and judicial efforts to demarcate a clear definitional distinction between rental purchase contracts and "credit sales," for purposes of determining the applicability of the Truth In Lending Act, have been unsatisfactory. See notes 75-94 and accompanying text *infra*.

³⁰ See notes 36-39, 43-46, and accompanying text *infra*.

³¹ See text at notes 15-16 *supra*.

pear not to fulfill this condition because they do not obligate a lessee to pay rent beyond a single term.³² In addition, such agreements do not require payments to equal or exceed the property's value; they divide what would ordinarily be a lease agreement in which the rental fee would equal or exceed the value of the property into a series of short term, renewable contracts, each requiring payment of a rental fee substantially less than the value of the property.³³ Rental purchase contracts, therefore, arguably fall outside the literal terms of the Truth In Lending Act's "credit sale" definition,³⁴ and may be exempt from the Act's regulations.³⁵

³² See note 25 and text accompanying notes 15-16 *supra*.

³³ See note 25 *supra*.

³⁴ The consumer's express power to stop payments and terminate the arrangement contrasts with the mandatory "contracts to pay" requirement in the pivotal "credit sale" definition. Indeed, the lessee under a rental purchase contract renews "at his sole election", see note 28 *supra*, whereas the person acquiring property in a credit sale "contracts to pay . . . a sum" without reservation. See text accompanying notes 15-16 *supra*.

³⁵ More persuasive grounds support the exemption of rental purchase contracts from the Truth In Leasing Act, which Congress enacted in 1976. Consumer Leasing Act of 1976, Pub. L. No. 94-240, 90 Stat. 257 (codified at 15 U.S.C. §§ 1601, 1640, 1667-1667e (1976)). The Truth In Leasing Act defines a consumer lease as

[a] contract in the form of a lease or bailment for the use of personal property by a natural person for a period of time exceeding four months, and for a total contractual obligation not exceeding \$25,000 . . . whether or not the lessee has the option to purchase or otherwise become the owner of the property at the expiration of the lease, except that such term shall not include any credit sale as defined in section 1602(g) of this title.

15 U.S.C. § 1667 (1976) (emphasis added). Because a rental purchase contract does not bind the lessee to rent beyond a single short-term period, the mandatory rental term is invariably shorter than four months. This renders the disclosure requirements of the Truth in Leasing Act inapplicable. See note 90 *infra*.

Accordingly, the Federal Reserve Board maintains that leases similar to rental purchase contracts are exempt from Truth In Leasing disclosure requirements because they do not meet the four-month term requirement. In an unofficial staff opinion letter discussing whether leases for respective terms of four months, three months, and month-to-month were "consumer leases," the Board stated:

It is the staff's opinion that none of the [rental purchase] contracts . . . is a "consumer lease" under the Consumer Leasing Act or Regulation Z. . . . [A] lease of personal property . . . on a month-to-month basis (even though the lease extends beyond four months) is not a consumer lease within the meaning of the Act and would not be subject to the disclosure requirements of Regulation Z. . . .

Fed. Res. Bd. Letter No. 1169 (March 28, 1977), reprinted in [1974-1977 Transfer Binder] CONS. CRED. GUIDE (CCH) ¶ 31,566. The Board added, however, that disclosure requirements of the Truth in Leasing Act do not apply only if "a term of four months or less is not employed by the lessor for the purpose of circumvention or evasion of the statutory or regulatory requirements." *Id.* This reflects the Board's awareness that unconditional non-regulation of rental purchase contracts could open the door to abuse in certain situations.

B. *The Position of the Federal Reserve Board*

The Federal Reserve Board³⁶ has unofficially ruled that the Act does not encompass rental purchase contracts.³⁷ The Board claims that because the lessee's option to terminate the rental negates any obligation to pay full market value for the property, the transaction falls outside section 1602(g)'s definition of "credit sale."³⁸ The Board recommended in 1977 that Congress amend the credit sale definition to codify its administrative position.³⁹ Congress, however, did not act on the Board's proposal.

³⁶ Congress empowered the Federal Reserve Board to enforce disclosure under the Truth In Lending Act:

The [Federal Reserve] Board shall prescribe regulations to carry out the purposes of [the Act]. These regulations may contain such classifications, differentiations, or other provisions, and may provide for such adjustments and exceptions for any class of transactions, as in the judgment of the Board are necessary or proper to effectuate the purposes of [the Act], to prevent circumvention or evasion thereof, or to facilitate compliance therewith.

15 U.S.C § 1604 (1976). See text accompanying notes 36 & 75-77 *infra*.

³⁷ The Federal Reserve Board has issued three unofficial staff opinion letters concerning the regulation of rental purchase contracts. In response to an inquiry about whether the Truth In Lending Act and Regulation Z would apply to a rental agreement similar to the SAMPLE RENTAL PURCHASE CONTRACT at Appendix *infra*, a Board staff member advised that Regulation Z did not apply because the

lease agreement may be cancelled at any time, given 30 days prior notice, at no cost or penalty to the customer. . . . Therefore, a lessee under the plan [has not] contracted "to pay as compensation for the use a sum substantially equivalent to or in excess of the aggregate value of the property or services involved."

Fed. Res. Bd. Letter No. 750 (Jan. 11, 1974), *reprinted in* [1969-1974 Transfer Binder] CONS. CRED. GUIDE (CCH) ¶ 31,069, (quoting 12 C.F.R. § 226.2(n) (1975)).

In a second unofficial staff opinion letter, Jarauld C. Kluckman, Associate Director of the Board's Truth In Lending Section, reached the same conclusion: "In light of the consumer lessee's option to terminate without liability . . . we believe that the lease transaction referred to would not be subject to Regulation Z." Fed. Res. Bd. Letter No. 761 (Mar. 12, 1974), *reprinted in* [1969-1974 Transfer Binder] CONS. CRED. GUIDE (CCH) ¶ 31,083. Two years later, Mr. Kluckman reaffirmed his opinion in a third unofficial staff letter:

It is staff's opinion that the lease agreement in question does not fall within the definition of a "credit sale" because it does meet the first requirement as set forth in § 226.2(t) [of Regulation Z]. We note that the lease agreement contains an express provision permitting termination of the lease agreement at any time, by either party, upon 30 days prior written notice. Such termination by the lessee results in no penalty or additional cost being imposed upon the lessee. Therefore, the lessee . . . has not contracted "to pay as compensation for use a sum substantially equivalent to or in excess of the aggregate value of the property and services involved."

Fed. Res. Bd. Letter No. 1192 (June 15, 1977), *reprinted in* [1974-1977 Transfer Binder] CONS. CRED. GUIDE (CCH) ¶ 31,623, (quoting 12 C.F.R. § 226.2(t) (1975)).

³⁸ See note 34 *supra*. The Federal Reserve Board similarly claims that the rental purchase contract transaction is not subject to the disclosure requirements of the Truth In Lending Act, because it does not satisfy the four-month term requirement. See note 35 *supra*.

³⁹ See BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, DRAFT BILL ON SIMPLIFICATION OF TRUTH IN LENDING § 104(2) (1977), *reprinted in Simplify and Reform the Truth In*

The Board's refusal to classify rental purchase contracts as credit sales comports with its traditional reluctance to subject any arrangements that resemble leases to regulation under the Truth In Lending Act. In 1967, the Board recommended that because of the difficulty of computing finance charges on true leases,⁴⁰ Congress should draft the credit sale definition to exclude them from the proposed Truth In Lending Act. In 1975, the Board proposed that Congress amend the Act to exclude disguised leases as well.⁴¹ Congress, aware that excluding leases from the Truth In Lending Act might encourage installment creditors to use lease arrangements to avoid credit disclosure,⁴² declined to implement either proposal.

