Consumer Law Guide

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PREFACE

This publication is one of a series prepared and distributed by the Legal Assistance Branch of the Administrative and Civil Law Department of The Judge Advocate General's School, U.S. Army (TJAGSA) to assist legal assistance attorneys in the delivery of legal assistance. The law changes much more rapidly than this publication can be updated and distributed. For this reason, use this publication only as a guide and not as final authority on any specific law or regulation. Where appropriate, legal assistance attorneys should consult more regularly updated references before rendering legal advice.

This publication has been prepared by numerous past professors of Consumer Law at TJAGSA and updated by the present professor of Consumer Law. As you use this publication, if you have any recommendations for improvement, or corrections, please send your comments and suggestions to The Judge Advocate General's Legal Center and School, ATTN: ALCS-ADA-LA, Charlottesville, Virginia 22903-1781 or oren.mcknelly@conus.army.mil.

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The following Legal Assistance Branch publications are currently available in "zipped" format:

Number	Title
JA 260	Soldiers' & Sailors' Civil Relief Act
JA 262	Legal Assistance Wills Guide
JA 263	Legal Assistance Family Law Guide
JA 265	Legal Assistance Consumer Law Guide
JA 269	Legal Assistance Federal Income Tax Information Series
JA 270	Uniformed Services Employment and Reemployment Rights Act
JA 274	Uniformed Services Former Spouses' Protection Act - Outline and References
JA 275	Tax Assistance Program Management Guide

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D: 32 CFR Part 232 – Limitations on Terms of Consumer Credit Extended to Service Members and Dependents; Final Rule

CHAPTER 1

CONSUMER LAW OVERVIEW

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CHAPTER 1

CONSUMER LAW OVERVIEW

I. WHAT IS CONSUMER LAW?[1]

A. Resources.

1. NATIONAL CONSUMER LAW CENTER, UNFAIR AND DECEPTIVE ACTS AND PRACTICES (6th ed. 2004 & Supp. 2006).

2. Howard J. Alperin & Roland F. Chase, Consumer Law: Sales Practices and Credit Regulation (1986 & Supp. 2008-2009).

3. AMERICAN BAR ASSOCIATION, CONSUMER PROTECTION HANDBOOK (2004).

B. Scope.

1. Consumer law is broadly defined as "the law regulating consumer transactions."

2. A consumer transaction occurs when a person obtains goods, real property, credit, or services for personal, family, or household purposes.

3. Sources of substantive consumer law:

a) The body of consumer law includes established doctrines from common law (especially contracts), federal and state statutes, administrative rules, and judicial decisions that protect consumers.

b) Consumer law generally supplements established doctrines from the common law.

[1] This discussion is adapted from the Preface and Introductory comments in HOWARD J. ALPERIN & ROLAND F. CHASE, CONSUMER LAW (1986 & Supp. 1998). All quotes are taken from that book.

(1) Prior to the Consumer Statutes being enacted in the 1960's and 1970's, most consumer transactions were governed by the principal of *caveat emptor* (buyer beware).

(2) Common law fraud was extremely hard to prove and rarely resulted in significant damages, making attorneys reluctant to represent consumers in pursuing personal claims.

4. Consumer law generally does NOT include civil rights legislation, poverty law, minimum wage legislation, or antitrust.

C. Objectives and Means.

1. Primary Objective. The primary objective of consumer law is to balance the interests of consumers and merchants in the marketplace.

a) The underlying assumption is that, without protection, consumers are at a disadvantage.

b) Consumer protection laws create a counterbalance to the inherent advantages of the merchant.

2. Primary Means. Consumer protection laws generally strive to achieve their objectives by giving special protection to the consumer in the form of:

a) Information contained in required disclosures; and/or

b) Limitations on merchant behavior (e.g. prohibition on disclaimer of warranties).

D. The players.

1. State and federal legislatures.

2. State and federal administrative agencies.

a) Attorney General's Office.

(1) Investigation.

(2) Injunctive Relief.

(3) Restitution.

(4) Civil Penalties.

b) Federal Reserve Board.

(1) Promulgates banking rules in the Code of Federal Regulations (CFR).

(2) Consult Code of Federal Regulations (CFR).

c) Federal Trade Commission.

(1) Rules.

(a) Interprets and enforces Federal Reserve Board Rules.

(b) Develops its own rules & "standards" for interpretation and enforcement of federal consumer protections statutes.

(2) Enforcement of FTC Act (and others).

(a) Investigation.

(b) Adjudication.

(3) The FTC provides consumers practical information about the law and how to identify and avoid fraud and deception in the marketplace. Consumers can file a complaint with the FTC by calling 1-877-FTC-HELP or by using the online complaint form at www.ftc.gov.

3. Courts at all levels.

II. ANALYZING CONSUMER PROTECTION PROBLEMS

In considering a consumer law problem, the attorney must consider all aspects of the transaction and use all available protections/solutions to develop the most effective course of action for the client. To aid in this thought process, we offer the following as areas to think through in each case.

A. The Transaction. The first thing to consider is the way the transaction occurred. Depending on where it took place, or the sales techniques used, federal and state laws may offer the consumer some protection. Except as noted, these areas are covered in the chapters of this guide.

1. State Unfair and Deceptive Acts and Practices (UDAP) laws (Chap. 2 and Appendix B).

2. FTC Door-to-Door Sales Rule (Chap. 3).

3. FTC Telemarketing Rule (Chap. 3).

4. Mail Order and Telephone Merchandise Rule (Chap. 3).

5. Consumer Leasing Act (Chap. 3).

6. Truth-in Lending Act Cooling Off Period (Chap. 5).

7. Traditional contract and tort law defenses and remedies. This guide does not cover basic contract law.

B. The Goods. The second place to look for possible help is the goods themselves. There may be some deficiency in the quality of the goods that will allow your client to take advantage of some protections.

1. Magnuson-Moss Warranty Act (15 U.S.C. §§ 2301-12) (Chap. 4)

2. Uniform Commercial Code Warranty Provisions (§§ 2-312 - 2-318) (Chap. 5).

3. State Warranty Laws/"Lemon" Laws (Appendix B).

C. The Payment. The next area to look for protection is the manner of payment for the goods. Specific federal protections applicable to credit transactions are discussed in Chapter 5.

1. Truth-in-lending Act 1968

2. Fair Credit Billing Act 1974

3. Electronic Funds Transfer Act 1970 and 1974

D. The Aftermath. Finally, the collection of debts by merchants and the reporting of consumer information to credit reporting agencies is governed by two federal statutes discussed in Chapter 8.

1. Fair Debt Collection Practices Act 1974

2. Fair Credit Reporting Act 1970

E. Other Specific Protections. Federal and state consumer protection laws govern a wide range of other transactions not included in the federal statutes listed above. While this Guide will not attempt to cover every scenario in which the consumer may benefit from consumer protection law, it will address some specific areas of particular interest to military legal assistance attorneys, including landlord-tenant law, credit discrimination, credit repair, identity theft, and military specific remedies.

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CHAPTER 2

UNFAIR AND DECEPTIVE ACTS AND PRACTICES (UDAP)

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CHAPTER 2

UNFAIR AND DECEPTIVE ACTS AND PRACTICES (UDAP)

I. RESOURCES.

A. NATIONAL CONSUMER LAW CENTER, UNFAIR AND DECEPTIVE ACTS AND PRACTICES (6th ed. 2004 & Supp. 2006). The majority of this outline is from the National Consumer Law Center (NCLC) resources.

B. Federal Trade Commission Act, 15 U.S.C. § 45.

C. State UDAP Statutes (listed by state at Appendix B).

II. INTRODUCTION.

A. The UDAP Statutes are very state specific so this outline is prepared only to give you a general idea of the substance and application of common provisions of UDAP statutes.

B. Practitioners must research individual state law on any specific question in the area of UDAP.

III. UNFAIR AND DECEPTIVE ACTS AND PRACTICES (UDAP) - WHAT ARE THEY?

A. General label for a variety of statutes with broad applicability to consumer transactions aimed at preventing deception and abuse in the marketplace.

B. Coverage. UDAP statutes cover a wide range of consumer topics. They range from regulation of sales practices to regulation of advertising, warranties and credit offers. UDAP can include a wide range of merchant activity. The term is a somewhat imprecise because it includes a wide range of consumer protection statutes.

C. History. The impetus behind many of the current UDAP statutes is the Federal Trade Commission Act (described below). Other authors attribute the rise in consumer protection acts to the work of Ralph Nader and other consumer advocates.

D. Federal Trade Commission Act. 15 U.S.C. § 45.

1. "[U]nfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful."

2. The Federal Trade Commission power under 15 U.S.C. § 45 is, however, in addition to the authority of the states. The FTC does not displace state law unless the state law is inadequate or contrary to the Commission's regulations. *See American Financial Services v. FTC*, 767 F. 2d 957 (D.C. 1985).

3. Enforcement - only by the FTC. This can be a severe limitation on the utility of the FTC Act. Therefore, state statutes become very important to the consumer law practitioner, since these statutes will, at a minimum, give state agency enforcement. In addition, many allow for private causes of action as a remedy.

E. State UDAP statutes. The provisions of these statutes vary by state. Thus, legal assistance practitioners must familiarize themselves with the protections their state offers when they arrive at a new installation. Some general features of these statutes include the following:

1. Every state, the District of Columbia, Puerto Rico, Guam, and the Virgin Islands have passed at least one statute that deals broadly with most consumer transactions.[1] See Appendix B. Almost any abusive business practice aimed at consumers is at least arguably a UDAP violation, unless the trade practice falls clearly outside the scope of the statute. Many state attorneys general compile and publish case summaries, attorney general opinions, regulations, and enforcement proceedings. If available, you should keep a file of your local attorney general summaries. Further, numerous states have manuals or texts on applicable consumer protection laws. If possible, legal assistance offices should obtain a copy of the appropriate state's manual.

2. States call these statutes a variety of names including consumer protection acts, consumer sales acts, unfair trade practice acts, deceptive and unfair trade practices acts, deceptive consumer sales acts, deceptive trade practices acts, and consumer fraud acts. The National Consumer Law Center labels all state consumer statutes of general applicability as Unfair and Deceptive Acts and Practices (UDAP) statutes.[2]

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[1] NATIONAL CONSUMER LAW CENTER, UNFAIR AND DECEPTIVE ACTS AND PRACTICES § 1.1 (6th ed. 2004) [hereinafter NCLC UDAP]. .For a state-by-state guide to these statutes, *see id.* at Appendix A.

[2] *Id.*

3. The state statutes supplement the FTC Act; they do not displace it in any fashion.

4. "Legislatures and courts have been careful to guarantee that UDAP statutes are broad and flexible, so that they can apply to creative, new forms of abusive business schemes in almost all types of consumer transactions. Even when UDAP statutes enumerate specifically prohibited practices, most statutes also prohibit other unfair, unconscionable, and/or deceptive practices in more general terms."[3]

5. States will usually authorize enforcement by state authorities (usually the Attorney General), as well as private enforcement, thus allowing for widespread redress of marketplace misconduct and abuse of consumers.

6. Many of the statutes include awards of private damages, attorney's fees as well as punitive, treble, or minimum damage awards. This is often a critical aspect of a consumer statute for the legal assistance practitioner. Absent an Expanded Legal Assistance Program (ELAP) at their installation, legal assistance attorneys will have to refer many of these cases to private practitioners if the parties do not resolve the situation out of court. Private practitioners, whose livelihood depends on getting paid, may hesitate to take a case if the potential for the court awarding attorney's fees is not present.

7. May provide a source of counter-claims. Many cases in the consumer area come to light as counterclaims to actions against the consumer. For example, a creditor sues the consumer to recover a debt allegedly owed. The consumer will then raise consumer protection violations by the creditor as defenses or counter-claims against the creditor. In addition, some state statutes provide a mandatory counterclaim provision. If the consumer has a claim against the merchant, it must be resolved in the same suit as the underlying action against the consumer.

IV. GENERAL UDAP PRINCIPLES.

A. Burden of Proof:

1. Pleadings must allege a UDAP statute violation.

[3] *Id.*

2. The burden of proof is on consumers to prove facts that meet the elements required by the statute.

B. Liberal Construction. UDAP statues should be interpreted liberally to effect their object, to eradicate deception, protect consumers, and to correct marketplace imbalances. UDAP Statutes are generally considered remedial in nature. Thus, courts construe them liberally in favor of consumers. *See* e.g., *Boubelik v. Liberty State Bank*, 527 N.W.2d 589 (Minn. App. 1995); *Iadanza v. Mather*, 820 F.Supp. 1371 (D.Utah 1993); *Smith v. Commercial Banking Corp.*, 866 F.2d 576 (3d Cir. 1989), *Schnall v. Hertz Corp.*, 78 Cal.App.4th 1144, 93 Cal. Rptr. 2d 439 (2000); *Dressel v. Ameribank*, 247 Mich. App. 133, 635 N.W. 2d 328 (2001).

V. SCOPE.

A. Statutory Definitions: Many state statutes limit their applicability to certain kinds of transactions. The common definitions for the general types of transactions covered are below.

1. Trade or commerce. Usually a very broad interpretation that would apply to almost any profit-oriented transaction. This would normally include sales, financing, debt collection, and warranty actions. Some things not commonly thought to be trade or commerce are considered to fall into this category. For example, doctors, lawyers, and other professionals are considered to be conducting trade or commerce. A scheme to defraud workers compensation insurers is in trade or commerce. See *St. Paul Fire& Marine Ins. Co v. Ellis & Ellis*, 262 F.3d 53 (1st Cir 2001) (Mass. Law). Academic Research and publication is not considered trade or commerce because they are not entrepreneurial. See *Johnson v. Schmitz*, 119 F. Supp. 2d 90 (D. Conn. 2000)

2. Goods.

a) Some apply UCC definition from sections 2-105 and 9-105, rather than their own definition.

b) Case law has found that the following:

(1) Are NOT Goods: money, an intangible property right, such as a joint venture. See *Stroud v. Meister*, 2001 U.S. Dist LEXIS 13282 (N.D. Tex. Aug. 22, 2001).

(2) ARE Goods: Living property like a horse; construction of a house on land (although the real estate is not)

3. Merchandise. Sometimes given a broader scope than goods, merchandise usually includes various types of property such as goods, services, realty, commodities, and intangibles. Thus, money and real property have been considered merchandise even though they are not "goods."