Lending Act: Hearings on S. 1312, S. 1501, and S. 1653 Before the Subcomm. on Consumer Affairs of the Senate Comm. on Banking, Housing and Urban Affairs, 95th Cong., 1st Sess. 60, 65 (1977). The Board proposed that the new definition include "instances where the consumer becomes contractually obligated to purchase property or services and cannot cancel without substantial penalty. . . . This would codify the present administrative construction of the Act." BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM: MEMORANDUM ANALYSIS ISSUES IN BOARD'S DRAFT BILL ON SIMPLIFICATION OF TRUTH IN LENDING (1977), reprinted in *Simplify and Reform the Truth in Lending Act: Hearings on S. 1312, S. 1501, and S. 1653 Before the Subcomm. on Consumer Affairs of the Senate Comm. on Banking, Housing and Urban Affairs, 95th Cong., 1st Sess. 48 (1977)*. The Board desired to provide "a more orderly way [of] making clear which transactions are covered." *Id.* See note 35 *supra*.

⁴⁰ During the 1967 Senate Truth In Lending hearings, Governor Robertson of the Federal Reserve Board testified that it is impossible to calculate a finance charge on a true lease. See 1967 SEN. TIL HEARINGS, *supra* note 4, at 663. Creditors compute finance charges on regular credit sales by reference to either the total amount financed, or the difference between the cash selling price and the deferred payment price; charges for rentals, however, derive from the use of property, not from its value. *Id.* See also *id.* at 353 (statement of Darrel M. Holt, Mortgage Bankers Association of America); *id.* at 401 (statement of Douglas Hewitt, Executive Secretary, Farm and Industrial Equipment Institute).

⁴¹ See, e.g., [1975] BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, ANN. REP. TO CONGRESS ON TRUTH IN LENDING App. B, at 5. The Board believed that the Truth In Leasing Act would suffice to cover lease arrangements that prove to be disguised credit sales. See *Truth-In-Leasing: Hearings on H.R. 4657 Before the Subcomm. on Consumer Affairs of the House Comm. on Banking, Currency and Housing, 94th Cong., 1st Sess. 31 (1975)*.

⁴² Congresswoman Leonor Sullivan, for example, questioned the advisability of removing disguised leases from the ambit of Truth In Lending regulation:

[I]f H.R. 4657 were to become law as introduced, including § 104(a) repealing the provisions of § 103(g) of the Truth In Lending Act applying to certain leases, would there not be an incentive to installment credit sellers to adopt consumer leases as a means of avoiding annual percentage-rate disclosure, so that one of the major purposes of Truth In Lending would be destroyed?

Equal Credit Opportunity Act Amendment to the Consumer Leasing Act of 1978: Hearings Before the House Comm. on Banking, Finance and Urban Affairs, 95th Cong., 1st Sess. 20, 21 (1978) (reprinting letter from Representative Sullivan to the Honorable Jeffrey Bucher, Federal Reserve System (July 8, 1978)). In response, Mr. Bucher stated:

While H.R. 4657 will not require the disclosure of an annual percentage rate, as would be the case under Truth In Lending, we doubt the practicality of requiring rate disclosures in connection with leasing.

C. Judicial Responses

Five out of the seven United States district courts that have considered the question have held that rental purchase contracts are not credit sales as defined by the Truth In Lending Act.⁴³ These courts found that the rental purchase agreements clearly provided that the lessee would become the owner of the property by paying the specified number of rental fees.⁴⁴ Nonetheless, the courts deferred to the Federal Reserve Board's position⁴⁵ and held that the transactions were not credit sales because they did not obligate the lessees to pay the full values of their lease property.⁴⁶

The two courts most recently confronting the issue, however, found that the rental purchase contracts involved were functionally equivalent to credit sales.⁴⁷ One court stated: "For all practi-

With reference to the question of whether a partial repeal of section 103(g) [15 U.S.C. § 1602(g)] would provide a loophole and incentive for certain creditors to convert their credit sale agreements into leases and, thus, avoid the requirement of disclosing annual percentage rates, we doubt that the complications involved in making such conversions to leases would lead creditors to change their agreements merely to avoid annual percentage rate disclosures.

id. at 31-32.

⁴³ *Dorsey v. Curtis Mathes Sales Co.*, No. 4-78 Civ. 436 (D. Minn. Mar. 23, 1979); *Turner v. Curtis Mathes Centers, Inc.*, No. 3-78-1135(D) (D. Minn. Mar. 1979); *Smith v. ABC Rental Sys., Inc.*, 491 F. Supp. 127 (E.D. La. 1978); *Clark v. Aquarius TV Rental, Inc.*, No. CA 4-77-133 (N.D. Tex. Oct. 18, 1977); *Terrell v. Mr. T's Rental*, No. C75-2053A (N.D. Ga. June 4, 1976); *Griggs v. Easy TV & Rental, Inc.*, No. C75-2509A (N.D. Ga. April 8, 1976). *But see* *Waldron v. Best T.V. & Stereo Rentals, Inc.*, 485 F. Supp. 718 (D. Md. 1979); *Johnson v. McNamara*, No. H-78-238 (D. Conn. Apr. 12, 1979).

⁴⁴ In *Smith v. ABC Rental Sys., Inc.*, 491 F. Supp. 127 (E.D. La. 1978), the written rental purchase contract did not contain an express purchase option, although the retailer had widely advertised it. The court, however, did not reach the issue of whether the lessee had a purchase option, because it found the lease did not meet the "contracts to pay" condition.

⁴⁵ See note 37 *supra*.

⁴⁶ The court in *Smith v. ABC Rental Sys., Inc.*, 491 F. Supp. 127 (E.D. La. 1978) did not cite the Board's opinion letters. In three other cases, the courts relied solely on the Federal Reserve Board letters (discussed at notes 35 & 37 *supra*). See *Clark v. Aquarius TV Rental, Inc.*, No. CA 4-77-133 (N.D. Tex. Oct. 18, 1977); *Griggs v. Easy TV & Rental, Inc.*, No. C75-2509A (N.D. Ga. Apr. 8, 1976); *Boyd v. ABC Rental Sys., Inc.*, No. C74-456-L(B) (W.D. Ky. Sept. 12, 1975). In *Terrell v. Mr. T's Rental*, No. C75-2503A (N.D. Ga. June 4, 1976) the court adhered to its holding in *Griggs* and dismissed the case with little additional discussion of the merits. Two recent courts cited *Smith*, *Clark*, *Terrell*, *Griggs*, *Boyd*, and the Federal Reserve Board letters in summarily rejecting the lessee's attempt to characterize the rental purchase contract as a conditional sales contract. See *Dorsey v. Curtis Mathes Sales Co.*, No. 4-73 Civ. 436 (D. Minn. Mar. 23, 1979); *Turner v. Curtis Mathes Centers, Inc.*, No. 3-78-1135(D) (D. Minn. Mar. 1979).

⁴⁷ *Waldron v. Best TV & Stereo Rentals, Inc.*, 485 F. Supp. 718 (D. Md. 1979); *Johnson v. McNamara*, No. H-78-238 (D. Conn. Apr. 12, 1979).

cal purposes, . . . the 'rental' relationship established by this form contract is indistinguishable from a credit sale, in which the creditor has agreed to sell the item to the debtor, the purchase price being payable over a two year period."⁴⁸ Both courts declined to adopt the Federal Reserve Board's position and held that the transactions could be credit sales subject to the Truth In Lending Act's provisions.⁴⁹

III

THE CONSEQUENCES OF EXCLUSION

A. *Effects on Retailers and Consumers*

Functionally equivalent to ordinary credit sales,⁵⁰ but not generally considered to be subject to the Truth In Lending Act's restrictions,⁵¹ rental purchase contracts are a highly attractive sales

In *Waldron*, the court relied upon prior cases decided under the state's Uniform Commercial Code in rejecting the argument that the rental purchase contract was not a credit sale. The court observed that agreements in prior cases had been characterized under the UCC as conditional sales, notwithstanding inclusion of a lessee's termination option. Further, public policy favored subjecting the disputed agreement to the Truth In Lending Act's provisions:

Under the terms of the agreement involved in this case, [the lessee] will own the television set if the 78 successive weekly payments are made. Yet, without the disclosure contemplated by the Act, [the lessee] faces a difficult problem in calculating the rate of interest being charged; practically, she is unable to shop for credit, and the purpose of the statute is frustrated.

Waldron v. Best TV & Stereo Rentals, Inc., 485 F. Supp. 718, 720 (D. Md. 1979).

⁴⁸ *Johnson v. McNamara*, No. H-78-238 slip op. at 4 (D. Conn. Apr. 12, 1979). The court found that Congress intended courts considering whether a transaction is a disguised sale or true lease to follow commercial law principles. The court reasoned that under the Uniform Conditional Sales Act and the Uniform Commercial Code, the issue of whether an agreement was a true lease or disguised sale typically depends on whether the contract permits the lessee to acquire title to the property.

In the court's view, conditional sales agreements and rental purchase contracts differ only because under the latter a lessee can cancel without incurring liability through a deficiency judgment. In Connecticut, however, the Retail Installment Sales, Financing, Trading Practices, Home Solicitation Sales Act prohibits the collection of deficiency judgments. *See* CONN. GEN. STAT. § 42-98(f) (1979). Therefore, the *McNamara* court reasoned, the legal obligations between the parties to a rental purchase contract are functionally the same as they would have been had the lessee unequivocally agreed to purchase the property through installments. Slip op. at 11.

The court concluded that the rental purchase contract was a credit sale within the meaning of the Truth In Lending Act. *Id.* The Court's decision hinged on the Connecticut Retail Installment Sales Act's prohibition of deficiency judgments in conditional sales. The court specifically declined to decide whether the Federal Reserve Board opinion letters correctly interpreted "credit sale." Slip op. at 14 n.3.

⁴⁹ *Waldron v. Best TV & Stereo Rentals, Inc.*, 485 F. Supp. 718 (D. Md. 1979) (denying motion for summary judgment); *Johnson v. McNamara*, No. H-78-238 slip op. at 11 (D. Conn. Apr. 12, 1979).

⁵⁰ *See* text accompanying notes 25-28 *supra*.

⁵¹ *See* text accompanying notes 30-34 *supra*; notes 36-39 and accompanying text *supra*.

device for retailers.⁵² By stating only a weekly rental fee, the retailer may conceal the costs of deferred payment as well as the total purchase price of the property. This allows him to reap the benefits of credit sales while avoiding the liabilities and regulations that the Truth In Lending Act imposes on other lenders. It also gives him an unfair competitive advantage over retailers offering conventional credit sales.⁵³

The exclusion of rental purchase contracts creates the same problems for credit consumers that led Congress to enact the Truth In Lending Act twelve years ago. Undisclosed credit information limits the consumer's ability to shop comparatively for the best deal,⁵⁴ and enables creditors to impose harsh, unfair terms on consumers,⁵⁵ who are left without the remedies provided by

⁵² Retailers using rental purchase contracts may derive substantial profits not available through other payment arrangements. They may, for example, receive as much as double the retail price of the item before transferring title to the consumer. In *Griggs v. Easy TV & Rental, Inc.*, No. C75-2509A (N.D. Ga. Apr. 8, 1976), the consumer rented a stereo for \$45 per week. Under the purchase option, the lessee would receive title after 18 consecutive weekly rentals, for a total lease-purchase price of \$810. The retailer admitted that the cash retail value of the stereo was only \$350. *Id.* at Exhibit "H" (recommendation of special master). Similarly, in *Turner v. Curtis Mathes Centers, Inc.*, No. 3-78-1135(D) (D. Minn., March 1979), the bi-weekly rental fee for a television set was \$31.10. The arrangement required 78 successive weekly rentals, equalling a total lease-purchase price of \$1212.90, before the lessee acquired ownership. The television, which previously had been rented to other customers, had a retail value of only \$773. *Id.*, slip. op. at 2.

If the consumer fails to exercise the purchase option, the retailer keeps all rental fees paid, regains possession of the lease property, and is free to sell the property or rent it again. *See id.* In *Turner*, the consumer paid the rental fee for 44 consecutive weeks, which represented approximately 88% of the \$773 retail value of the television. *See id.* When the consumer failed to renew the contract, however, the retailer retained the rental fees and rented the property again. *Id.*

Many consumers fail to maintain rentals beyond several months. *See Smith v. ABC Rental Sys. of New Orleans*, No. 77-2733, slip op. at 3 (E.D. La. Aug. 11, 1978) (retailer testified that 73% of customers kept goods less than four months).

⁵³ Unfair advantage may result from the favorable appearance of the transaction. Retailers offering ordinary credit sales must make disclosures pursuant to the Act. The absence of such disclosure in rental purchase contracts may cause consumers to presume that the retailer provides free credit. *See note 54 infra.*

⁵⁴ The Truth In Lending Act facilitates comparison shopping by requiring that consumers be provided with uniformly computed itemizations of credit costs. An unregulated rental purchase contract, however, aggregates all costs of the transaction into a single (*e.g.*, weekly) fee. The fee may or may not include a charge for the right to defer payment. Because finance charges are buried in the rental fee, the consumer is unable to ascertain directly whether the rental purchase contract or a regular credit sale is more economical. Similarly, rental purchase contracts do not state the total purchase price of the property. This hinders comparison of rental purchase contract arrangements with outright purchases. *See notes 7, 18, and accompanying text supra.*

⁵⁵ The potential harshness of the terms of a rental purchase contract offsets the attractiveness of the low weekly payments and lack of initial deposit. For example, the lease-

the Truth In Lending Act. This stacks the odds against the consumer ever fulfilling his hopes of ownership.

B. *Effectuating Congressional Intent*

The Truth In Lending Act signifies "a transition in congressional policy from a philosophy of 'Let the buyer beware' to one of 'Let the seller disclose.'" ⁵⁶ The Federal Reserve Board's position that a lessee's option to terminate a rental purchase contract brings it outside the ambit of the Act is inconsistent with congressional intent. First, the Board's position fails to recognize that the Truth In Lending Act's remedial nature implies that the Act's terms merit liberal construction to eliminate unscrupulous and predatory credit practices.⁵⁷ Second, it violates the long-standing commercial law principle, incorporated in the Truth In Lending Act, that characterizations of commercial transactions should favor substance over form.⁵⁸

property might be used merchandise. See, e.g., *Turner v. Curtis Mathes Centers, Inc.*, No. 33-78-1135(D), slip op. at 2 (D. Minn. Mar. 1979). The maintenance agreement may terminate before the consumer owns the goods. See SAMPLE RENTAL PURCHASE CONTRACT at Appendix *infra* (maintenance obligation expiring three months before potential ownership transfer to lessee). The payment schedule is perhaps as long as 104 weeks, during which time a single missed payment entitles the retailer to repossess the goods. Finally, the contract may authorize the retailer to remove the lease property from the consumer's premises, and require the consumer to release and discharge all claims or causes of action relating to his entry.

The use of rental purchase contracts victimizes low-income consumers. Consumers with limited education and low-income lack the resources to challenge—and thus are more vulnerable to—disingenuous credit practices. See generally FTC CREDIT PRACTICES REPORT (1968 HEARINGS), *supra* note 21, at 41. In comparing wholesale and retail prices of best-selling products in the low-income market and the general market, the Federal Trade Commission concluded that

the low-income market is a very expensive place to buy durable goods. . . . The most probable reason is that the poor . . . are attracted by the more liberal credit policies. . . . Low-income market retailers . . . feature "easy credit," but the customer pays a great deal for this privilege in the form of grossly higher prices.