4. Services. Performance of services for consumers generally includes home construction, tax and investment advice to include brokerage, snow removal, heir tracking, banking services, mortgage brokering, removing snow and trash, and insurance adjusting and legal services. See *Cuyler v. Minns*, 60 S.W. 3d 209 (Tex App. 2001) (Client could sue even though attorneys did not charge for their services.).

5. Personal, family or household use. Many UDAP statutes limit applicability to personal, family, and household related transactions, expressly excluding business related transactions.

a) Objective v. Subjective. Courts differ as to the standard for determining what constitutes a personal versus business transaction.

(1) Subjective refers to the consumer's personal intent for the use of the goods or service.

(2) Objective refers to the intended use of the good or service by a reasonable (typical) consumer.

b) Other statutes (such as Truth in Lending, Magnuson-Moss Warranty Act, Fair Debt Collection) use the phrase "personal, family, or household use," making cases decided under those statutes persuasive precedent.

c) A wide variety of things have been found to be for personal, family or household use. For example, an antique is personal even when bought for display at the office. A pyramid scheme has been considered a consumer transaction, even though it is a "business" opportunity. Where a use is part personal and part

commercial, courts generally find the transaction to be covered by UDAP statutes.[4]

d) Courts have found numerous transactions not to be for personal, family or household use. For example, the purchase of a hay bailer to be used on family farm; ownership of a house for use as rental property; the making of business loans; investment advice; political solicitations; and a debt for taxes.

B. Scope issues that may sometimes exempt a transaction from UDAP coverage.

1. Credit and banking activities.

a) Usually INCLUDED where UDAP statute applies to "goods & services" or "Trade or Commerce."

b) When credit and banking activities are not covered, the UDAP statute will generally use express language to exempt these activities.

2. Debt collection.

a) Usually INCLUDED where UDAP statute applies to "Trade or Commerce." A Florida Court and Tenn. Supreme Court have decided that post sale repossession practices do not relate to the original sale and thus are not covered. See *City of Cars, Inc v. Simms*, 526 So. 2d 119 (Fla Dist. Ct. App. 1988); *Pursell v. First Am. National Bank*, 937 S.W.2d. 838 (Tenn. 1996). But see *Holley v. Gurnee Volkswagen & Oldsmobile Inc*., 2001 U.S. Dist LEXIS 7274 (N.D. Ill. Jan 4, 2001) (The court held repossession is covered).

b) The underlying debt, however, must be connected to the sale of goods and services for the collection to be covered.

3. No-purchase activities.

a) UDAP statutes generally require a purchase (sale) or solicitation in order to apply.

[4] *See, e.g.*, Marascio v. Campanella, 298 N.J. Super.491, 689 A.2d 852 (App. Div. 1997) (commercially owned, unoccupied property that is part residential and part commercial still covered by UDAP statute).

b) Thus, sweepstakes offers, shoplifters, free counseling, mere offers to sell have been found to NOT fall under UDAP statutes.

c) Where dealer loaned car to consumer free of charge UDAP does not apply.

4. Post sale activities - most states do include this in "trade or commerce" and in "sales of goods and services." Thus failure to pay out an insurance claim is within trade or commerce. However, it may be an issue in a minority of states.

5. Real property. States split on this issue.

a) "Trade or commerce" and "merchandise" states: Courts in these states consistently find that real property falls within the UDAP statute. A UDAP Statue that applies to "property" covers real estate sales.

b) "Sales of consumer goods & services" states tend to find that real property does NOT fall within the UDAP scope. (e.g. AK, FL, MO.). A few courts, however, still include real property (e.g. PA, CO, & IL).

c) Some states include real estate transactions but have special provisions; for example Indiana's UDAP statue covers real estate transactions, but only the attorney general may bring action and only if the seller intended to defraud or mislead. In New York, the highest court held that the UDAP statute may not apply to a simple sale of a house, but would apply to a seller of homes who promoted the sale of over priced homes, promised repairs, claimed FHA involvement, steered buyers to affiliated banks and lawyers who would not alert the buyer to problems, and threatened to withhold down payments. See *Polonetsky v. Better Homes Depot*, 97 NY.2d 46, 760 N.E.2d 1274 (2001).

6. Residential Leases; Mobile Home Parks.

a) Many states include these within UDAP, especially those that use the "trade or commerce" definition.

b) Minnesota and Texas courts have found UDAP statutes to apply to landlord-tenant matters. See *Love v. Amsler*, 441

N.W. 2d 555 (Minn. Ct. App 1989) and *Myers v. Ginsburg*, 735 S.W.2d 600 (Tex. App. 1987).

c) A few states have held that comprehensive landlord-tenant regulation occupies the field and prevents UDAP action. (KS, OH & WA).

d) Rental of real property is explicitly included in UDAP statutes in MD, MI and NJ.

VI. ANALYZING UDAP CASES.

A. Look for *per se* violations in all aspects of the transaction.

1. Statutory "Laundry list" (*per se* violations). Some UDAP statutes have a laundry list of prohibited practices plus a catchall phrase prohibiting other deceptive practices.

2. State UDAP regulations (*per se* violations). About half of the states have regulations making listed activities a *per se* UDAP violation.

3. Violation of Federal Consumer Protection Statutes.

4. Make sure violation is within the scope of the UDAP statute.

5. Even if the deceptive act or practice falls under a *per se* violation, pleadings should always include a general or catch all claim in case the *per se* violation fails because of a technical reason.

B. Proving violation when there is no per se violation. When a practice must be proven without the aid of a *per se* theory, the consumer should adopt a three prong approach.

1. Develop the Facts. Painting a broad detailed picture will help the judge or jury find in favor of the consumer and help the consumer (plaintiff) identify corroborating victims. The consumer lawyer should carefully investigate the following:

a) Advertising.

b) Written promotional material.

c) Oral claims.

d) Key facts not disclosed.

e) Sales techniques.

f) Contract terms.

g) Collection practices.

h) Credit terms.

2. Look for precedent applicable to a specific practice that holds that the exact practice or a similar practice is a UDAP violation. Look for the following:

a) Case law.

b) State and federal statutes and regulations (Don't forget legislative history!)

c) Staff commentaries.

d) FTC Cases/Consent Agreements.

e) FTC Trade Regulations, Rules, Letter Rulings.

3. Use General UDAP standards to show how the action violates broad deception and unfairness standards in UDAP statutes.

VII. GENERAL UDAP VIOLATIONS.

A. Deception/Statutory Fraud. Some states prohibit deception. Others prohibit misleading or fraudulent conduct. Many state UDAP statutes prohibit both deceptive and unconscionable practices. Consumers need to show only one or the other, not both.

1. Compare to common law fraud.

a) Common law fraud requires proof of:

(1) A false representation of a material fact.

(2) Detrimental reliance on the fact at issue.

(3) Damages as a result of the reliance.

(4) Scienter-usually requiring the defendant to have knowledge of the falsity.

(5) Defendant's intentional misrepresentation seeking reliance.

b) Deception - modern conception virtually eliminates these proof requirements.

(1) Shaped by federal court interpretation of the FTC Act. To show deception under the FTC Act, intent, scienter, actual reliance or damage, and even actual deception are unnecessary.

(2) Capacity to deceive is enough! Proof that a practice has a tendency or capacity to mislead or deceive even a significant minority of consumers may be sufficient to support a finding that the practice is deceptive.

(a) FTC has interpreted to the FTC Act to require that the practice be “likely” to deceive.

(b) Most state courts have continued to follow the standard of “tendency or capacity” to support a finding of deception under state UDAP statutes.

(3) Jurisdictions that require proof of actual damages generally construe the requirement liberally in favor of the consumer.

(4) The burden of proof is normally preponderance of the evidence, unlike the clear and convincing standard for proving common law fraud.

(5) Seller’s behavior may not cure an otherwise deceptive practice.

(a) A good faith effort, e.g. acting on advice of counsel is not a defense.

(b) Cessation of practice at time of suit is not a defense under FTC act (but will be considered in a case seeking an injunction.)

(c) Industry-wide practice. It is not a defense that the challenged practice is engaged in throughout the industry or is a customary business practice. For example, it is not a defense that none of the state's auto repair shops comply with a written authorizations regulation.[5]

(d) Mere Puffing. To show that a practice amounts to mere puffing the seller must demonstrate that the practice is harmless, fanciful, and has no capacity to deceive.

2. Vulnerable Consumers.

a) Historically - "the ignorant, the unthinking, and the credulous . . . ." *Charles of the Ritz Distributors Corp. v. Federal Trade Commission*, 143 F.2d 676, 679 (2d Cir. 1944). Courts today label these consumers the "least sophisticated." *See, e.g., Taylor v. Perrin, Landry, Delaunay & Durand*, 103 F.3d 1232 (5th Cir. 1997); *Clomon v. Jackson*, 988 F.2d 1314 (2d Cir. 1993).

b) FTC has begun to look at the target audience and see if they are behaving reasonably for that audience under the circumstances.

c) Courts have stuck to the least sophisticated standard, a practice can be deceptive even if most consumers are not misled and only especially vulnerable consumers are deceived.

B. Unfairness. Does not mislead, merely takes advantage of. In states providing a private right of action for unfair practices, consumers are given a highly flexible remedy that can be used innovatively. See *Curtis Mfg. Co. v. Plastic-Clip Corp.*, 888 F. Supp. 1212 (D.N.H. 1994) (holding that New Hampshire UDAP statute's list of unfair and deceptive acts is non-exhaustive, and the facts can establish that other conduct is unfair).

[5] Huff & Morse, Inc. v. Riordan, 345 N.W.2d 504 (Wis. Ct. App. 1984)

1. Broader than deception.

2. Historical Criteria. *FTC v. Sperry and Hutchinson Company*, 405 U.S. 233, 244-45 (1972) [hereinafter "S&H"]. Do not have to prove all three, can show practice unfair with showing just one of the elements listed in the S&H case. The criteria include the following:

   a) Does the practice offend public policy? (Is it within the penumbra of some common law, statutory, or other established concept of unfairness?)

   b) Is the practice immoral, unethical, oppressive, or unscrupulous?

   c) Does the practice cause substantial injury to consumers?

3. FTC Standard (1980; codified in 1994, 15 U.S.C. § 45(n))

   a) Fairly broad acceptance federally. However, States tend to stick to the S & H standard and their own jurisprudence.

   b) Focuses almost exclusively on substantial consumer injury.

   c) Criteria for FTC standard.

      (1) Likely to cause substantial injury to consumers;

      (2) The injury must NOT be outweighed by any countervailing benefits to consumers or competition that the practice produces; AND

      (3) The injury must be of the type that the consumers themselves could not have reasonably avoided.

   d) The distinctions between the current FTC standard and the S&H standard may have little practical effect because unfairness is a question of fact for the jury or judge.

   e) Application of Unfairness. For purposes of state UDAP statutes unfairness is not limited to traditional notions of deception or fraud, but encompasses other types of wrongful business conduct and can be unfair even if it is permitted by

statute or common law principles. The following are examples of practices found to be unfair.

(1) Contracts of adhesion.

(2) Coercive (high pressure) sales.

(a) Intimidation.

(b) Coercion.

(c) Personal disparagement.

(d) Refusing to let customers leave until they sign contracts.

(e) Dismantling equipment and refusing to put it back together until customer signs service contract.

(f) Refusing to return down payment unless customer agrees to forfeit portion of down payment.

(3) Pressuring vulnerable groups like children or homeowners with marginal credit leaving a vacuum where predatory lending can develop.

C. Unconscionable.

1. Unconscionable practices are also unfair. UDAP cases found it to be unfair to charge unconscionable high prices for autos or lease to own TVs that cost twice as much than if you bought it directly. In Texas, it is a UDAP violation to take advantage of a disaster declaration by the Governor by charging exorbitant prices for necessities. An $1156 fee to cash an $11,171 social security check has been found to be a UDAP violation. See *In re Wernly*, 91 B.R. 702 (Bankr. E.D. Pa. 1988).

2. Factors.

a) Seller took advantage of inability of consumers to protect their interests.

b) Price grossly exceeded that of similar available items.

c) Consumer unable to receive a substantial benefit from transaction.

d) No reasonable probability that the consumer could pay in full.

e) Transaction was excessively one-sided in favor of the seller.

f) Seller made a misleading statement of opinion that was likely to cause the consumer to rely to his/her detriment.

3. 17 States prohibit unconscionable practices (AL, AR, D.C., FL, ID, IN, KS, KY, MI, NE, NJ, NM, NY, OH, OR, TX, UT) See also: Cal Civ Code § 1770(a)(19).

VIII. TYPES OF UDAP ACTIONS.

A. Unsubstantiated claims. It is a UDAP to make an unsubstantiated claim about a product even if the claim later turns out to be true.

1. Deception action. More than just wishful thinking about a product. Every product claim carries with it a representation that the party making the claim possesses a reasonable basis for doing so.

2. Unfairness action. Based on an imbalance of knowledge. Economically more reasonable for the manufacturer to substantiate a

claim than for the consumer. Easier to show seller did not have an adequate basis for making a claim at the time it was made. If an advertiser makes claims allegedly based on scientific surveys or studies, they must meet scientific standards and results have to be accurately and fairly reported.

B. Deceptive pricing.

1. Bait and switch. The advertising of a product with no intention of selling it (the bait) in order to get consumers into the building and get them to buy something else (the switch), usually a higher priced product.

2. Unavailability of advertised items. Similar to a bait and switch, except the business does intend to sell the advertised products, but has very few of them. The purpose is the same. Once the business sells the few it has, the business will try to get the consumer to buy something else. Stores can comply by clearly and adequately disclosing limitations of availability on advertisement.

3. Bargain sales. Comparing a “sale” price to a reference price that makes it appear that consumers are getting a bargain when, in fact, they are not.

4. Other: Wholesale, factory-direct, seconds, "below-cost/invoice," "liquidation sale," "going-out-of-business." The special circumstance such as the bankruptcy or flood sale must be true, the prices have to be lower than regular, and the seller cannot order additional goods for the sale.

5. Free. Usually to get the “free” item, you must buy another item that is marked up to help defray the cost of the “free” item to the business. The FTC also prohibits many of these types of schemes. Not allowed to mark up price on non-free item.

6. Low-balling. The seller advertises a low price, but through a variety of means, ends up selling it to the consumer for a higher price. This frustrates the consumer’s comparison-shopping. It is deceptive to sell goods above advertised price.

7. Consumer special selection/winning. Making the offer seem like a good deal by saying the consumer is “specially selected” or has won the opportunity for the deal when the scheme is really designed to

make contact with prospective buyers and special prices are not being offered.