Id. at 58.

⁵⁶ *Mourning v. Family Publications Serv.*, 411 U.S. 356, 377 (1973).

⁵⁷ See *id.*; *Sellers v. Wollman*, 510 F.2d 119 (5th Cir. 1975) (Truth In Lending Act liberally construed in favor of the consumer); *N.C. Freed Co. v. Board of Governors of the Fed. Res. Sys.*, 473 F.2d 1210 (2d Cir. 1973), *cert. denied*, 414 U.S. 827 (1973) (statute's remedial nature requires that its terms be construed liberally to effectuate underlying congressional purpose); *Sneed v. Beneficial Finance Co.*, 410 F. Supp. 1135 (D. Hawaii 1976) (Truth In Lending Act viewed as remedial, to be construed liberally).

⁵⁸ In 1876, the Supreme Court stated that "[i]n determining the real character of a contract, courts will always look to its purpose, rather than to the name given to it by the parties." *Hervey v. Rhode Island Locom. Works*, 93 U.S. 664, 672 (1876). See notes 66-74 and accompanying text *infra*.

1. *The Scope of "Credit Sale"*

The legislative history of section 1602(g) of the Act suggests that Congress intended to regulate rental purchase arrangements. The initial credit cost disclosure bill before Congress in 1960 defined "credit" as "any loan, residential mortgage, deed of trust, advance, or discount; any conditional sales contract; any contract to sell or sale, . . . any rental-purchase contract; any contract or arrangement for the hire, bailment, or leasing of property . . . and any transaction or series of transactions having a similar purpose or effect."⁵⁹ This definition encompasses the typical rental purchase transaction, either as a "rental purchase contract"⁶⁰ or

⁵⁹ S. 2755, 86th Cong., 2d Sess. § 2(1), 106 CONG. REC. 97 (1960). This definition of "credit" resembled the Federal Reserve Board's Regulation (12 C.F.R. § 222.8(h)(3) (1949)), which was derived from Executive Order No. 8843, 3 C.F.R. 976 (1938-1943 Compilation). The Executive Order defined the "extension of credit" as

any loan or mortgage; any installment purchase contract, any conditional sales contract, or any sale or contract of sale under which part or all of the price is payable subsequent to the making of such sale or contract; *any rental-purchase contract*, or any contract for the bailment or leasing of property under which the bailee or lessee either has the option of becoming the owner thereof or obligates himself to pay as compensation a sum substantially equivalent to or in excess of the value thereof; any contract creating any lien or similar claim or property to be discharged by the payment of money; any purchase, discount, or other-acquisition of, or any extension of credit upon the security of, any obligation or claim arising out of any of the foregoing; and any transaction or series of transactions having a similar purpose or effect.

Id. § 4(e), 3 C.F.R. at 979 (1938-1943 Compilation) (emphasis added).

⁶⁰ See FRB Interpretation § 222.112, 13 Fed. Reg. 7326 (1948). The Board determined that a particular rental purchase arrangement was either an extension of installment credit or a delivery in anticipation of an installment sale:

§ 222.112 *Rental-purchase arrangements*. In order to increase the sale of a certain type of listed article [see 12 C.F.R. § 222.9 (1949)], a company proposes to rent and deliver to interested persons for use in their homes, such articles for one month at a charge of \$5 *under a written rental agreement which contains no obligation or option for the purchase of the article*. However, before the expiration of the 30-day period, either there would be a sale of an article of the type delivered, or the article that was delivered would be returned to, and reconditioned by, the company for sale elsewhere. In the event of a completed sale, the lessee-purchaser could either retain the article previously delivered to him or receive a new article. If the former should occur, the regular retail purchase price would be reduced by \$5; but if the latter should occur, no such reduction in price would be made. The reduced purchase price or the regular purchase price, as the case may be, would be treated as the selling price subject to the down payment, maturity and monthly payment provisions of Part 222.

The *absence* from the written rental agreement of *an obligation or option to buy* would not be deemed to be of controlling significance in circumstances such as these. Viewed in their entirety, the transactions in question look toward the completion of a sale and, at the outset, should comply with [this part] either as an ordinary

as a series of transactions having a similar purpose or effect.⁶¹

The Senate Committee on Banking and Currency abandoned the original section defining "credit"⁶² and substituted separate definitions of "credit"⁶³ and "credit sales."⁶⁴ The Committee emphasized, however, its continued intent to include disguised leases within the meaning of "credit sales."⁶⁵

extension of installment credit or as a delivery in anticipation of an installment sale under § 222.6(g).

Id. (emphasis added). The Board's interpretation makes clear that the absence of an *obligation* to buy does not preclude characterizing a transaction as an extension of installment credit. More surprisingly, the Board asserts that the absence of even an *option* in the consumer to buy does not preclude an arrangement from constituting, for disclosure requirement purposes, an "extension of installment credit" or "a delivery in anticipation of an installment sale." *Id.* This analysis clearly includes rental purchase contracts in the definition of credit sale.

⁶¹ A series of rental purchase contracts can be functionally equivalent to a "conditional sale." Under both arrangements, the consumer has possession and use of the good while he makes regular payments towards its purchase price, and eventually owns the good.

⁶² See text accompanying note 59 *supra*. The Committee did not explain why it discarded the definition, but observed that "[t]he original language was deleted because it was somewhat cumbersome and sweeping and referred to various types of lease situations which might not be true extensions of credit." S. REP. NO. 392, 90th Cong. 1st Sess. 12 (1967). Witnesses who testified at hearings probably convinced the Committee that the definition, construed literally, could produce "bizarre results which the drafters cannot have intended." 1967 SEN. TIL HEARINGS, *supra* note 4, at 401. (statement of Douglas Hewitt, Executive Secretary, Farm and Equipment Institute); see *id.* at 353 (statement of Darrel M. Holt, Mortgage Bankers Association of America); *id.* at 663 (statement of J.L. Robertson, Vice Chairman, Board of Governors of the Federal Reserve System). Under the definition, for example, a one week car rental could involve "credit" for which the customer pays a charge. *Id.* at 401 (statement of Douglas Hewitt). Similar charges were raised and rebutted during the Senate hearings on another bill, which contained an identical definition of credit. See S. 750, 88th Cong., 1st Sess. § 3(2), reprinted in *Truth In Lending—1963-64: Hearings on S. 750 Before the Subcomm. on Production and Stabilization of the Senate Comm. on Banking and Currency*, 88th Cong., 1st Sess. 1298, 1304 (1963-1964).

⁶³ Governor Robertson of the Federal Reserve Board testified that "it would be preferable to define credit as 'the right granted by a creditor to a debtor to defer payment of debt or to incur debt and defer its payment,' followed by an enumeration of some of the important types of credit listed in section 3(2) of the present bill." 1967 SEN. TIL HEARINGS, *supra* note 4, at 663. The Senate adopted Governor Robertson's suggestion in its definition of "credit". See 15 U.S.C. § 16(e) (1976).

⁶⁴ See 15 U.S.C. § 1602(g) (1976).

⁶⁵ The Committee noted in the report accompanying S. 5 that the definition of "credit sale" "also makes it clear that credit means [the] bailment lease situations described further in section 3(c)." S. REP. NO. 392, *supra* note 19, at 12. According to Governor Robertson, this new definition was sufficiently broad to cover any situation the Federal Reserve System perceived to be within the intent of S. 5. 1967 SEN. TIL HEARINGS, *supra* note 4, at 663.