8. Offering goods and services to consumers without disclosing all conditions and limitations on the offer is deceptive.

C. General Misrepresentation.

1. Uniqueness. Making false claims about a product's uniqueness, exclusiveness, or originality.

2. Safety. Failure to disclose latent safety risks associated with a product.

3. Quality and comparison. Misrepresenting "a product's quality, style, nature, composition, identity or ingredients."[6]

4. Size. Misrepresenting a product's size or weight usually by using oversized containers, slack fill in the container, etc.

5. Endorsement. Misrepresenting the endorsement or approval of a product by an agency, company, or government organization.

6. Products characteristics, uses and benefits. A representation that an insurance policy would last as long as the plaintiff lived was a UDAP violation because it misrepresented the characteristics of the policy. See *Jones v. Ray Ins. Agency*, 59 S.W.3d 739 (Tex. App. 2001).

7. Products method of manufacture such as made by handicap persons.

8. Approval or affiliation of a product.

D. Deceptive performance practices.

1. Layaway. Sellers must disclose all aspects of their layaway policies to consumers. Specifically, they must disclose the goods covered, the period the offer is held open, the down payment, and the cash price. The seller must hold the specific goods or an exact duplicate when payment is made, must be price originally agreed upon.

[6] NCLC UDAP at § 4.7.3.

2. Delay and non-delivery. Failure to make prompt delivery or to honor a request for a full refund when delivery is delayed unreasonably. If delivery is going to be late seller must disclose right to full refund.

3. Damaged and defective goods. Failure to disclose defects or damages known to the seller, even if the sale is "as is." Most of these cases deal with automobile sales. Concealment of known defects could also be fraud.

4. Used as new. Sellers must disclose when a product is rebuilt, reconditioned, etc. Selling demonstrator car as new not UDAP when seller told buyer it was a demonstrator and buyer signed knowing mileage. See *Hodges v. Koons Buick Pontiac GMC, Inc*., 2001 U.S. Dist. LEXIS 9591 (Jan 3, 2001).

5. Packaging – Oversized boxes or containers misrepresenting the size, amount or dimension of the product.

IX. UDAP APPLICATION TO SELECTED AREAS.

A. Debt collection.

1. UDAP statutes may provide relief when Fair Debt Collection Practices Act cannot such as:

a) For creditor abuses,

b) When creditors do not oversee the collection practices of the collections agencies they hire to collect their debts,

c) or may provide for better relief such as attorney fees.

2. Misrepresentations as to

a) Identity/affiliations of collector such as:

(1) Work with U.S. Marshall or Sheriff's office.

(2) Work for government agency.

(3) Use of fictitious titles for their job position.

(4) The debt collector or creditor must disclose that letters, forms, questionnaires are for the purpose of collecting a debt.

b) Imminence of threatened actions.

(1) Cannot threaten that nonpayment "may" result in litigation unless suit is the ordinary response.

(2) Cannot threaten that if no payment is received within a specified number of days, a specified action will be initiated if that determination has yet to be made.

(3) Cannot use simulated telegrams to misrepresent the urgency of the matter.

c) Legal consequences.

(1) Cannot be designed to create fear and take advantage of consumer's ignorance of legal procedures.

(2) Cannot threaten garnishment without telling the consumer a court order is required.

(3) Cannot say debtor is subject to prosecution under Federal Mail Fraud Statutes.

3. Harassment.

a) Threats of violence.

b) Threats of ridicule.

c) Threats to inform employers.

B. Contracts/Warranties.

1. A mere breech of contract without anything else does not necessarily lead to a UDAP violation.

2. Systematic breech of many consumer contracts or a failure to disclose is a UDAP violation. See *Guste v. Orkin Exterminating Co.*, 528 So.

2d 198 (La. Ct. App. 1988) (Orkin promised fixed annual renewal prices and then unilaterally raised the fees for 200,000 customers.).

3. It is an unfair practice not to provide disclosures in the same language as the advertisement.

4. Misrepresentation as to cancellation rights.

5. Confusing contract terms may even be unfair. *See, e.g., Michaels v. Amway Corp.*, 206 Mich. App. 644, 522 N.W.2d 703 (1994); *Orlando v. Finance One*, 369 S.E.2d 882 (W.Va. 1988). Oral representations inconsistent with the written contract, even if the contract states that oral representations inconsistent with the contract are not part of the deal. See also *Commonwealth v. Monumental Properties*, 459 Pa. 450 (1974); *Oldendorf v. Gen. Motors Corp*, 322 Ill. App. 3d 825 (2001); *Gonsalves v. First Ins. Co*. 55 Haw. 155 (1973).

6. Entering into a contract with no intention to fulfill obligations is a UDAP violation.

7. UDAP violation to conceal breach of contact as long as possible.

8. Most state courts find warranty breach as a *per se* UDAP violation.

C. Insurance.

1. Look at State Unfair Insurance Practices (UNIP). Every state has adopted UNIP legislation, which defines and prohibits unfair methods of competition and unfair or deceptive acts and practices in the insurance business.

2. Violations of state UNIP are probably *per se* violations of state UDAP.

3. If not UNIP violation, still look to State UDAP.

D. Rent-to Own (RTO).

1. The RTO industry is a major source of sales, particularly of appliances, to the low income community. The industry markets to low income consumers by advertising in minority media, on buses, and in public housing projects.

2. Deceptive inducements or sales practices. RTO companies will often use many of the techniques already mentioned including, bait and switch, low-balling, etc. In addition, look carefully for other misrepresentations, such as describing the transaction as a lease when it is in fact a contract for sale.

3. Disclosure problems. Look for lack of disclosure in the sale. Usually, the companies will not disclose the total of all the payments (which is 3 or 4 times the normal sale price) or the effective annual percentage rate, which is often usurious.

4. Repossession. Many times the RTO companies will use misrepresentations in repossession efforts to coerce the consumer into paying. This includes threats of criminal or civil actions they have no intention of pursuing, misrepresenting their workers as law enforcement officials, and seeking more than they are entitled to under the contract to settle the matter.

X. GENERAL UDAP PROCEDURE.

A. Notice or Demand Letter.

1. Required in nine states (AL, CA, GA, , IN, MA, ME, TX, WV,WY) as a precondition to suit. (MS requires that the consumer utilize an informal dispute resolution procedure prior to the suit.)

2. Gives seller an opportunity to resolve informally.

3. Different from notice provisions. Notice to the Attorney General before judgment is entered is a precondition to suit.

4. Must give the seller sufficient information to review the law and determine whether the requested relief should be granted.

   a) Identify claimant.

   b) Reasonably describe the unfair and deceptive practice.

   c) Reasonably describe the injury.

5. In writing.

6. MailBox Rule. The principle that when a pleading or other document is filed or served by mail, filing or service is deemed to have occurred on the date of mailing.

B. Elements to Plead. Some state courts have developed a standard list of elements for a UDAP claim. (CO, DE, GA, HI, IL, MN, NH, NJ, NY, NC, OK, OR, PA, SC, TN, TX, VT, WA, WI).

C. Allegations should be specific in order to organize the case and to make it more credible.

D. Public interest.

1. In some states (CT, CO, WA, IL, GA, MN, NE, SC, NY.), the suit must be in the public interest.

a) Violates a statute that has a specific legislative declaration of public interest impact, or

b) Part of pattern or general course of conduct that has the real potential of repetition.

2. Most states do not have this requirement.

E. Damages. A private cause of action exists in every state except Iowa, but actual damages may be a prerequisite in some states.

1. Actual. Some damage.

2. Consequential damages, all damages foreseeable flowing from a UDAP.

3. Statutory. Vary between $25 to $5,000, even if actual damages have not been proven.

4. Treble damages are possible for willful, bad faith, and intentional violations.

F. Class actions. Preconditions by one may satisfy preconditions for all. Class actions adjudicate numerous claims that individually damaged consumers would not pursue because they are uniformed of their rights, deterred from filing individual suits because of ongoing relationships with defendant, or because their claims may be too small to merit adjudication.

G. Attorney's fees.

1. Almost all states that authorize a private cause of action authorize reasonable attorney's fees for successful litigants.

2. UDAP statues make it possible for attorneys to devote significant resources to a case even if the consumer's dollar loss is relatively minor. This encourages consumers to remedy marketplaces abuses and increases the seller's maximum liability if they refuse to settle.

3. However, some limit the amount/allowance of fees based on the consumer status (personal v. business); certain defenses (bona fide error defense); or the seller's conduct (willful v. negligent).

H. Evidence to look for in UDAP cases.

1. Pattern of practice.

a) Sales manuals.

b) Training materials.

c) Internal memos.

2. Former employees.

3. Look at all written materials to see if they are deceptive on their face or fail to comply with applicable rules or regulations.

4. Seek discovery of all persons who have purchased or borrowed from the merchant within specified time frame- relevant for punitive damage claims, can also show impact on public.

5. Evidence of merchant's financial status.

6. Look for collected consumer complaints from FTC, Better Business Bureau, and state or local enforcement agencies. (Military Sentinel website).

7. The merchant's own business web site.

8. Past court records.

9. Publicity about consumer's plight may bring out other victims or disgruntled past employees.

10. Consider expert testimony.

XI. CONCLUSION

See Appendix B of the Consumer law guide for state UDAP statutes

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CHAPTER 3

PROTECTIONS BASED ON THE TRANSACTION

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CHAPTER 3

PROTECTIONS BASED ON THE TRANSACTION

I. COOLING OFF PERIOD FOR DOOR-TO-DOOR SALES (a.k.a. Rule Concerning Cooling-Off Period For Sales Made At Homes Or At Certain Other Locations).

A. References.

1. 16 C.F.R. § 429. Promulgated by the FTC under its authority to regulate unfair and deceptive acts and practices, the Rule Concerning Cooling-Off Period For Sales Made at Homes or at Certain Other Locations is found in the CFR rather than a consumer protection statute.

2. National Consumer Law Center, Unfair and Deceptive Acts and Practices, § 5.8.2 (6th ed. 2004).

3. State statutes, Appendix B.

B. General.

1. The Rule gives the consumer the unilateral right to rescind consumer purchase contracts for three business days following a door-to-door sale.

   a) It is purely a unilateral right. The consumer does not need to have any reason at all.

   b) This is separate authority from any other source of claim that the consumer may have, such as a warranty or other protection.

   c) Right to rescind may be exercised even if the seller has performed the service before cancellation. Example – A home improvement contractor performs right away, consumer cancels, the builder can only take back material, but cannot charge for the service. Could be a UDAP if the seller performed in order to frustrate consumer's cancellation right.

2. Rule contains disclosure requirements and notice requirements.

a) Violations of either the disclosure or notification rules can arguably give rise to a remedy.

b) The problem, as we shall see below is that the rule contains no explicit enforcement mechanism for the consumer. Enforcement is left to the FTC.

C. Definitions and exclusions.

1. Door-to-door Sale.

a) Sale, lease or rental (rent-to-own companies routinely do not provide notice).

b) Consumer goods and services (primarily for personal, family, or household purposes).

c) Total purchase price of $25.00 or more (includes interest and service charges).

d) Personal solicitation by the seller.

e) At a place other than the permanent place of business of the seller. For example:

(1) Buyer's residence. A company that persuades a sale prospect to invite their neighbors to an in-home sales meeting is covered under the rule.

(2) Facilities rented on a temporary or short-term basis including hotel or motel rooms, convention centers, fairgrounds, or restaurants.

(a) This could happen to soldiers. A Marine was on liberty and eating pizza in a local pizza parlor. He was apporached by an attractive young female who struck up a conversation with him. During the conversation the talk gradually turned to what a wonderful job she had and what a great boss she had. As it turned out (no coincidence) the boss was also in the pizza parlor. He came over and began a sales pitch. Before it was over, the Marine had purchased a

photographic reproduction package. The Rule applies to this scenario because it occurred in a place other than the regular place of business of the seller.

(3) Sales at the buyer's workplace.

(4) Sales in dormitory lounges (barracks).

2. Business day. Any calendar day except Sundays and federal holidays. The current federal holidays are New Year's Day, Martin Luther King, Jr.'s Birthday, Presidents Day, Memorial Day, Independence Day, Labor Day, Columbus Day, Veteran's Day, Thanksgiving and Christmas. The day of sale is excluded in the calculation.

3. Exclusions.

a) Pre-arranged visits after initial contact at a seller's regular place of business. An example would be if you went to Sears and saw a kiosk for vinyl siding. The person at the counter makes an appointment for the sales rep to come to your house. The Rule does not apply because it is a pre-arranged visit.

b) Contracts in which the cooling-off period of the Truth-in-Lending Act applies. (See TILA outline).

c) Buyer-initiated contacts for a bona-fide emergency need provided the seller obtains a written waiver dated and signed by the buyer explaining the emergency. This is designed to eliminate the rule's applicability to items such as purchases of a new heating unit in the middle of winter when your old one gives out.

d) Solicitations by mail or telephone, but the Mail and Phone Order Rule or the Telemarketing Rule may apply. The FTC has adopted telemarketing rules that include disclosure requirements and include cooling off rules for certain transactions.

e) Buyer initiated visit for repairs of personal property. This eliminates the appliance repairman and the like from the rule.

f) Sale (or rental) of:

(1) Real property.

(2) Insurance.

(3) Securities.

g) Automobile tent sales/auctions (where dealer has permanent place of business elsewhere).

h) Craft Fairs.

D. Requirements of the Rule.

1. Copy of the fully completed contract for the consumer to retain. This means no blanks. This is a common way for legal assistance attorneys to win - look for blanks - the more the better and particularly those in the cooling off period part of the form or the TILA disclosures. Sellers often copy other seller's disclosure notices not realizing that the other seller has properly deleted language not applicable to their sale, however it is applicable to the new seller.

2. Oral and written notice of the rescission right.

a) One easily detachable, fully completed copy for consumer, one copy for consumer to send to seller to cancel the contract;

Here is another place where some of the scam artists blow it - although these errors are getting rare. They print the rescission form on the back of the Truth in Lending disclosures. When the consumer sends in the rescission form they tear off part of the TILA disclosures. Or alternatively, they do not leave enough copies of the form for the consumer.

b) Date of transaction, and;

c) Name and address of seller. This is the permanent address for purpose of sending the notice of recision.

d) Seller must orally inform the consumer of the right to rescind.

- This becomes a problem of proof. The rule requires oral notice. The legal assistance client frequently denies it. The

company rarely has proof, but some tape a verification call and may then have proof.

e) Notice of the right to rescind must be in close proximity to the signature block of the consumer.

f) Seller must not attempt to misrepresent right to rescind.

g) Notice must be in bold print.

h) Notice must be in the same language as that used during the sales presentation.

i) Notice need not conform exactly to FTC recommended language.