The language pertaining to disguised leases is nearly identical to that used to distinguish between true leases and conditional sales in the form of leases under the Uniform Conditional Sales Act:

In this Act "Conditional sale" means . . . (2) any contract for the bailments or leasing of goods by which the bailee or lessee contracts to pay as compensation a sum substantially equivalent to the value of the goods, and by which it is agreed that the bailee or lessee is bound to become, or has the option of becoming,

2. Characterizing the Transaction

Congress imported concepts from the field of commercial law into the Truth In Lending Act.⁶⁶ In commercial law generally, the characterization of a particular transaction depends on the intent of the parties, as shown by express provisions of their agreement, and by facts underlying the entire transaction.⁶⁷

a. *Express Provisions.* When courts interpret express provisions in an agreement to determine if it is encompassed by the Truth In Lending Act, they should construe the parties' intentions by examining the treatment of similar provisions in other areas of commercial law. One such analogy, whether a transaction is a true lease or an installment sale, is one of the most frequently litigated questions under the Uniform Commercial Code (UCC).⁶⁸ Section 1-201(37) of the UCC states:

ing the owner of such goods upon full compliance with the terms of the contract.

UNIFORM CONDITIONAL SALES ACT § 1 (act withdrawn 1943). According to the drafters' comments that accompanied § 1:

It is well known that some sellers attempt to evade the conditional sale recording acts by calling the contract a "lease" . . . and providing for the payment of "rent." Wherever these "leases" are substantially equivalent to conditional sales, they should be subject to the same restrictions. This equivalency seems to exist when the buyer is bound to pay rent substantially equal to the value of the goods and has the option of becoming or is to become the owner of the goods after all the rent is paid.

UNIFORM CONDITIONAL SALES ACT § 1, Commissioners' Note (act withdrawn 1943). For an interpretation of § 1 of the Uniform Conditional Sales Act, see Coogan, *Leases of Equipment and Some Other Unconventional Security Devices: An Analysis of U.C.C. Section 1-201(37) and Article 9*, 1973 DUKE L.J. 909, 936-38, 941. Professor Coogan interprets § 1 of the Uniform Conditional Sales Act to require an absolute obligation on the part of a lessee to pay an amount substantially equivalent to the purchase price of the lease property for the transaction to qualify as a conditional sale. *Id.* at 941.

⁶⁶ For example, Congress's definition of "credit sale" was adapted from the old Uniform Conditional Sales Act's definition of "conditional sale." See UNIFORM CONDITIONAL SALES ACT § 1 (act withdrawn 1943). The definition of "credit" was taken from the proposed Uniform Consumer Credit Code. See S. REP. No. 392, *supra* note 19, at 12.

⁶⁷ One court observed that in construing the Truth In Lending Act "the Federal Reserve Board and the majority of courts have focused on the substance, rather than the form, of credit transactions. . . ." *Joseph v. Norman's Health Club, Inc.*, 532 F.2d 86, 90 (8th Cir. 1976). They examine "the practices of the trade, the course of dealing of the parties, and the intention of the parties in addition to specific contractual obligations." *Id.* Another court explained that "[e]ach transaction must be factually evaluated in the light of all relevant evidence, to determine whether that particular transaction constituted a violation of the Act." *Haskins v. American Buyers Club, Inc.*, 77 F.R.D. 715, 717 (S.D. Ill. 1978) (dictum). See also *Meyers v. Clearview Dodge Sales, Inc.*, 539 F.2d 511, 515 (5th Cir. 1976) ("[defendant's] argument elevates form over substance in an effort to avoid the realities of the credit transaction").

⁶⁸ See J. WHITE & R. SUMMERS, *HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE* 878 (2d ed. 1980).

[w]hether a lease is intended as security is to be determined by the facts of each case; however, (a) the inclusion of an option to purchase does not of itself make the lease one intended for security, and (b) an agreement that upon compliance with the terms of the lease the lessee shall become or has the option to become the owner of the property for no additional consideration or for a nominal consideration does make the lease one intended for security.⁶⁹

According to case law developed under the UCC, express contractual provisions that limit the lessor's remedies, deny the lessee equity in the property, and allow the lessee to terminate the agreement suggest that a transaction is a lease. In contrast, contract terms that transfer ownership to the lessee, grant the lessee the right to renew the rental, and require rental fee payments totaling substantially more than the property's market value, indicate that an agreement is a credit sale.⁷⁰ Although a termination clause negates the lessee's obligation to pay the property's full

⁶⁹ U.C.C. § 1-201(37).

⁷⁰ According to Professors White and Summers, several contractual terms suggest that a transaction is a true lease:

- (a) Provision specifying purchase option price which is approximately the market value at the time of the exercise of the option.
- (b) Rental charges indicating an intention to compensate lessor for loss of value over the term of the lease due to aging, wear and obsolescence.
- (c) Rentals which are not excessive and option purchase price which is not too low.
- (d) Facts showing that the lessee is acquiring no equity in leased article during the term of lease.

J. WHITE & R. SUMMERS, *supra* note 68, at 879 (citing *In re Alpha Creamery Co.*, 4 U.C.C. Rep. 794, 798 (W.D. Mich. 1967)). Contractual terms supporting characterization as a "security interest" include (1) provisions stating that upon making periodic payments for the required time, the lessee automatically becomes the owner "without paying anything additional"; (2) a purchase option affording the lessee no economic choice but to exercise the option at the end of the lease term; (3) terms making the lessee the financier; (4) stipulations requiring the lessee to pay for taxes, repairs, maintenance, and for insurance on the goods with the lessor as beneficiary; (5) a clause giving the lessor the option to accelerate payments upon the lessee's default. *See id.* at 880-83.

Besides the lease agreement itself, other factors must be considered, such as the expectations of the parties, whether the "lessor" is in the business of renting or selling goods, and whether the lessee has an option to renew the lease. *See* Claxton, *Lease or Security Interest: A Classic Problem of Commercial Law*, 28 MERCER L. REV. 599 (1977); Coogan, *supra* note 65, at 956-64.

An analogous problem is ascertaining if a transaction constitutes a "sale" under Article Two of the Uniform Commercial Code, or if the transaction is not encompassed by the Code. *See* U.C.C. § 2-106(1). Generally, courts have left this question for the fact-finder, who must determine the intentions of the parties. *See, e.g.,* Morgan v. Freel, 475 P.2d 641 (Colo. App. 1970); Lebowitz v. McPike, 151 Conn. 566, 201 A.2d 469 (1964); Meinhard-Commercial Corp. v. Hargo Woolen Mills, 112 N.H. 500, 300 A.2d 321 (1973).

value, it does not preclude judicial determination that the transaction is an installment sale.⁷¹

Using the analysis of such provisions under the UCC as an analogue for characterizing rental purchase contracts, some provisions of a rental purchase contract suggest that it is a lease, while others indicate that it is a credit sale. An option to terminate however, does not by itself preclude characterization as a credit sale.

b. *Underlying Facts*. Courts should also consider facts underlying the transaction. Most consumers enter into rental purchase contracts primarily because they desire to own the leased property.⁷² Indeed, retailers promote this desire in their advertisements.⁷³ Another indication of intent that approximates a credit sale is that a rental purchase contract's rental fee may exceed the

⁷¹ Courts have found terminable or open-end leases to be security interests under the U.C.C. For example, in *United Rental Equip. Co. v. Potts & Callahan Contracting Co.*, 231 Md. 552, 191 A.2d 570 (1963), the disputed lease required rental for a minimum period of one month. At the end of the month, the lessee could renew by paying the same rental fee per month until he chose to return the equipment to the lessor. The parties had agreed that if the lessee elected to purchase, 85% of the rental fees would apply towards the purchase price. The lessee argued that because the lease obligated the lessor for only a one month term, the lessee did not have the right or option to purchase the property. Rejecting this argument, the court held that "the parties contemplated the purchase of the [property] by [the lessee] if he continued to pay the specified monthly rental and otherwise complied with the lease." *Id.* at 559, 191 A.2d at 574. Considering a similar agreement, the court in *In re Royer's Bakery, Inc.*, 1 U.C.C. Rep. 342 (E.D. Pa. 1963), determined that the lease was a security interest even though the lessee had the right to terminate without further obligation by giving 30 days notice.

Some commentators, however, regard a lessee's right to terminate a lease agreement as so significant that it should completely overshadow the existence of an option to purchase for nominal or no additional consideration. *See, e.g., Coogan, supra* note 65, at 936-41. Others view this interpretation as "somewhat extreme." Claxton, *supra* note 70, at 604 n.32.

⁷² *See* note 73 and accompanying text *infra*.

⁷³ In *Smith v. ABC Rental Sys. Inc.*, 491 F. Supp. 127 (E.D. La. 1978), Smith, the lessee, claimed that he had entered into the lease agreement because of the rental purchase plan, featured in the company's advertisements. He contended that the advertisements led him to believe that he was purchasing, not renting, the lease-property, and that he was obligated to make payments for 18 months. During the trial, Smith submitted copies of ABC's television and radio advertisements, which stressed that consumers "need to know before [they] buy," that they could "rent to own," and that all of the payments would be credited towards purchasing the property. *Id.* at 128. The contract itself, however, which Smith did not read, made no mention of the purchase plan. *Id.* The president of ABC Rental testified that the company merely gave the rented item to a consumer who paid the rental fees for 18 months. *Id.* The court, holding that the lease was not a credit sale, observed that ABC's advertisement "was misleading in that it prominently featured the rental purchase plan. . . ." *Id.* at 129.

fair rental value chargeable under a conventional lease.⁷⁴ Taken together, these facts warrant a presumption that the parties intended the rental to result in a sale. This presumption renders the rental purchase contract presumptively a credit sale covered by the Truth In Lending Act.

IV

ELIMINATING THE EXCLUSION: APPLYING THE TRUTH IN LENDING ACT TO RENTAL PURCHASE CONTRACTS

A. Regulation by the Federal Reserve Board

Congress granted the Federal Reserve Board authority to prescribe regulations⁷⁵ containing "such classifications, differentiations, or other provisions . . . necessary or proper . . . to prevent circumvention or evasion [of the Act]."⁷⁶ The Supreme Court has observed that such broad authority indicates "the clear desire of Congress to insure that the Board [has] adequate power to deal with such attempted evasion . . . no matter what adroit or unscrupulous practices [are] employed by those extending credit to consumers."⁷⁷

Previous regulation by the Board establishes a precedent for presumptively including an entire class of transactions within the scope of the Act, even though certain transactions within the class may not involve the actual extension of credit.⁷⁸ The Board, for example, has exercised its full regulatory power in promulgating the Four Installment Rule, which requires credit cost disclosure whenever a consumer is offered credit "which is payable by agreement in more than four installments, or for which the payment of a finance charge is or may be required."⁷⁹ The Supreme Court has ruled the Four Installment Rule constitutional, holding:

In *Johnson v. McNamara*, No. H-78-498 (D. Conn. Apr. 12, 1979), the lessee alleged that she telephoned the lessor to inquire specifically about the rental-purchase of a stereo. She claimed the rental purchase contract appealed to her because she could purchase the set without a substantial down payment. She asserted that she intended at all times to purchase the stereo, and stopped making the required weekly payments only when the product was stolen from her residence. See Plaintiff's Memorandum in Opposition to Motion to Dismiss and in Support of Motion for Summary Judgment as to Liability, *Johnson v. McNamara*, No. H-78-498 (D. Conn. Apr. 12, 1979).

⁷⁴ For example, in *Johnson v. McNamara*, No. H-78-498 (D. Conn. Apr. 12, 1979), the lessee paid a fee of \$14.97 *per week* under a rental purchase agreement. Two years later, a different retailer offered a conventional lease at a cost of \$14.95 *per month*. See *Hartford Courant*, Feb. 25, 1979, at 3, 21.

⁷⁵ See 15 U.S.C. § 1604 (1976); note 35 *supra*.

⁷⁶ 15 U.S.C. § 1604 (1976).

⁷⁷ *Mourning v. Family Publications Serv.*, 411 U.S. 356, 365-66 (1973).

⁷⁸ See, e.g., *id.* at 374.

⁷⁹ 12 C.F.R. § 226.2(s) (1980).

[w]here . . . the transactions or conduct which Congress seeks to administer occur in myriad and changing forms, a requirement that a line be drawn which insures that not one blameless individual will be subject to the provisions of an act would unreasonably encumber effective administration and permit many clear violators to escape regulation entirely.⁸⁰

Rental purchase contracts are among the "myriad forms" of transactions that "escape" credit disclosure regulation under the Truth In Lending Act.

The Federal Reserve Board should promulgate a regulation that would establish an irrebuttable presumption that rental purchase contracts are "credit sales" within the meaning of the Act. Although the regulation would inevitably include some rental purchase contracts that might otherwise be exempted as "true leases,"⁸¹ the need for administrative convenience and the prevention of blatant violations outweigh concerns about potential overinclusiveness.

The Federal Reserve Board has maintained, however, that a rental purchase contract terminable by the lessee is not a credit sale,⁸² and has recommended that Congress amend the credit sale definition to conform to the Board's administrative position.⁸³ Consequently, it is unlikely that the Board will reverse its position without a mandate from Congress.

B. Regulation by Judicial Interpretation

Courts interpreting the Truth In Lending Act generally give great weight to the Federal Reserve Board's interpretations. Along with Regulation Z,⁸⁴ promulgated under the Act, such interpretations "constitute part of the body of 'informed experience and judgment of the agency to whom Congress delegated appropriate authority.'" ⁸⁵ Nevertheless, the paramount judicial duty is to interpret statutes to effectuate legislative intent. Unofficial staff opinion letters, accordingly, are not binding on the courts, and they may consider independently whether a particular interpreta-

⁸⁰ *Mourning v. Family Publications Serv.*, 411 U.S. 356, 374 (1973).

⁸¹ Courts have also had difficulty establishing a clear distinction between "credit sales" and "true leases." See notes 68-74 and accompanying text *supra*.

⁸² See note 37 and accompanying text *supra*.

⁸³ See note 39 and accompanying text *supra*.

⁸⁴ See, e.g., 12 C.F.R. §§ 226.101-1503 (1980).

⁸⁵ *Philbeck v. Timmers Chevrolet, Inc.*, 499 F.2d 971, 976 (5th Cir. 1974) (citing *Mourning v. Family Publications Serv.*, 411 U.S. 356, 372 (1973)).

tion is consistent with the purposes of the Act.⁸⁶ The legislative history of section 1602(g) indicates that Congress intended the Truth In Lending Act to govern leases that are actually disguised credit sales. Courts, therefore, should examine arrangements on a case by case basis to determine whether they constitute leases or credit sales.

Reliance upon judicial initiative, however, is unsatisfactory. The low sums of money commonly in dispute often do not justify the expenses of litigation. The consumers most likely to use and encounter problems with rental purchase contracts—those with low income and limited education—are least likely to initiate legal action.⁸⁷ When litigation does arise, the parties often will settle the case before the court reaches a decision on the merits.⁸⁸ Case by case resolution, moreover, may expose retailers to considerable unexpected liability for failing to comply with the Act.⁸⁹

C. Congressional Action: Amending the "Credit Sale" Definition

The Truth In Lending Act does not currently insure that rental purchase contracts will contain adequate credit cost disclo-

⁸⁶ In *Johnson v. McNamara*, No. H-78-498, slip op. at 7 (D. Conn. Apr. 12, 1979), the court noted that "[i]n terms of persuasiveness, unofficial staff interpretations stand at the bottom of the hierarchy of administrative rulings interpreting the federal Truth In Lending Act, behind both official staff interpretations and interpretations of the Federal Reserve Board itself. Unofficial staff interpretations . . . are therefore not binding on this court." See *Grubb v. Oliver Enterprises*, 358 F. Supp. 970, 973 n.6 (N.D. Ga. 1972).