3. Waiver is not allowed. (Exception - emergency needs).

4. Sellers must honor rescission.

a) Seller not permitted to sell or transfer credit note before midnight on the fifth business day following the transaction.

- Frequent violation. The seller cannot transfer any note until the rescission period has passed.

b) If the consumer cancels the contract, the seller has 10 days within which to provide the consumer with instructions regarding the disposition of the goods already delivered to the consumer.

E. Mechanics of rescission.

1. Consumer must mail or deliver written notice to seller before midnight of the third business day following the transaction.

a) Problem of proof - mailing - best to use return receipt mail - that leaves the consumer with a form to keep. If you use telegraph, fax etc - get some sort of proof of transmission.

b) Both Ohio and Delaware have allowed a continuing right to cancel beyond the three days if the notice is defective. See

Pinnacle Energy v. Price, 2001 Del. C.P. LEXIS 28 (Mar. 21, 2001) and *Williams v. Shroyer*, 2000 Ohio App. LEXIS 5798 (Dec. 13, 2000).

2. Use cancellation form provided by the seller, or, use any written form, to include a telegram, that communicates the desire to rescind to the seller.

   a) Rule really does mean any form - you can write it on a MRE carton and mail it and it is effective - Dear seller I cancel, love, Buyer.

   b) However, mere stopping payment on a check may not be enough.

3. Seller must return trade-in, if any, within 10 days or receipt of consumer's notice.

4. Consumer's responsibilities following rescission.

   a) Make goods already delivered available to the seller, or,

   b) Follow the seller's instructions regarding return of the goods.

5. Return is at the seller's expense.

6. Risk of loss during return is on the seller.

7. If the seller fails to pick up the goods within 20 days, the consumer may retain the goods with no further obligation to the seller.

F. FTC Application and Interpretation of the Rule.

1. Strict interpretation against the seller.

2. If the buyer cancels the contract after the seller has performed, there is no recovery for the seller based on *quantum meruit*. Some states, however, do interpret their own rule to allow for *quantum meruit* recovery. If the seller is performing work in order to discourage the buyer from exercising cancellation rights, look to state UDAP statutes for relief.

3. The federal rule does not provide for an extended right to rescind for noncompliance with the notice provisions, but state UDAP statutes may.

G. Remedies.

1. No independent cause of action for rule violation.

2. Rule violation may be *prima facie* evidence of a state UDAP violation.

H. Relationship with state laws.

1. Rule does not preempt state law, except when state law is directly in conflict with the rule.

2. Examples.

a) State law authorizing a cancellation fee preempted.

b) State law with no requirement for providing notice preempted.

3. Some state laws have broader coverage than the FTC Rule. See *Williams v. Schroyer*, 2000 Ohio App. LEXIS 4798 (Dec. 13, 2000) (home repair transactions are covered where buyer originally calls seller but then further negotiations take place at the buyer's home.)

II. TELEPHONE AND INTERNET TRANSACTIONS.

A. References.

1. National Consumer Law Center, Unfair and Deceptive Acts and Practices §§ 5.9 (6th ed. 2004).

2. Telephone Consumer Protection Act of 1991, 47 U.S.C. § 227 (2000).

3. Telemarketing and Consumer Fraud and Abuse Prevention Act, 15 U.S.C. §§ 6101 - 6108 (2000) [implemented by the Telemarketing Sales Rule].

4. Telemarketing Sales Rule, 15 C.F.R. § 310.

5. Telephone Disclosure and Dispute Resolution, 15 U.S.C. § 5711 (2000) [implemented by the Telephone Discolusure and Dispute Resolution Rule].

6. Restrictions on Use of Telephone Equipment, 47 U.S.C. § 227 (2000).

7. Telephone Disclosure and Dispute Resolution Rule, 16 C.F.R. § 308.

8. FCC Report and Order In the Matter of Rules and Regulations Implementing the Telephone Consumer Protection Act of 1991, CG Docket No. 02-278, FCC 03-153 (July 3, 2003). .

9. State telemarketing statutes (see Appendix B).

B. Overview.

1. Developments in communications technology, including widespread use of the internet, cellular telephones, and autodialing, have resulted in new and overlapping rules and regulations governing solicitation of consumers.

2. Both the Federal Communications Commission (FCC) and the Federal Trade Commission (FTC) have important roles in protecting consumers from abusive practices involving telephone, computer, and facsimile solicitations.

3. The manner in which a consumer may enforce substantive rights, including his or her entitlement to damages, will be determined by the applicable federal statute, an analogous state statute, or an applicable state UDAP statute.

C. Telephone Consumer Protection Act (TCPA) of 1991.

1. General. The TCPA is implemented by the FCC through its promulgation of Restrictions on Telephone Solicitation, 47 C.F.R. § 64.1200.

2. Unlike other consumer protections statutes that address deficiencies in traditional contract law as applied to consumers, the TCPA is primarily concerned with protecting consumer privacy by preventing unwanted or harassing commercial solicitations.

3. Prohibitions and requirements. The statue and rule create the following prescriptions and prohibitions.

   a) Automatic telephone dialing systems, or an artificial or prerecorded voice, may not be used to initiate a telephone call to any of the following:

      (1) Emergency telephone lines; including "911", or emergency numbers to hospitals, doctors, health clinics, poison control center, or fire or police departments.

      (2) Guest room or patient room of a hospital, health care facility, elderly home, or similar establishment.

      (3) Any telephone number assigned to a paging service, cellular telephone service, specialized mobile radio service, or other radio common carrier service, or any service for which the called party is charged for the call.

   b) Artificial or prerecorded voice may not be used to initiate any telephone call to any residential line without the prior consent of the called party, unless the call:

      (1) Is made for emergency purposes;

      (2) Is not made for a commercial purpose;

      (3) Is made for a commercial purpose but does not involve an unsolicited advertisement;

      (4) Is made to a person with whom the caller has an established business relationship at the time the call is made; or

      (5) Is made by or on behalf of a tax-exempt nonprofit organization.

   c) A telephone facsimile machine, computer, or other device may not be used to send an unsolicited advertisement to a telephone facsimile machine.

d) Telemarketing calls that are legally permissible may not be disconnected prior to 15 seconds or 4 rings.

e) No more than 3 percent of answered calls may be "abandoned," meaning that no live sales representative is connected to the call within 2 seconds after the called person's greeting.

f) All artificial or prerecorded telephone messages must initially state clearly the identity of the individual or business responsible for initiating the call; and, prior to the conclusion of the call, a telephone number at which the responsible entity may be called.

g) Telemarketing calls may not be initiated to a residential telephone subscriber between 9:00 p.m. and 8:00 a.m. (local time at the called party's location).

h) In a separate rule, the FCC has required all telemarketers to transmit Caller ID information to the called party. 47 C.F.R. § 64.1601(3).

4. Do-Not-Call Registry.

a) The most widely publicized provision of the TCPA requires telemarketers to maintain a company specific do-not-call list and to not call numbers listed on the national do-not-call registry.

b) The FTC's Telemarketing Sales Rule, 15 C.F.R. § 310.4(b)(1)(ii)-(iii), discussed elsewhere in this outline, contains similar provisions for do-not-call lists.

c) The National Do-Not-Call Registry referred to in both the FCC's Restrictions on Telephone Solicitation and the FTC's Telemarketing Sales Rule is located on the Internet at https://www.donotcall.gov.

(1) Registrations of residential telephone numbers, including cell phones, become effective after 31 days and remain current for 5 years.

(2) Complaints of telemarketer violation of the Do-Not-Call provisions of either rule may be submitted on the same website.

d) Specific requirements concerning do-not-call lists.

(1) Initiation of a telephone solicitation to a number on the national do-not-call registry is a violation of the rule unless the telemarketer can demonstrate one of the following:

(a) Adequate business procedures designed to comply with the rule;

(b) That the subscriber has provided a prior express invitation or permission for the call; or

(c) The telemarketer has a personal relationship with the subscriber.

(2) Telemarketers are required to maintain a company specific do-not-call list of subscribers who do not wish to receive telemarketing calls by or on behalf of that entity.

(3) Telemarketers must provide the called party with the name of the individual caller, the name of the person or entity on whose behalf the call is being made, and a telephone number or address at which the person or entity may be contacted.

(4) Tax-exempt nonprofit organizations are not required to maintain an entity specific do-not-call list.

5. Key definitions applicable to the Restrictions on Telephone Solicitation

a) "Established business relationship" means a prior or existing relationship formed by a voluntary two-way communication between a person or entity and a residential subscriber on the basis of the subscriber's purchase or transaction with the entity within the previous 18 months; or on the basis of the

subscriber's inquiry or application regarding products or services offered by the entity within the previous 3 months.

b) "Telemarketer" means the person or entity that initiates a telephone call or message for the purpose of encouraging the purchase or rental of, or investment in, property, goods, or services, which is transmitted to any person.

c) A "telephone solicitation" does not include a call or message (1) to any person with the person's prior express invitation or permission; (2) to any person with whom the caller has an established business relationship; or (3) by or on behalf of a tax-exempt nonprofit organization.

6. Enforcement.

a) The TCPA creates a private cause of action in state court authorizing either actual damages or statutory damages of $500, whichever is greater, for each violation. Treble damages are available for violations that are willful or knowing.

b) Violations supporting a cause of action include the provisions regarding prerecorded telephone calls; autodialers; receipt of more than one call in any 12-month period in violation of the do-not-call registry provisions; calls outside of the permissible time frame; blocking Caller ID; abandoning calls; and failing to provide required identification.

c) Complaints may also be filed directly with the FCC.

d) Although the federal statute does not authorize attorney's fees, state UDAP statutes may provide such an award.

D. Telemarketing and Consumer Fraud and Abuse Prevention Act

1. General. The Telemarketing Consumer Fraud and Abuse Prevention Act, passed in 1994, is partially implemented by the FTC's Telemarketing Sales Rule.

a) The purpose of the statue is to empower the FTC to issue regulations "prohibiting deceptive and abusive telemarketing acts and practices."

b) Violations of the Telemarketing Sales Rule are generally defined as unfair or deceptive acts or practices within the meaning of the Fair Trade Act.

c) Unlike the FCC's Restrictions on Telephone Solicitation, the Telemarketing Sales Rule does not create a private cause of action unless actual damages exceed $75,000. Thus, enforcement is primarily accomplished by the FTC, or by use of a state UDAP statute that creates a separate cause of action.

2. Telemarketing Sales Rule – Prescriptions and Prohibitions.

a) Deceptive Telemarketing Acts or Practices (16 C.F.R. § 310.3). The following conduct is defined as a deceptive act or practice.

(1) Failure to truthfully disclose, in a clear and conspicuous manner, the following material information before customer pays for goods or services:

(a) Total costs of the transaction and the quantity of any goods or services subject to the sale.

(b) All material restrictions, limitations, or conditions of the transaction.

(c) Any policy of not making refunds, cancellations, or exchanges.

(d) All material terms and conditions of any refund, cancellation, or repurchase policy that IS mentioned in the call.

(e) In a prize promotion, the odds of receiving a prize and all material conditions or costs to receive or redeem the prize, that no purchase or payment is required to win a prize or to participate in a prize promotion or it does not increase chances to win.

(f) In the sale of goods or services to protect, insure or otherwise limit a customer's liability in the event of unauthorized use of a customer's credit card, the limits on a cardholder's liability

pursuant to 15 U.S.C 1643. (Liability limit $50).

(g) If there is a negative option feature, all material terms, including that the customer's account will be charged unless the customer takes an affirmative action to avoid the charges.

(h) In a request for charitable contribution: the identity of the charitable organization and the purpose to solicit a charitable contribution.

(2) Misrepresenting, directly or by implication, any of the following:

(a) Total costs of transaction.

(b) Any material restrictions, limitations, and conditions of transaction.

(c) Any material aspect of the performance, efficacy, nature, or central characteristics of the goods or services.

(d) Any material terms and conditions of any refund, cancellation, or repurchase policy.

(e) Any material aspect of a prize promotion.

(f) Any material aspect of an investment opportunity.

(g) Seller's affiliation with any government or third party organization.

(h) That any customer needs offered goods or services to provide protections already provided under 15 U.S.C. § 1643. ($50 limit of liability for credit card unauthorized use.)

(i) Any material aspect of negative options.

(3) Solicitors for charitable organization even if they seek donations rather than purchases of goods or services can not misrepresent the following:

(a) The nature, purpose or mission of the charity.

(b) That any charitable contribution is tax deductible.

(c) The purpose for which any charitable contribution will be used.

(d) The percentage or amount that goes to the charity after admin fees are deducted.

(e) Material aspects of prize promotions.

(f) Affiliation, endorsements or sponsorship by any person or government.

(4) Obtaining or submitting for payment a form of negotiable paper without the person's express verifiable authorization. (Includes charitable contributions). Authorization is verifiable if it is:

(a) Express and in writing.

(b) Express and made orally and is tape-recorded.

(c) Authorization must include the following: the number of payments; the dates the authorization will be submitted for payment; the customer's name and billing information; the date of customer's oral authorization; and the telephone number the customer can call for inquiry.

(d) Written confirmation of the transaction has been sent to the customer by first class mail and has all information required for oral authorization above. Prior to submission for payment and the confirmation includes all disclosures required under the Rule.

(e) Express verifiable authorization is not needed if the method of payment is a credit card subject to protections of the Truth in Lending Act and Regulation Z or a debit card subject to the protections of the Electronic Funds Transfer Act and Regulation E.

(5) Making a false or misleading statement to induce any person to pay for goods or services or to induce a charitable contribution.

b) Assisting and facilitation. It is a deceptive telemarketing act or practice to provide substantial assistance or support to a telemarketer who that person knows, or consciously avoids knowing, is engaged in a violation of the Telemarketing Sales Rule.

c) Credit card laundering. It is a deceptive telemarketing act or practice for a merchant, or an employee of a merchant, to engage in any credit card action not authorized directly by the cardholder or the merchant agreement with the cardholder.

d) Abusive Telemarketing Acts or Practices. The following are defined as abusive telemarketing acts or practices.

(1) Threats, intimidation, profane, or obscene language.

(2) Requesting or receiving payment for goods and services to fix credit reports UNLESS:

(a) The time frame in which the seller is supposed to have provided all goods and services has passed; and

(b) The seller provides the person with documentation of success in the form of a credit report having been issued more than 6 months after the results were achieved.

(3) Requesting or receiving payment for goods and services to obtain the return of money or other value from a previous telemarketing transaction until 7 business days

after the money or other item is returned to the consumer.

(4) Requesting or receiving payment or fee in advance of obtaining a loan or other extension of credit.

(5) Using preacquired account information without the expressed informed consent of the consumer including, at a minimum, obtain from the customer the last four digits of the account number to be charged. And make an audio recording of entire transaction.

(6) Disclosing or receiving, for consideration, unencrypted consumer account numbers for use in telemarketing; except in processing of payment for a business transaction.

(7) Causing billing information to be submitted for payment, directly or indirectly, without the express informed consent of the customer.

e) A pattern of telephone calls. The following are defined as abusive telemarketing acts or practices when engaged in by a telemarketer.

(1) Causing the phone to ring repeatedly and continuously with intent to annoy, abuse, or harass any person at the called number.

(2) Denying or interfering in any way with a person's right to be placed on the "do-not-call" registry.

(3) Initiating a call when that person's telephone number is on the "do-not-call" registry maintained by the FTC. (Number remains on the "do-not-call" registry for 5 years (renewable); unless the seller:

(a) Has obtained an express agreement in writing with the person authorizing calls to that person; or

(b) Has an established business relationship (within 18 months of last purchase or 3 months of

inquiry) with that person and they have not said they do not want to receive calls under another section of the rule.

(4) Initiating a call with a person who has previously stated that he or she does not wish to receive calls made by or on behalf of the seller whose goods or services are being offered or on behalf of a charitable organization. EXCEPT, seller or telemarketer is not liable IF:

(a) It has established and implemented WRITTEN procedures to comply with this rule;

(b) It has trained its personnel on these procedures;

(c) The seller or telemarketer maintains a list of those who may not be called; AND

(d) The subsequent call is a result of error.

(5) Abandoning an outbound telephone call. If a person answers it and the telemarketer does not connect the call to sales rep in two seconds or promptly plays a recorded message that states the number and name of the seller on whose behalf the call was placed

f) Calling time restrictions. It is an abusive telemarketing act or practice for telemarketers a call a consumer earlier than 8:00 a.m. or later than 9:00 p.m. at the called person's location UNLESS the person consents to such calls.

g) Required oral disclosures in the sale of goods or services. It is an abusive telemarketing act or practice for a telemarketer to fail to make the following oral disclosures:

(1) The identity of the seller;

(2) That the purpose of the call is to sell goods and services;

(3) The nature of the goods and services; AND

(4) That no purchase or payment is necessary to be able to win a prize or participate in a prize promotion if a prize promotion is offered.

(5) In a charitable solicitation, the identity of the charitable organization and the fact that the purpose of the call is to solicit a charitable contribution.

3. Record Keeping Requirements:

a) Seller or telemarketer must keep for 24 months:

(1) All substantially different advertising, brochures, telemarketing scripts, and promotional materials;

(2) The name and last known address of each prize recipient and the prize awarded for all prizes represented to have a value of $25 or more.

(3) The name and address of each customer who purchases goods, the date the goods were shipped, and the amount paid.

(4) The names and addresses of all current and former employees directly involved in telephone sales.

(5) All verifiable authorizations (for cashing checks, etc.) required by the rule.

b) Records may be kept in any form that the seller or telemarketer keeps similar records in the ordinary course of its business and if change ownership successor must maintain records.

4. Key Definitions.

a) MATERIAL means likely to affect a person's choice of, or conduct regarding, goods or services.

b) CUSTOMER means any person who is or may be required to pay for goods or services offered through telemarketing.

c) DONOR means any person solicited to make a charitable contribution.

d) ESTABLISHED BUSINESS RELATIONSHIP means a relationship between seller and consumer based on:

(1) The consumer's purchases, rental, or lease of the seller's goods or services or a financial transaction between the consumer or seller within the eighteen months immediately proceeding the date of the telemarketing call; or

(2) The consumer's inquiry or application regarding a product or service offered by the seller within the three months immediately proceeding the date of the telemarketing call.

e) SELLER means any person who, in connection with a telemarketing transaction, provides, offers to provide, or arranges for others to provide goods or services to the customer in exchange for consideration.

f) TELEMARKETER means any person who, in connection with telemarketing, initiates or receives telephone calls to or from the customer.

5. Scope.

a) Telemarketing is defined as any plan, program or campaign which is conducted to induce the purchase of goods or services by use of one or more telephones and which involves more than one interstate telephone call.

b) Specifically excluded are:

(1) Catalog sales where

(a) The catalog:

(i) Contains written description or illustration of goods;

(ii) Gives the business address of seller;

(iii) Contains multiple pages of written material and illustrations; and

(iv) Is issued at least once per year.

(b) AND the seller only RECEIVES calls initiated by consumer to take orders without further solicitation.

(2) Sale of pay-per-call services (already regulated under 16 C.F.R Part 308).

(3) Sale of franchises (already regulated under 16 C.F.R. Part 436).

(4) Calls where the sale is not complete until after a face-to-face presentation by the seller.

(5) Calls initiated by consumer:

(a) Without any solicitation on the part of the seller;

(b) In response to an advertisement through any media or, EXCEPT:

(i) investment opportunities

(ii) Services to remove derogatory credit information

(iii) Services to assist in the return of money or value for previous telemarketing transactions

(iv) Ads that promise a high degree of success in obtaining or arranging extensions of credit.

(6) In response to a direct mail solicitation that clearly, conspicuously, and truthfully discloses all material information required by the Rule except for solicitations for investment opportunities, prize promotions, and business opportunities other than business arrangements covered by franchise rule.

(7) Calls between a telemarketer and any business (except for the sale of nondurable office or cleaning supplies).

(8) Businesses not covered under the Rule.

(a) Banks, federal credit unions, and federal savings and loans.

(b) Common carriers (long distance telephone companies and airlines).

(c) Non-profit organizations.

(9) Charities are not required to comply with "Do Not Call" registry, however you can tell them individually not to call and they must stop.

6. Enforcement of the Rule.

a) Violation of the Rule is an unfair and deceptive act or practice under 15 U.S.C. § 57a.

b) Any state officer can bring an action on behalf of consumers.

c) Actual damages or up to $500 statutory damages are available for violations of the "no call" provision or for calls at inconvenient times under the Telephone Consumer Protection Act. The consumer need not prove any monetary loss or actual damages to recover under the Telephone Consumer Protection Act.

d) Prior to initiating an action (if feasible), notice is to be given to the FTC.

e) If a telemarketer violates the "do not call" registry, they can be fined up to $11,000 per violation.

7. Interrelationship with Other Protections. As with all consumer cases, attorneys must look to all available protections to protect the consumer's interests. Here are two protections related to telemarketing that a consumer might be able to assert.

a) Fair Credit Billing Act (FCBA)

(1) If the consumer purchases goods from a telemarketer using a credit card, consider the claims and defenses protections under the FCBA. (15 U.S.C. § 1666i)

(2) Basic Requirements (For more detail, see Chapter 5).

(a) Claims and defenses may include a dispute as to quality of merchandise and nondelivery of goods.

(b) A consumer has right to assert against card issuer claims or defenses concerning property or services purchased with credit card, if:

(i) The consumer has made a good faith effort to resolve the problem with the merchant honoring the card;

(ii) The amount of the initial transaction exceeds $50;

(iii) The initial transaction was in the same state as the cardholder's designated address or within 100 miles of such address; and

(iv) Location of transaction is matter of state law; states differ on whether mail or telephone order occurred at consumer's home or seller's place of business.

(c) In a telemarketing case, the consumer's position is that the transaction took place in her home

state because the telemarketer conducted the solicitation there. You, as the attorney should anticipate an argument from the telemarketer.

(d) The merchant is not controlled by or the same as the card issuer (e.g. Sears or J.C. Penney - store card).

8. The FTC Mail or Telephone Order Merchandise Rule. (See below). This rule requires delivery of goods ordered over the phone within 30 days.

III. THE MAIL OR TELEPHONE ORDER MERCHANDISE RULE

A. Reference.

1. 16 C.F.R. Part 435.

2. National Consumer Law Center, Unfair and Deceptive Acts and Practices, §5.9 (6th ed. 2004).

B. Requirements of the Rule (16 C.F.R. § 435.1).

1. TIMELY SHIPMENT. It is an unfair and deceptive act or practice for a seller to solicit any order for the sale of merchandise to be ordered by the buyer through the mails or by telephone unless, at the time of the solicitation, the seller has a reasonable basis to expect that it will be able to ship any ordered merchandise to the buyer:

a) Within that time clearly and conspicuously stated in any such solicitation, OR

b) If no time is clearly and conspicuously stated, within thirty (30) days after receipt of a properly completed order from the buyer.[1]

(1) The seller cannot extend the delivery deadline by counting thirty days as running from later date such as when the seller charges credit card.

[1] Note that if the seller applies for credit at the time of the sale, the seller has 50 days to ship the merchandise.

(2) The seller does not comply by sending all part of the merchandise- for example – software for the computer purchased.

2. Seller's duty to maintain systematic records. Failure of the merchant-seller to have records or other documentary proof establishing its use of systems and procedures which assure the shipment of merchandise in the ordinary course of business within the time period required above will create a rebuttable presumption that the seller lacked a reasonable basis for any expectation of shipment within that time.

3. Buyer's option to cancel. Where a seller is unable to ship merchandise within the time set forth above, the seller must:

a) Offer to the buyer, clearly and conspicuously and without prior demand, an option either to consent to a delay in shipping; or to cancel the buyer's order and receive a prompt refund.

b) The offer must be made within a reasonable time after the seller first becomes aware of its inability to ship within the time limit, but in no case later than end of the time limit.

c) Any offer to the buyer of such an option shall fully inform the buyer about the buyer's right to cancel the order and to obtain a prompt refund and shall provide either a definite revised shipping date, or notice that the seller is unable to make any representation regarding the length of the delay.

d) If the revised shipping date is 30 days or less AFTER the applicable time limit expires, the buyer is deemed to have consented to the delay if:[2]

(1) Seller does not receive, prior to shipment and prior to the expiration of the definite revised shipping date, a response from the buyer rejecting the delay and canceling the order, AND

(2) The merchandise arrives on or before the revised shipping date.

[2] Seller must EXPRESSLY inform buyer of this provision in its notice regarding the revised shipping date.

e) If the definite revised shipping date is more than thirty (30) days AFTER the applicable time limit expires, the buyer is automatically deemed to have CANCELED UNLESS[3]

(1) The seller ships the merchandise within thirty (30) days of the expiration of the applicable time limit (and has not received an affirmative cancellation before shipping) OR

(2) The seller has received from the buyer within thirty (30) days of the applicable time limit a response specifically consenting to the shipping delay.

f) The seller may solicit buyer's consent to further unanticipated delay.

4. Exercising the option to cancel. The seller must:

a) Furnish the buyer with adequate means to exercise the option and notify the seller regarding cancellation.

b) Return of the merchandise is at the seller's expense.

5. Seller's duty to honor cancellation. The seller must deem an order canceled and make a prompt refund to the buyer whenever the seller receives, prior to the time of shipment, notification from the buyer canceling the order pursuant to any option described above.

C. Definitions. (16 C.F.R. § 435.2)

1. "Mail or telephone order sales:" sales in which the buyer has ordered merchandise from the seller by mail or telephone, regardless of the method of payment or the method used to solicit the order.

2. "Telephone:" refers to any direct or indirect use of the telephone to order merchandise, regardless of whether the telephone is activated by, or the language used is that of human beings, machines, or both.

3. "Shipment:" the act by which the merchandise is physically placed in the possession of the carrier.

[3] Seller must EXPRESSLY inform buyer of this provision in its notice regarding the revised shipping date.

4. "Receipt of a properly completed order:"

   a) Where the buyer tenders full or partial payment in the proper amount in the form of cash, check, money order, or authorization from the buyer to charge an existing charge account, THEN

   b) The time at which the seller receives both said payment and an order from the buyer containing all of the information needed by the seller to process and ship the order.

   c) However, if the seller receives notice that the check or money order tendered by the buyer has been dishonored or that the buyer does not qualify for a credit sale, "receipt of a properly completed order" means the time at which:

      (1) The seller receives notice that a check or money order for the proper amount tendered by the buyer has been honored,

      (2) The buyer tenders cash in the proper amount, OR

      (3) The seller receives notice that the buyer qualifies for a credit sale.

   d) Refund.

      (1) RULE 1: Cash Sales/Goods not Shipped

         (a) the buyer tendered full or partial payment in the form of cash, check or money order, AND

         (b) the merchandise has not been shipped.

         (c) Refund = a return of the amount tendered in the form of cash, check or money order.

      (2) RULE 2. Credit Sales

         (a) There is a credit sale, AND

         (b) The seller is a creditor.

(c) Refund = a copy of a credit memorandum or the like or an account statement reflecting the removal or absence of any remaining charge incurred as a result of the sale from the buyer's account.

(3) RULE 3: Credit Sales/Third Party Creditor

(a) There is a credit sale, AND

(b) A third party is the creditor.

(c) Refund = a copy of an appropriate credit memorandum or the like to the third party creditor which will remove the charge from the buyer's account OR a statement from the seller acknowledging the cancellation of the order and representing that it has not taken any action regarding the order which will result in a charge to the buyer's account with the third party.

(4) "Prompt refund" shall mean:

(a) Cash, Check, or Money Order: refund sent by first class mail within 7 working days of the date on which the buyer's right to refund vests.

(b) Credit Sale: a refund sent to the buyer by first class mail within one (1) billing cycle from the date on which the buyer's right to refund vests.

(5) The "time of solicitation" of an order shall mean that time when the seller has:

(a) Mailed or otherwise disseminated the solicitation to a prospective purchaser,

(b) Made arrangements for an advertisement containing the solicitation to appear in a newspaper, magazine or the like or on radio or television which cannot be changed or canceled without incurring substantial expense, or

(c) Made arrangements for the printing of a catalog, brochure or the like which cannot be changed without incurring substantial expense, in which the solicitation in question forms an insubstantial part.

(6) Failure to refund shipping and handling charges is a UDAP. See United States v. Lillian Vernon Corp., 5 Trade Reg. Rep (CCH) 23,270 (S.D.N.Y. 1992).

D. Exclusions. (16 C.F.R. § 453.3). The following are excluded from the Mail or Telephone Order Merchandise Rule:

1. Subscriptions, such as magazine sales, ordered for serial delivery, after the initial shipment is made in compliance with this part.