⁸⁷ See Rothstein, *The Myth of Sisyphus: Legal Services Efforts on Behalf of the Poor*, 7 U. MICH. J.L. REF. 493, 498-99 (1974). See generally Ventantonio, "Equal Justice Under the Law": *The Evolution of a National Commitment to Legal Services for the Poor and a Study of Its Impact on New Jersey Landlord-Tenant Law*, 7 SETON HALL L. REV. 233, 252-60 (1976).

⁸⁸ In *Waldron v. Best T.V. & Stereo Rentals, Inc.*, 485 F. Supp. 718 (D. Md. 1979), for example, the parties settled their dispute after the court denied the lessor's motion to dismiss the case. Pursuant to the settlement agreement, the lessee filed a motion to dismiss the case with prejudice. The lessee's motion specified that the lessor "maintain[ed] that it violated no federal or state laws, statutes, rules or regulations and, to the contrary, contend[ed] that it ha[d] complied with all such requirements." *Id.* at 720. Under the settlement agreement, the lessor agreed to pay the lessee \$750 "in order to avoid the inconvenience and expense of further litigation." *Id.*

⁸⁹ Section 1640(f) of the Truth In Lending Act affords relief from liability to creditors for

any act done or omitted in good faith in conformity with any rule, regulation, or interpretation thereof by the Board or in conformity with any interpretation or approval by an official or employee of the Federal Reserve System duly authorized by the Board to issue such interpretations or approvals under such procedures as the Board may prescribe therefor, notwithstanding that after such act or omission has occurred, such rule, regulation, interpretation, or approval is amended, rescinded, or determined by judicial . . . authority to be invalid for any reason.

15 U.S.C.A. § 1640(f) (1979).

sure. Because a regulation insuring such disclosure is unlikely under the current statute in light of the Federal Reserve Board's position and judicial responses, Congress should amend the Act's definition of "credit sale" to unambiguously cover rental purchase contracts.⁹⁰ The Senate approved legislation in 1979 that would revise the definitions of "credit sale" and "creditor."⁹¹ Despite the Federal Reserve Board's recommendation, the revised definition of "credit sale" does not address the issue of whether rental purchase contracts are credit sales.⁹²

Congress should incorporate an unambiguous definition of "credit sale" that would specify a convenient method for determining if credit disclosures are required.⁹³ It should specifically include rental purchase contracts but be general enough to en-

⁹⁰ Rental purchase contracts should be regulated as "credit sales" under the Truth In Lending Act, rather than as "leases" under the Truth In Leasing Act, for several reasons. First, the Truth In Leasing Act's requirement of a four-month lease term would exempt most rental purchase contracts. See notes 35 & 38 *supra*. Second, regulation as a "lease" might induce retailers to transform ordinary credit sales into rental purchase contracts to avoid the strict disclosure requirements and penalties of the Truth In Lending Act. See text accompanying note 22 *supra*. Most important, rental purchase contracts bear a closer resemblance to sales than to leases. See notes 65, 72-74, and accompanying text *supra*.

⁹¹ See S. 108, 96th Cong., 1st Sess. § 2 (1979), reprinted in 1979 TIL SIMPLIFICATION HEARINGS, *supra* note 2, at 134-35. Section 2(b) of S. 108 would amend the definition of "credit sale" so that "[t]he term . . . refers to any sale in which the seller is a creditor." 1979 TIL SIMPLIFICATION HEARINGS, *supra* note 2, at 135. Section 2(a) of S. 108 would alter the definition of "creditor" [15 U.S.C. § 1602(f)] by striking the first sentence of the definition and inserting additional language:

The term "creditor" refers only to a person who *both* (1) *regularly extends*, whether in connection with loans, sales of property or services, or otherwise, consumer credit which is payable by agreement in more than four installments or for which the payment of a finance charge is or may be required; and (2) is the *person to whom the debt* arising from the consumer credit transaction *is initially payable*. . . . Notwithstanding the foregoing, a person who *regularly arranges for the extension of consumer credit*, which is *payable* in more than four installments or for which the payment of a finance charge is or may be required, *from persons who are not creditors* is a creditor.

Id. at 134 (emphasis added).

The Senate intended this amendment to eliminate confusion under the current Act regarding the responsibilities of assignees and "arrangers of credit." See S. REP. NO. 73, 96th Cong., 1st Sess. 10 (1979). The National Consumer Law Center argues that this amendment "significantly reduces the scope of the Truth In Lending Act . . . by narrowing the key term 'creditor,'" and will "do away with the existing system of cooperative checks and balances among multiple financiers and arrangers substantially decreasing the accuracy of disclosures and the likelihood of the cooperation among creditors necessary for compliance by the business providing the disclosure statement." See 1979 TIL SIMPLIFICATION HEARINGS, *supra* note 2, at 35.

⁹² See note 39 and accompanying text *supra*.

⁹³ The finance charge on a rental purchase contract could, for example, be determined by comparing the cash retail price with the lease price, to establish a ratio for proration.

compass other transactions similar in purpose and effect. For example, Congress might amend section 1602(g) to include lease transactions and other similar arrangements in which the completion of a series of lease contracts results in the automatic transfer of ownership to the lessee upon payment of rental fees substantially equivalent to the value of the lease property.⁹⁴

CONCLUSION

Congress enacted the Truth In Lending Act to eliminate deceptive practices in the credit industry, promote consumer awareness of credit costs, and facilitate comparison shopping for credit. Retail merchants have circumvented the legislative controls by structuring as leases transactions that are in substance "credit sales." Nonregulation of rental purchase contracts is unfair to consumers and inconsistent with Congress's intent in enacting Truth In Lending disclosure provisions. The Federal Reserve Board has declined to regulate rental purchase contracts, and the courts, generally deferring to the Board's position, are reluctant to solve the problem. Congress should amend the Truth In Lending Act's "credit sale" definition to explicitly encompass rental purchase contracts and subject them to credit disclosure provisions. Such legislation is necessary to further the goals and purposes of credit disclosure regulation.

Karen F. Meenan

⁹⁴ For example, Congress might adopt the following amendment to § 1603(g):
Sec. 2 Definitions

2(b) Subsection (g) of section 103 of the Truth In Lending Act is amended to read as follows:

(g)(1) The term "credit sale" means any sale in which the seller is a creditor.

(2) The following transactions are sales for the purchase of this subsection:

(i) any lease or series of leases which provide that the lessee may, at his option, become owner of the lease-property for no more than a nominal fee, upon payment of rental fees substantially equivalent to or greater than the value of the lease property; and

(ii) any transaction or series of transactions with similar purpose or effect.

(3) With respect to transactions described in subsection (2)(i) and (ii), the disclosures required by section 128 shall be calculated on the assumption that the lessee will become owner of the lease property not before the last date specified in the contract or series of contracts.

APPENDIX
SAMPLE RENTAL PURCHASE CONTRACT

THIS IS A RENTAL AGREEMENT ONLY

THE UNDERSIGNED, HEREIN CALLED "RENTER," WHETHER ONE OR MORE, DOES JOINTLY AND SEVERALLY HEREBY RENT FROM THE RENTAL COMPANY, HEREIN CALLED "OWNER," THE ABOVE DESCRIBED PERSONAL PROPERTY, HEREIN CALLED "PROPERTY," AT THE RENTAL RATES SET FORTH ABOVE, PAYABLE WEEKLY IN ADVANCE FOR WEEK-TO-WEEK TERMS BEGINNING ON THE COMMENCEMENT DATE STATED ABOVE, EXCEPT AS STATED BELOW.