2. Orders of seeds and growing plants.

3. Orders made on a collect-on-delivery (C.O.D.) basis.

4. Transactions governed by the Federal Trade Commission's Trade Regulation Rule entitled "Use of Negative Option Plans by Sellers in Commerce," 16 C.F.R. part 425.

E. Relationship to Other Laws/Rules

1. The FTC does not intend to preempt action in the same area, which is not inconsistent with this part, by any State, municipal, or other local government. GA and ID have incorporated the FTC statute into their UDAP regulations. Numerous states have similar rules.

2. The Rule does not annul or diminish any rights or remedies provided to consumers by any State law, municipal ordinance, or other local regulation, insofar as those rights or remedies are equal to or greater than those provided by this part.

3. The Rule does not supersede those provisions of any State law, municipal ordinance, or other local regulation, which impose obligations or liabilities upon sellers, when sellers subject to this part are not in compliance therewith.

4. The Rule supersedes those provisions of any State law, municipal ordinance, or other local regulation, which are inconsistent with this

part to the extent that those provisions do not provide a buyer with rights, which are equal to or greater than those rights granted a buyer by this part.

F. Internet fraud.

1. The Mail or Telephone Merchandise rule is broad enough to cover Internet fraud when the problem is failure to deliver, or delay in delivering merchandise. See FTC, Dot Com Disclosure § 14(A)(2) (2000)) providing guidance on how on-line sellers should comply with the Mail or Telephone Order Merchandise Rule. The FTC can proceed against deceptive on-line services under its general authority.

2. Examples of businesses subject to Internet fraud include:

a) Credit repair services,

b) Miracle cures and weight loss products,

c) Pyramid schemes,

d) Off-site betting,

e) Bogus income opportunities ,

f) Internet got consumer to download a program that hijacked the user's computer modem so that all calls were routed through Moldova at a great expense to the consumer. The operator of the scheme got part of the revenue generated by the scheme through the international operator.

g) Billing consumers for "free" website services or for unauthorized purchases by asking consumer to provide credit card number just to prove they were eighteen. For example an adult website which advertised it was for free and then charged the credit card number used to prove the consumer was eighteen was required to pay $30 million to settle a suit brought by the FTC and New York Attorney General. See FTC v. Crescent Publishing Group, Inc. (S.D.N.Y. filed 2001) at www.ftc.gov/os/2001/11/crescentstip.pdf (stipulated final judgment and order).

G. Enforcement Provisions.

1. No Private Cause of Action under the Federal Rule.

2. Federal Trade Commission.

3. Look to State UDAP statutes. These may provide a private cause of action.

IV. UNORDERED MERCHANDISE

A. Reference.

1. 39 U.S.C. § 3009 (2000).

2. National Consumer Law Center, Unfair and Deceptive Acts and Practices, § 5.8.4 (6th ed. 2004).

B. General.

1. Consumers unsure of their legal rights found it inconvenient to send back items and are scared of debt collection threats. In the past, sellers have threaten to turn over accounts to a debt collection agency or report the delinquency to a credit reporting agency.

2. Federal law prohibits use of the mails to send unordered merchandise, except for free gifts and merchandise mailed by a charitable organization soliciting contributions. 18 U.S.C. § 3009.

3. Merchants mailing free samples to consumers must clearly and conspicuously mark the sample as such, and provide notice that the consumer may treat the unsolicited merchandise as a gift.

4. "Unordered merchandise" is merchandise mailed without the prior expressed request or consent of the recipient.

5. Violations of this rule constitute an unfair method of competition and an unfair trade practice in violation of the FTC act.

6. Consumers may generally bring an action under the state UDAP statute or federal law.

a) Example. It is a UDAP violation to send a document that looks like an invoice as part of an offer of services attempting to imply services were ordered.

b) Example. It is a UDAP violation to deliver and bill the consumer for more than the consumer ordered.

C. Schemes invoking unordered goods.

1. A seller promised free gifts to business employees in order to get their names on invoices for unordered merchandise as a means of leading the company to believe the merchandise had been properly ordered.

2. Consumers were induced to call a 900 number to claim a packages being held after failed attempts of delivery. The packages contained unordered merchandise and were not being held by postal carrier.

3. Representation that they were customer's normal supplier, shipped unordered merchandise, sent bills and used a fictitious law firm's name to collect the debts.

4. Company sent past due and renewal invoices to organizations including churches for unordered computer service contracts and then rarely performed the services.

D. Negative Option Plans – book of the month club is an example. FTC requires sellers to disclose plan terms, including the negative option, minimum purchase requirements, postage charges, and refusal rights. Membership must be canceled upon request once minimum order has been met. The seller must give the consumer written notice of the nature of the goods before arrival, including a form allowing the consumer to reject the selection.

V. TELEPHONE DISCLOSURE AND DISPUTE RESOLUTION ACT (900 NUMBERS)

A. Reference.

1. Telephone Disclosure and Dispute Resolution Act of 1992, 15 U.S.C. § 5711.

2. Telephone Disclosure and Dispute Resolution Rule, 16 C.F.R. § 308.

3. National Consumer Law Center, Unfair and Deceptive Acts and Practices, § 5.9.8 (6th ed. 2004).

B. The Telephone Disclosure and Dispute Resolution Act of 1992 regulates the use of 900 numbers on the federal level and is enforceable by the FTC.

1. This rule prohibits common carriers form disconnecting a subscriber's local or long distance service because of unpaid 900 number charges.

2. Consumers whose telephone bills include fraudulent 900 number charges should be advised to refuse to pay.

3. Carriers are required to itemize 900 number charges on the bill separately to alert consumers of the charges.

4. Carriers must establish procedures to handle customer complaints about 900 number charges but have discretion about the standards used for forgiving charges. Carriers must forgive the debt if the FTC, the FCC, or a court finds that the 900-number service violates federal law.

5. If feasible, telephone companies should offer the option of blocking access from their telephone to 900 numbers.

6. Businesses must make disclosures regarding costs and chance of winning prizes at the beginning of the call and must allow the consumer to hang up with no charge after the introductory disclosures. They must also disclose an alternate free way to enter contests for prizes.

7. Businesses cannot direct advertisement to children under 12 except for bona fide education products. Advertisements directed to children under eighteen are allowed but must include a warning to get parental permission.

8. Providers cannot switch consumers from 800 numbers to 900 numbers, nor from an 800 number to a collect call.

C. Telephone companies must require their subscribers to comply with the statute and must terminate subscribers that violate the statute.

VI. CONSUMER LEASING ACT (CLA).

A. References.

1. Chapter 5 of the Truth in Lending Act, 15 U.S.C. § 1667a-f (2000).

2. Regulation M, 12 C.F.R. Part 213.

3. National Consumer Law Center, Truth in Lending Chapter 9 (4th ed. 1999 and 2002 Supp.).

B. Purpose.

1. To ensure that lessees of personal property receive meaningful disclosures that enable them to compare lease terms with other leases and, where appropriate, with credit transactions;

2. To limit the amount of balloon payments in consumer lease transactions; and

3. To provide for the accurate disclosure of lease terms in advertising.

C. Key Definitions (12 C.F.R. § 213.2)

1. "Open-end lease" means a consumer lease in which the lessee's liability at the end of the lease term is based on the difference between the residual value of the leased property and its realized value.

2. "Closed-end lease" means a consumer lease other than an open-end lease as defined in this section. As a practical matter, closed-end leases are the most common ones you'll see. According to the Federal Trade Commission, "[w]ith a closed-end lease, you may return the vehicle at the end of the lease term, pay any end-of-lease costs, and walk away." Keys to Vehicle Leasing, available at http://www.ftc.gov/bcp/conline/pubs/autos/leasing/index.htm (visited 5 May 2000).

3. "Realized value" means:

a) The price received by the lessor for the leased property at disposition;

b) The highest offer for disposition of the leased property; or

c) The fair market value of the leased property at the end of the lease term.

4. "Residual value" means the value of the leased property at the end of the lease term, as estimated or assigned at consummation by the lessor, used in calculating the base periodic payment.

D. Scope

1. Requirement 1: A "consumer lease". These are contracts in the form of a bailment or lease for the use of personal property

2. By a natural person

3. Primarily for personal, family, or household purposes, – Consumer's submission of documentary evidence not rebutted by lessor is sufficient to prove lease for consumer purposes. See Clement v. American Honda Finance Corp., 145 F. Supp. 2d 206 (D. Conn. 2001).

4. For a period exceeding four months, and

a) Rent-to-Own appliance leases that can be terminated at any time without penalty have been held to NOT meet this requirement. Thus, the Act would not apply to them. See Annotation, Construction And Application Of Consumer Leasing Act (15 U.S.C.A. SS 1667- 1667E), 129 A.L.R. Fed. 587, §3a. (1996).

b) However, if there is a penalty to terminate, the Act has been held to apply. See Official Staff Commentary, § 213.2(e)-2(ii).

5. For a total contractual obligation **not exceeding $25,000.**

a) Total Contractual Obligation is not defined in the statute or rule.

b) A provision in the Official Staff Commentary, however, indicates that the total contractual obligation is not necessarily the same as the total of payments disclosed under §213.4(e). The total contractual obligation includes nonrefundable amounts a lessee is contractually obligated to pay to the lessor, but excludes items such as:

(1) Residual value amounts or purchase-option prices;

(2) Amounts collected by the lessor but paid to a third party, such as taxes, license and registration fees.

(3) This requirement exempts many automobile leases from the Act. STATE LAW may help here.

c) The applicability of the Act does NOT depend on whether or not the lessee has the option to purchase or otherwise become the owner of the property at the expiration of the lease.

6. Requirement 2: A "lessor" makes the lease. This is:

a) A person who regularly leases, offers to lease, or arranges for the lease of personal property under a consumer lease.

b) A person who has leased, offered, or arranged to lease personal property more than five times in the preceding calendar year or in the current calendar year is subject to the act

E. Exclusions.

1. The Act does NOT apply to "credit sales" under Regulation Z (12 CFR 226.2(a)).

2. It also does not apply to leases for agricultural, business, or commercial purposes or a lease made to an organization.

3. The Act does not apply to a lease transaction of personal property which is incident to the lease of real property and which provides that:

a) The lessee has no liability for the value of the personal property at the end of the lease term except for abnormal wear and tear; and

b) The lessee has no option to purchase the leased property.

F. Requirements of the Act.

1. Disclosures. Regulation M (12 C.F.R., Part 213) substantially changes disclosures under the Act.

a) Form of Disclosures (12 C.F.R. § 213.3)

(1) The disclosures shall be made

(a) clearly and conspicuously,

(b) in writing,

(c) the CLA requirement that disclosures be made in writing is overridden only of the lessor companies with the requirements of the Electronic Signatures in Global and National Commerce Act, effective October 1, 2000, which was enacted to validate electronic signatures, documents and disclosures. . If the lessor did not comply then the consumer should be entitled to the standard CLA penalties. The lessor's use of electronic disclosures may also be relevant to a fraud claim if the consumer can show that it was part of a scheme to dupe the consumer to enter into a highly disadvantageous transaction.

(d) in a form the consumer may keep.

2. The writing must

a) be dated

b) identify the lessor and the lessee.

c) Disclosures may be made:

(1) in the contract or other document evidencing the lease.

(2) in a separate statement that identifies the consumer lease transaction.

(3) Disclosures required to be segregated may be provided in a separate dated statement that identifies the lease, and the other required disclosures may be provided in the lease contract or other document evidencing the lease.

3. Timing of disclosures. A lessor shall provide the disclosures to the lessee prior to the consummation of a consumer lease. A dealer violates the CLA if the dealers provides a vehicle to consumer contingent on financing coming through, then later cancel the contract and rewrite it at some later time as a lease on terms less favorable to the consumer then back dates that lease to when the consumer received the vehicle. See Jafri v. Lynch Ford, Clearinghouse No. 53,536 9 N.D. Ill. Aug. 25, 2000).

a) Minor variations. A lessor may disregard the effects of the following in making disclosures:

(1) That payments must be collected in whole cents;

(2) That dates of scheduled payments may be different because a scheduled date is not a business day;

(3) That months have different numbers of days; and

(4) That February 29 occurs in a leap year.

4. Content of disclosures. 12 C.F.R. § 213.4. For any consumer lease subject to this part, the lessor shall disclose the following information, as applicable.

a) Segregation of certain disclosures. The following disclosures shall be segregated from other information and shall contain only directly related information. The disclosures shall be provided in a manner substantially similar to the applicable model form in appendix A to Regulation M (The Federal Box). (2) §§213.4(b) through (f), (g)(2), (h)(3), (i)(1), (j), and (m)(1).

b) Amount due at lease signing. The total amount to be paid prior to or at consummation, using the term "amount due at lease

signing." The lessor shall itemize each component by type and amount. Where a disclosure required the consumer to pay $1,582, the CLA has been violated where the lessor instead promised to pay this amount for the consumer, and does pay the amount. . See Patterson v. Bob Wade Lincoln-Mercury, Inc., 55 VA. Cir. 499, 2000 Va. Cir. LEXIS 619 (2000). But see Dauti v. Hartford Auto Plaza, Ltd., 2002 WL 1727916 (D. Conn. June 4, 2002) (no violation where dealer agreed to accept $3000 instead of the disclosed $3045.15).

c) Payment schedule and total amount of periodic payments. The number, amount, and due dates or periods of payments scheduled under the lease, and the total amount of the periodic payments.

d) Other charges. The total amount of other charges payable to the lessor, itemized by type and amount that are not included in the periodic payments.

(1) Total of payments. The total of payments, with a description such as "the amount you will have paid by the end of the lease." This amount is the sum of the amount due at lease signing (less any refundable amounts), the total amount of periodic payments (less any portion of the periodic payment paid at lease signing), and other charges. In an open-end lease, a description such as "you will owe an additional amount if the actual value of the vehicle is less than the residual value" shall accompany the disclosure.

(2) Payment calculation. In a motor-vehicle lease, a mathematical progression of how the scheduled periodic payment is derived. The calculation must show the following 11 steps:

(a) Gross capitalized cost. If requested by the lessee, an itemization shall be provided before consummation.

(b) Capitalized cost reduction. “The amount of any net trade-in allowance, rebate, noncash credit, or cash you pay that reduces the gross capitalized cost.”

(c) Adjusted capitalized cost.

(d) Residual value The value the lessor claims the car will be worth at the end of the lease.

(e) Depreciation and any amortized amounts. The difference between the adjusted capitalized cost and the residual value.

(f) Rent charge. This is the difference between the total of the base periodic payments over the lease term minus the depreciation and any amortized amounts.

(g) Total of base periodic payments.

(h) Lease term.

(i) Base periodic payment.

(j) Itemization of other charges. An itemization of any other charges that are part of the periodic payment.

(k) Total periodic payment. The sum of the base periodic payment and any other charges that are part of the periodic payment.

(3) Early-termination notice. In a motor-vehicle lease, a notice substantially similar to the following: "Early Termination. You may have to pay a substantial charge if you end this lease early. The charge may be up to several thousand dollars. The actual charge will depend on when the lease is terminated. The earlier you end the lease, the greater this charge is likely to be." The CLA requires the disclosure to be “clear” and the term clear means more than just legible, but must also include the ability to understand the formula in the disclosure. See *Applebaum v. Nissan Motor Acceptance Corp*., 2000 U.S. Dist. LEXIS 15645 (E.D. Pa. Oct. 27, 2000).

(4) Notice of wear and use standard. In a motor-vehicle lease, a notice regarding wear and use substantially similar to the following: "Excessive Wear and Use. You may be charged for excessive wear based on our standards for normal use." The notice shall also specify the amount or method for determining any charge for excess mileage.

(5) Purchase Option at End of lease term. Notice of the purchase price and when the lessee may exercise this option.

(6) Statement referencing non-segregated disclosures. A statement that the lessee should refer to the lease documents for additional information on early termination, purchase options and maintenance responsibilities, warranties, late and default charges, insurance, and any security interests, if applicable.

(7) Rent and other charges. The rent and other charges paid by the lessee and required by the lessor as an incident to the lease transaction, with a description such as "the total amount of rent and other charges imposed in connection with your lease [state the amount]."

e) Other (Non-segregated) Disclosures

(1) Description of property. A brief description of the leased property sufficient to identify the property to the lessee and lessor.

(2) Conditions and disclosure of charges for early termination. A statement of the conditions under which the lessee or lessor may terminate the lease prior to the end of the lease term; and the amount or a description of the method for determining the amount of any penalty or other charge for early termination, which must be reasonable.

(3) Maintenance responsibilities. The following provisions are required:

(a) Statement of responsibilities. A statement specifying whether the lessor or the lessee is

responsible for maintaining or servicing the leased property, together with a brief description of the responsibility;

(b) Wear and use standard. A statement of the lessor's standards for wear and use (if any), which must be reasonable

(4) Purchase option during the lease term. A statement of whether or not the lessee has the option to purchase the leased property and, if prior to the end of the lease term, the purchase price or the method for determining the price and when the lessee may exercise this option.

(5) Liability between residual and realized values. A statement of the lessee's liability, if any, at early termination or at the end of the lease term for the difference between the residual value of the leased property and its realized value.

(a) The lessor has a duty to mitigate damages and must use reasonable diligence in selling the vehicle. A court can use UCC Article 9 to determine commercial reasonableness.

(b) If formula fails to provide credit for realized value, the form aula is unreasonable. See *Atel Financial Corp v. Quaker Coal Co*., 132 F. supp. 2d 1233 (N.D. Cal. 2001).

(c) Dealers systematically inflate the residual value and then in default use the realized value (how much they got at a car auction) to determine the default charge. Federal courts have stated that this is unreasonable. This shows how arbitrary it is for lessors forcing the risk of a low sale price on consumers at early determination or default, while bearing that risk at scheduled termination. For example a consumer turns in a vehicle at the end of the lease period, having missed some early lease payments. Under a default formula the consumer would pay $6,600 for the difference between the residual value and the realized value, while if not in default

would only owe $500 for the payments he missed in the lease.

(6) Right of appraisal. If the lessee's liability at early termination or at the end of the lease term is based on the realized value of the leased property, a statement that the lessee may obtain, at the lessee's expense, a professional appraisal by an independent third party. The third party must be agreed to by the lessee and the lessor and will estimate the value that could be realized at sale of the leased property. The appraisal shall be final and binding on the parties. Practice tip: identify the appraiser at the beginning of the transaction.

(7) Liability at end of lease term based on residual value.

(8) Fees and taxes. The total dollar amount for all official and license fees, registration, title, or taxes required to be paid to the lessor in connection with the lease.

(9) Insurance. A brief identification of insurance in connection with the lease including:

(a) Voluntary insurance. If the insurance is provided by or paid through the lessor, the types and amounts of coverage and the cost to the lessee; or

(b) Required insurance. If the lessee must obtain the insurance, the types and amounts of coverage required of the lessee.

(10) Warranties or guarantees. A statement identifying all express warranties and guarantees from the manufacturer or lessor with respect to the leased property that apply to the lessee.

(11) Penalties and other charges for delinquency. The amount or the method of determining the amount of any penalty or other charge for delinquency, default, or late payments, which must be reasonable.

(12) Security interest. A description of any security interest held or to be retained by the lessor; and a clear identification of the property to which the security interest relates.

G. Limits on Advertisement (12 C.F.R. § 213.7)

1. General rule. An advertisement for a consumer lease may state that a specific lease of property at specific amounts or terms is available only if the lessor usually and customarily leases or will lease the property at those amounts or terms. The FTC has brought actions against dealerships alleging that advertising disclosures were in too fine of print, were inadequately conspicuous and the proper disclosures were not given.

2. Clear and conspicuous standard. Disclosures required by this section shall be made clearly and conspicuously.

a) Amount due at lease signing. Any affirmative or negative reference to a charge that is a part of the total amount due at lease signing shall not be more prominent than the disclosure of the total amount due at lease signing.

b) Advertisement of a lease rate. If a lessor provides a percentage rate in an advertisement, the rate shall not be more prominent than any of the disclosures required to accompany the rate; and the lessor shall not use the term "annual percentage rate," "annual lease rate," or equivalent term.

c) Advertisement of terms that require additional disclosure.

(1) Triggering terms. An advertisement that states any of the following items shall contain the disclosures required by paragraph (2):

(a) The amount of any payment;

(b) The number of required payments; or

(c) A statement of any capitalized cost reduction or other payment required prior to or at consummation, or that no payment is required.

(2) Additional terms. An advertisement stating any item listed in paragraph (1) shall also state the following items:

(a) That the transaction advertised is a lease;

(b) The total amount due at lease signing, or that no payment is required;

(c) The number, amounts, due dates or periods of scheduled payments, and total of such payments under the lease;

(d) A statement of whether or not the lessee has the option to purchase the leased property, and where the lessee has the option to purchase at the end of the lease term, the purchase-option price;

(e) A statement of the amount, or the method for determining the amount, of the lessee's liability (if any) at the end of the lease term; and

(f) A statement of the lessee's liability (if any) for the difference between the residual value of the leased property and its realized value at the end of the lease term.

(3) Alternative disclosures -- merchandise tags. A merchandise tag stating any item listed in paragraph (1) may comply with paragraph (2) by referring to a sign or display prominently posted in the lessor's place of business that contains a table or schedule of the required disclosures.

(4) Alternative disclosures -- television or radio advertisements.

(a) Toll-free number or print advertisement. An advertisement made through television or radio stating any item listed in paragraph (1) complies with paragraph (2) if the advertisement states the items listed in paragraphs (2)(a) - (c), and:

(i) Lists a toll-free telephone number along with a reference that such number may be used by consumers to obtain the other information required; or

(ii) Directs the consumer to a written advertisement in a publication of general circulation in the community served by the media station, including the name and the date of the publication, with a statement that information required by paragraph (2) is included in the advertisement. The written advertisement shall be published beginning at least three days before and ending at least ten days after the broadcast.

(b) Establishment of toll-free number.

(i) The toll-free telephone number shall be available for no fewer than ten days, beginning on the date of the broadcast.

(ii) The lessor shall provide the information required by paragraph (d)(2) of this section orally, or in writing upon request.

H. State Leasing Disclosure Statutes. The following states have leasing disclosure statutes that may provide additional protections:

1.	Arkansas	1999 Ark. Acts § 1059
2.	California	Cal. Civil Code § 2985.8
3.	Colorado	Colo. Rev. Stat. §§ 5-2-311 – 13
4.	Connecticut	Conn. Gen. Stat. §§ 36a-675 - 85 for additional protections see 2002 Conn. Legis. Serv. P.A. 02-81 (S.H.B.) (effective July 1, 2003).
5.	D. C.	D.C. Code Ann. § 28-3810
6.	Florida	Fla. Stat. § 521
7.	Hawaii	Haw. Rev. Stat. § 481L

8.	Illinois	815 Ill. Comp. Stat. Ann. § 636
9.	Indiana	Ind. Code §§ 9-23-2.5-1/24-4.5-2-101
10.	Iowa	Iowa Code § 537.1101
11.	Kansas	Kan. Stat. Ann. § 16a-1-101
12.	Louisiana	La. Rev. Code § 9:3301
13.	Maine	Me. Rev. Stat. Ann. Tit. 9-A § 5-101
14.	Maryland	Md. Code Ann. Com. Law § 14-2001
15.	Michigan	Mich. Comp. Laws § 445.991
16.	New Hampshire	N.H. Rev. Stat. Ann. Ch. 361-D
17.	New Jersey	N.J. Rev. Stat. § 56:12-60
18.	New York	N.Y. Pers. Prop. Law § 331
19.	Oklahoma	Okla. Stat. Ann. Tit. 14A § 1-101
20.	South Carolina	S.C. Code Ann. § 37-1-101
21.	Washington	Wash. Rev. Code § 63.10.010
22.	West Virginia	W.Va. Code § 46A-1-104
23.	Wisconsin	Wis. Stat. § 429-101

I. Taking Leased Vehicles Overseas.

1. The SCRA provides for the termination of auto leases. See Pub. L. No.108-189, § 305, formerly cited as 50 U.S.C. App. § 535.

a) A lease for a military service member or a servicemembers' dependents for personal or business use may be terminated if:

(1) During the term of the lease the servicemember enters military service for a term not under 180 days or gets extended to a period of not under 180 days.

(2) While in military service, executes lease and then receives military orders for a permanent change of station outside the continental United States or deploys with military unit for a period of not less than 180 days.

b) Termination of the lease is made by.

(1) Return of the motor vehicle to the lessor or their agent, not later than 15 days after delivery of written notice.

(2) The written notice can be any time after the lessee's entry into military service of the date of the lessee's military orders.

VII. CONCLUSION.

CHAPTER 4

PROTECTIONS BASED UPON PROBLEMS WITH THE GOODS

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CHAPTER 4

PROTECTIONS BASED UPON PROBLEMS WITH THE GOODS

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B. Magnuson-Moss Warranty - Federal Trade Commission Improvement Act, 15 U.S.C. §§ 2301-12 (2000).

C. 16 C.F.R. Subchapter G - Rules, Regulations, Statements, and Interpretations Under the Magnuson-Moss Warranty Act (Parts 700-03).

D. National Consumer Law Center, Consumer Warranty Law (3d ed. 2006 & Supp. 2008).

II. INTRODUCTION.

A. Consumer warranty law focuses on the rights of the consumer where personal property has been purchased or leased and it does not live up to the consumer's expectations.

B. Most of us make purchases today with at least the belief that the seller is going to stand behind the product. If nothing else, consumers can resort to the concept of offer and acceptance and hope that what they actually receive is what they bargained for in the first instance.

C. In this chapter we will cover, Article 2 of the Uniform Commercial Code (UCC), the Magnuson-Moss Warranty Act, state Lemon Laws, the FTC Used Car Rule, and used car Lemon Laws.

III. THE UNIFORM COMMERCIAL CODE, ARTICLE 2 (SALES)

A. The basic premise is that the warranty is part of the basis of the bargain between seller and consumer. The buyer agrees to limit his or her ability to revoke acceptance under the UCC in return for the promise by the seller to repair or replace the goods. The buyer and seller may also agree to a limit on consequential or incidental damages.

B. The UCC establishes a consumer remedy whenever a warranty is not fully met, even if the breach is relatively minor or unintentional and even if the seller is unaware of the defect, acts in good faith, and is not at fault. The UCC provides self help remedies of canceling the contract and deducting the consumer's damage from the outstanding balance.

C. UCC Article 2 provides the basic framework for warranty law.

1. Determines when express and implied warranties are created.

2. Provides initial regulation of disclaimers of implied warranties.

3. Initially determines the rules concerning privity of contract.

4. Sets out requirements as to notice of breach of warranty and creates standards for determining when a warranty is breached.

D. Scope of Article 2.

1. Has been enacted in every state EXCEPT LA.

2. Applies to "transactions in goods." (§ 2-102).

3. UCC shall be liberally construed and applied to promote its underlying purposes and policies. § 1-102. The UCC does not supersede earlier consumer protection laws. All statutes provide cumulative protections to buyers.

4. Generates two main questions when deciding UCC applicability.

a) Are "goods" involved?

(1) Applies to both new and used goods. For example, virtually every state applies the UCC warranty of merchantability to used automobile sales by merchants.

(2) Services are not covered under Article 2.

(3) Real property and houses are not covered. However, mobile homes are generally covered as well as some prefab homes to the extent they are treated as personalty, not reality.

(4) Mixed goods and services.

(a) Predominant Purpose Test: Was the predominant purpose of the transaction the purchase of goods?

(b) Courts use varying tests - know your state. Two of the more popular are:

(i) The Finished Product Test: Are the goods finished and just being installed or are the goods being created from raw materials specifically for this job? (NJ)

(ii) The *Bonebrake v. Cox* Test: Is the case one of the sale of a service with goods incidentally involved (contract with an artist for a painting as an example) or is it a sale with labor incidentally involved (contract for the purchase of a water heater that includes installation.) *Bonebrake v. Cox*, 499 F.2d 951 (8th Cir. 1991) (applying Iowa law).

b) Was there a "transaction" or a "sale" involving those goods?

(1) A "sale" consists in the passing of title from the seller to the buyer for a price (§ 2-106)

(2) Article 2 may apply to leases. However, a majority of jurisdictions have enacted Article 2A, which covers leases specifically.

5. Some UCC provisions apply to private sellers as well as merchants. (Compare § 2-103(1)(d) ("Seller") with § 2-104(1) ("Merchant")).

E. Warranties in General, (§§ 2-312 through 2-318).

1. Inspection of the goods.

a) May limit the defects the consumer can complain about. In order to vitiate an express warranty, the inspection must be sufficiently thorough and the buyer sufficiently sophisticated to

make material discoveries. Inspection after sale does not avoid an express warranty.

b) May also expand the basis of the bargain. Discovered characteristics constitute an express warranty that the goods will be sold and delivered in the present condition or will conform to the characteristics of the inspected sample or model.