**THIS IS A WEEK-TO-WEEK, DAY-TO-DAY, OR MONTH-TO-MONTH
RENTAL AGREEMENT ONLY**

TITLE AND TERM: TITLE REMAINS AT ALL TIMES IN THE OWNER. THE RENTER RECEIVES USE AND POSSESSION OF THE PROPERTY FOR SUCCESSIVE ONE-WEEK TERMS SO LONG AS WEEKLY RENTAL PAYMENTS ARE MADE ON OR BEFORE THE DATE DUE AND RENTER COMPLIES FULLY WITH ALL AGREEMENTS AND CONDITION HEREOF AND UNLESS THIS AGREEMENT IS TERMINATED AS PROVIDED HEREIN. IN THE EVENT RENTER FAILS TO RENEW FOR A WEEK-TO-WEEK TERM BY PAYMENT OF THE WEEKLY RENTAL RATE IN ADVANCE ON OR BEFORE THE DATE DUE AND RETAINS POSSESSION OF THE PROPERTY, RENTER AGREES TO RENT SAID PROPERTY ON A DAY-TO-DATE TERM AT THE OPTIONAL DAILY RENTAL RATES SET OUT ABOVE, PAYABLE IN ADVANCE. RENTER MAY ELECT TO THEREAFTER RENEW ON A WEEK-TO-WEEK BASIS ON ANY WEEKLY ANNIVERSARY OF THE FIRST DUE DATE ABOVE BY MAKING ALL REQUIRED PAYMENTS TO SAID ANNIVERSARY DATE AND THE PAYMENT FOR A ONE WEEK TERM THEREAFTER.

TERMINATION BY RENTER: RENTER, AT ITS OPTION, MAY AT ANY TIME TERMINATE THIS AGREEMENT BY RETURN OF THE PROPERTY TO OWNER IN ITS PRESENT CONDITION, FAIR WEAR AND TEAR EXCEPTED AND BY PAYMENT OF ALL RENTAL PAYMENTS DUE THROUGH THE DATE OF RETURN.

TERMINATION BY OWNER: THIS AGREEMENT SHALL AT THE OPTION OF THE OWNER AND WITHOUT NOTICE TERMINATE UPON THE FAILURE OF RENTER TO MAKE EVERY RENTAL PAYMENT REQUIRED HEREIN ON OR BEFORE THE DATE DUE, OR BY BREACH BY THE RENTER OF ANY AGREEMENT, CONDITION OR REPRESENTATION, ALL OF WHICH ARE AGREED TO BE MATERIAL. RENTER SHALL IMMEDIATELY RETURN THE PROPERTY TO OWNER IN ITS PRESENT CONDITION, FAIR WEAR AND TEAR EXCEPTED, AND RENTER SHALL REMAIN LIABLE FOR ALL PAYMENT HEREUNDER TO THE DATE OF TERMINATION AND FOR THE PERFORMANCE OF ALL AGREEMENTS AND CONDITION HEREOF.

LOCATION OF PROPERTY: RENTER WARRANTS AND AGREES THAT IT WILL KEEP SAID PROPERTY IN ITS POSSESSION AT THE RESIDENCE ADDRESS ABOVE AND WILL NOT REMOVE SAID PERSONAL PROPERTY FROM SAID ADDRESS WITHOUT AGREEMENT IN WRITING EXECUTED BY THE OWNER. IF RENTER MOVES SAID PROPERTY WITHOUT SECURING PRIOR AGREEMENT IN WRITING FROM OWNER, THIS AGREEMENT SHALL BE THEREBY BREACHED GIVING THE OWNER THE RIGHT OF IMMEDIATE POSSESSION AND RENTER SHALL BE LIABLE FOR PROSECUTION UNDER APPLICABLE STATE LAW.

INSURANCE: OWNER CARRIES NO INSURANCE ON THE ABOVE RENTAL PROPERTY.

DAMAGES: RENTER IS FULLY RESPONSIBLE FOR THE LOSS, THEFT OR DESTRUCTION OF SAID PROPERTY FROM ALL CAUSES WHATSOEVER AND AGREES TO PAY TO THE OWNER THE FAIR MARKET VALUE OF THE PROPERTY IN SUCH EVENT. IN THE EVENT OF DAMAGE AND/OR PARTIAL DESTRUCTION FROM ANY CAUSE WHATSOEVER, RENTER AGREES TO PAY TO THE OWNER A REASONABLE COST OF REPAIR TO SAID PROPERTY.

ASSIGNMENT: THIS AGREEMENT MAY BE SOLD, TRANSFERRED AND ASSIGNED BY OWNER WITHOUT RESTRICTION. RENTER HAS NO RIGHT TO ASSIGN, SUB-LEASE OR TRANSFER HIS RIGHTS HEREIN WITHOUT THE WRITTEN CONSENT OF OWNER.

MAINTENANCE AND TAXES: THE OWNER DOES HEREBY AGREE TO MAINTAIN THE PERSONAL PROPERTY IN GOOD WORKING ORDER AND ANY AND ALL MAINTENANCE OR REPAIRS TO THE PROPERTY OF THE OWNER RENTER HEREUNDER MUST BE PERFORMED BY THE OWNER AND THE OWNER WILL NOT BE RESPONSIBLE FOR COSTS OF ANY REPAIRS DONE AT THE REQUEST OF THE RENTER BY OTHERS. THE OWNER SHALL PAY ANY PERSONAL PROPERTY TAXES ON SAID PROPERTY. MAINTENANCE IS NOT PROVIDED BEYOND THE DATE SPECIFIED ABOVE AS "MAINTENANCE LIMIT."

OWNER'S RIGHT TO ENTER AND TAKE POSSESSION: THE OWNER AND ITS AGENTS, UPON THE TERMINATION OF THIS AGREEMENT, ARE SPECIFICALLY AUTHORIZED TO ENTER UPON ANY PREMISES WHERE THE PROPERTY MAY BE FOUND AND TO TAKE POSSESSION OF AND REMOVE THE PROPERTY WITHOUT LIABILITY, AND OWNER AND ITS AGENTS ARE HEREBY RELEASED AND DISCHARGED FROM ANY CLAIM OR CAUSE OF ACTION IN OR RELATING TO ENTRY AND TAKING POSSESSION AND RENTER AGREES TO INDEMNIFY OWNER AND ITS AGENTS FOR ALL COSTS, EXPENSES, AND DAMAGES OCCURRING DIRECTLY OR INDIRECTLY FROM OR RELATED TO THE TAKING POSSESSION AND THE REMOVAL OF SAID PROPERTY.

RENTER HAS NO RIGHT TO SELL, MORTGAGE, PAWN, PLEDGE, ENCUMBER, OR DISPOSE OF SAID PROPERTY OR TO MOVE SAID PROPERTY FROM THE RESIDENCE ADDRESS LISTED ABOVE. TO DO SO IS A BREACH OF THIS AGREEMENT AND RENTER SHALL BE LIABLE UNDER APPLICABLE STATE LAW.

IN THE EVENT RENTER AT HIS SOLE ELECTION RENEWS THIS RENTAL AGREEMENT FOR _____ SUCCESSIVE ONE-WEEK TERMS, OWNER WILL TRANSFER THE PROPERTY TO RENTER.

TIME IS OF THE ESSENCE OF THIS AGREEMENT

NO ORAL STATEMENTS OR AGREEMENTS SHALL BE VALID OR BINDING ON THE PARTIES HERETO. THIS RENTAL AGREEMENT MAY BE MODIFIED, VARIED, ALTERED OR EXTENDED, OR THE AGREEMENTS OR CONDITIONS HEREOF WAIVED ONLY BY AGREEMENT IN WRITING EXECUTED BY THE OWNER. RENTER ACKNOWLEDGES RECEIPT OF SAID PROPERTY IN SATISFACTORY OPERATING CONDITION. THE PROPERTY IS NOT REPRESENTED TO BE NEW PROPERTY.

I HAVE READ AND UNDERSTAND THE ABOVE RENTAL AGREEMENT