2. When one or more warranties arise, they are cumulative unless they are inconsistent.

3. Resolving Inconsistent Warranties (§ 2-317). Warranties, whether express or implied, shall be construed as consistent with each other and as cumulative, but if such construction is unreasonable the intention of the parties shall determine which warranty is dominant. In ascertaining that intention the following rules apply.

a) Exact or technical specifications displace an inconsistent sample or model or general language of description.

b) A sample from existing bulk displaces inconsistent general language of description.

c) Express warranties displace inconsistent implied warranties other than an implied warranty of fitness for a particular purpose.

F. Warranty of Title. (§ 2-312)

1. Seldom an issue in consumer transactions. .

2. Warrants that the goods are transferred free of any security interest, lien, or encumbrance that was not known to buyer at the time of contract formation.

3. Disclaimer or modification of the warranty of title is allowed, as long as the buyer is protected from surprise.

4. The seller is obligated, as part of the contract, to deliver good title. The implied warranty of title is also made by a secured party upon resale of repossessed goods.

5. A claim for breach of warranty does not require evidence that the seller knew of the defect in the title.

6. For a breach of the warranty of title, the buyer is entitled to damages based on the value of the goods "at the time and place of acceptance." § 2-714.

7. Warranty of title issues arise in sale of "Gray Market Vehicles" (manufactures outside of U.S.) that they may not meet the U.S. safety and emission standards. If the state refuses to issue certificate of title it is a breach of implied warranty of title.

G. Warranties of Quality - Express Warranties. § 2-313.

1. Express warranties are created in a number of ways:

a) Orally or in writing.

b) Advertising or pictures of product.

c) Label or words on container.

d) Observable qualities of product (odometer reading, etc.).

2. Three Types of express warranties: (1) affirmation of fact or promise or quality; (2) description of the goods; or (3) representation of the goods by sample or model. (§ 2-313)

a) Affirmation of fact or promise. This type of express warranty is proven by showing that an affirmation of fact or promise of quality was made by the seller to the buyer which related to the goods and became a basis for the bargain.

(1) An affirmation of fact or promise.

(a) Includes broad statements of quality, characteristics or conditions, such as "mechanically perfect;" "This car has never been in an accident;" "This car is still under the manufacturers warranty;" or "The car is in good working condition"

(b) Statements of gas mileage, prior repairs or maintenance, such as "We gave it a full inspection and tune-up;" "It was driven only on Sundays to church . . .;"

(c) Salesman's oral statement that the transmission had been redone created an express warranty. *See Moore v. Mack Trucks, Inc*., 40 S.W. 3d 888, 44 UCC Rep. 2d. 416 (Ky. Ct. App. 2001)

(d) Promise to repair problems with car found in first 30 days was an express warranty. *See Fassi v. Auto Wholesalers*, 145 N.H. 404, 762 A.2d. 1034 (2000)

(e) Distinguish from mere opinion ("puffing"). Statement must be the kind of statement that reasonably could play a role in the buyer's decision.

(i) "This car is what a car should be."

(ii) Buyer's sophistication may be a factor.

(iii) Statements that horse had no problems and would make a good show horse were either true or merely puffing. *See Sheffield v. Darby*, 244 Ga. App. 437, 535 S.E.2d 776 (2000).

(2) Made by the seller to the buyer.

(a) The affirmation need not be made by the actual retail seller (could be made by manufacturer, for example, in advertising).

(b) The affirmation need not be in the seller's own words (the seller can incorporate third party statements into the bargaining).

(c) An express warranty by affirmation may be created by a non-merchant seller.

(d) The statement may be made to the public, rather than directly to the individual buyer. The buyer must in fact see or hear the statement.

(3) Which relates to the goods. The description of the goods creates a core warranty that cannot be disclaimed. "A contract is normally a contract for a sale of something describable and described." § 2-313 comment 4.

(4) Becomes part of the "Basis of the Bargain."

(a) Encompasses the entire transaction, not just the contract or negotiations, including all reasonable assumptions and inferences.

(b) Do NOT have to prove actual reliance. The seller has the burden to show statement was not a basis of the bargain.

(c) Warranty can be part of basis of bargain even though not incorporated into a written contract.

(d) May include statements made after the deal is complete:

(i) Statements in product labels at delivery.

(ii) Written Manufacturer Warranty received with goods.

b) Description of the goods.

(1) Any description that is reasonably part of the basis of the bargain, regardless of the source. It can be picture or a label.

(2) The warranty is that the goods will meet that description.

(3) For example, a "wool coat" must be made of wool. A "1974 Pontiac" must be one.

c) Sample or model.

(1) If a sample or model is used, the seller is warranting that the item purchased is the same as the sample or model.

(2) A sample is an example piece drawn from a group of virtually identical products to be purchased. When the seller shows a buyer a sample, the buyer reasonable expects that the goods delivered will be substantially similar to the sample.

(3) A model is an example offered for inspection when the product being purchased is not present (e.g. the buyer test-drives a car on the lot, then orders the same car in a different color).

(4) Generally, whatever the buyer sees in the example must be in the goods purchased unless the seller warns of discrepancies.

3. The seller's intent to create a warranty is not an element.

4. An express warranty may not be disclaimed by language in the same contract. § 2-316(1). Where a general disclaimer is inconsistent with an express warranty, the express warranty will survive as an exception to the disclaimer. Purchasers of consumer products are generally protected by a strict construction of warranties in favor of the consumer buyer.

5. Three questions of fact must be answered in an express warranty action.

a) Was there an express warranty?

b) What did the warranty cover?

c) Did the product live up to the warranty?

H. Warranties of quality - Implied Warranties.

1. These warranties do not arise unless there is a possessory interest. *See Evans v. Chrysler Fin. Corp*., 44 UCC Rep. 2d 1003 (Mass. Super. Ct. 2001) where no warranty arose when potential buyer test started a car.

2. Warranty of merchantability. (§ 2-314).

   a) The most important warranty in the code. Unless excluded or modified, a warranty that the goods shall be merchantable is implied in every contract if the seller is a merchant with respect to goods of that kind.

   b) The warranty of merchantability requires that the goods will pass without objection in the trade or business. Fungible goods must be of fair average quality. The item must be fit for the ordinary purpose for which such goods are used.

   c) Elements of the Warranty of merchantability.

      (1) Sale of goods. § 2-105.

      (2) By a seller. Although usually not an issue, a question may arise whether a distributor or indirect manufacturer is a "seller."

      (3) Who is a merchant with respect to goods of that kind. A merchant "means a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction or to whom such knowledge or skill may be attributed by his employment of an agent or broker or other intermediary who by his occupation holds himself out as having such knowledge or skill." § 2-104(1).

         (a) Applies to the first sale someone ever makes in the business.

         (b) "Goods of that kind" are not limited to specific makes and models. For example, a car dealer is a merchant with respect to cars, even if he is a Ford dealer selling a used Chevrolet.

d) Goods must be merchantable. (UCC § 2-314(2)) Six factors. The goods must be of the type that:

(1) Pass without objection in the trade under the contract description;

(2) In the case of fungible goods, are of fair average quality within the description;

(3) Are fit for the ordinary purposes for which such goods are used;

(a) A tractor that continually stalled was not merchantable. *See Eggl. v. Letvin Equip. Co*., 632 N.W. 2d 435, 45 UCC Rep. 2d 538 (N.D. 2001).

(b) Used car must be fit for ordinary purpose of driving i.e. must be safe and substantially free of defects; excessive oil consumption would be breech. See *Lipinski v. Martin J. Kelly Oldsmobile, Inc*., 2001 Ill. App. LEXIS 805 (Ill. App. Ct. Oct. 19, 2001).

(4) Run, within the variations permitted by the agreement, of even kind, quality and quantity within each unit and among all units involved;

(5) Are adequately contained, packaged, and labeled as the agreement may require; and

(6) Conform to the promises or affirmations of fact made on the container or label if any.

e) Basic Principles.

(1) Strict Liability - "No Fault"

(2) No language/assertions are required.

(3) No reliance is required.

(4) Ensures a basic standard or quality.

(a) Quality measured at the time of the sale or delivery.

(b) The buyer must prove that a defect exists.

(5) The warranty has not been validly excluded or modified.

f) In an action based on breach of the implied warranty of merchantability, the plaintiff must show not only the existence of the warranty but the fact that the warranty was broken and the breach of warranty was the proximate cause of the loss sustained.

3. Warranty of fitness for a particular purpose. § 2-315.

a) Basic provisions.

(1) Imposed by law whenever the seller at the time of contracting has reason to know:

(a) Any <u>particular purpose</u> for which the goods are being purchased, and

(b) That the buyer is relying on the seller's skill or judgment to provide goods suitable for that purpose.

(2) Implied warranties of fitness for a particular purpose and merchantability can exist in the same transaction.

b) Elements of the warranty of fitness for a particular purpose..

(1) The "seller" . . .

(a) Does not have to be a merchant. § 2-103.

(b) However, the seller must have appropriate "skill and judgment" about the goods.

(c) Warranty only extends to the items of goods the seller sells, not the other components of the product into which it is installed.

(2) At the time of the contracting, has reason to know . . .

(a) Told by buyer.

(b) Actual knowledge is not required. Constructive knowledge from the circumstances is sufficient.

(c) Example. "I need a car that gets thirty miles to the gallon, what do you recommend?"

(d) *But see Ford Motor Co. v. Gen. Accident Ins. Co*., 365 MD. 321, 779 A. 2d 362, 45 UCC Rep. 2d 319 (2001) (A manufacturer's knowledge that a chassis cab could be modified for use as a tow truck did not, without more, create an implied warrant for a particular purpose).

(3) Any particular purpose . . .

(a) May be a related "special" or non-customary purpose.

(b) "Ordinary Use" may qualify. For example, a salesman who bought a car that turned out to be unreliable. The problem was that the product could not perform its ordinary use – to drive. However, the buyer had a particular purpose in that his livelihood depended on that ordinary use.

(c) *See Bako v. Crystal Cabinet Works, Inc*., 44 UCC Rep. 2d 1048 (Ohio Ct. App. 2001). Seller breached implied warranty by selling buyer a stain that was incompatible with the sealant the buyer stated she was using).

(4) And that the buyer is relying.

(a) The buyer must actually rely upon the seller's skill and judgment.

(b) Reliance only requires that the buyer be influenced by the seller's skill and judgment.

(5) On the seller's skill and judgment . . .

(a) Third party statements do not create skill and judgment (ex. Gov't study, another retailer, or friend)

(b) The seller must hold himself out to have certain skill and judgment.

(6) To select or furnish suitable goods . . .

(a) Can be a group of goods – "Any of my four cylinder cars will get 30 MPG" - whichever car the buyer buys, the warranty will apply for MPG.

(b) Seller must make the decision that the goods are suitable for the buyer's purpose.

(7) The goods are impliedly warranted to be fit for that purpose.

(a) More specific than other warranties.

(b) The goods may do exactly what the manufacturer intended, but violate the warranty because they do not meet the buyer's intended purpose.

(8) Seller's good faith is irrelevant.

I. Disclaimers and modifications of warranties of quality. §2-316.

1. Disclaimers are disfavored by the UCC. Courts generally construe disclaimers as narrowly as possible to protect the consumer buyer.

2. Express warranties. § 2-316(1).

   a) Modifying express warranties. Attempts to negate or limit the warranty are construed wherever reasonable as staking out the boundaries of the warranty.

   b) Express warranties may NOT be disclaimed. § 2-316(1).

   c) Whenever reasonable, language of express warranties should be construed consistently with words or conduct which may be construed to limit or negate those warranties. The negation or limitation of warranty is excluded if it is irreconcilable with warranty creation.

3. Implied warranties. § 2-316(2).

   a) Modifying implied warranties.

      (1) Exclusion or modification of the implied warranty of merchantability requires express language that is both conspicuous and uses the word "merchantability."

      (2) Exclusion or modification of the implied warranty of fitness for a particular purpose may be accomplished by general language, but must still be conspicuous.

      (3) Implied warranties, including the warranty of merchantability, may be excluded or modified by course of dealing or usage of trade, use of recognized language like "as is" or "with all faults," or by the buyer's prior inspection of the goods.

   b) State specific. About half of the states preclude or restrict a seller's ability to disclaim implied warranties. Be sure to check your state law.

   c) Disclaimers. The following arguments may be used to defeat disclaimers of warranties in contracts. They are based largely on the UCC policy that disclaimers are NOT favored.

      (1) Must be conspicuous – written so that a reasonable person against whom it is to operate should have noticed it.

(2) Must be available before the contract signed.

(3) Some states require that the consumer have actual knowledge of the disclaimer. *See Materials Mktg. Corp. v. Spenser*, 40 S.W.3d 172, 43 UCC Rep. Serv. 2d 1131 (Tex App. 2001). (holding that a limitation of liability clauses on the back of the contract was ineffective without evidence that the buyer was aware of it or that it was given to the buyer).

(4) A disclaimer of the warranty of merchantability must have the word merchantability in it (UCC § 2-316), unless the words "as is" or "with all faults" are used in a clear conspicuous manner.

(5) "As Is" disclaimers may be attacked using the circumstances of the sale to include the seller's conduct and the level of the consumer's knowledge. The "as is" disclaimer may be ineffective in circumstances where the disclaimer is unclear to the buyer because of the circumstances, i.e. contract signing rushed or the seller discouraged the buyer from reading the contract—"It's just a bunch of legalese.".

J. Procedural requirements for enforcing rights for breach of warranty.

1. Consumers seeking to enforce warranty rights normally must notify the seller that the warranty has been breached within a reasonable time after the breach is or should have been discovered. § 2-607(3)(a). Failure to do so precludes most UCC remedies.

2. Actions must also be brought within the statute of limitations. § 7-725.

a) The UCC defines the statute of limitations as 4 years after the cause of action accrues.

b) The UCC statute of limitation begins to run at the time of delivery of the goods, not from the time the defect is discovered or the time of injury.

K. Buyer's remedies for breach of UCC warranties.

1. Buyer's remedies prior to acceptance. § 2-711.

    a) When the seller tenders non-conforming goods, i.e. goods that fail to meet the terms of the contract, including all express and implied warranties, the buyer has a right to reject the goods within a reasonable time. § 2-601. The buyer's right to reject goods may be limited by the terms of the contract, i.e. a provision giving the seller the right to repair or replace non-conforming goods within a specified time period. § 2-719.

    b) Rejection of the goods requires the buyer to notify the seller of both the rejection, and the specific defects in the tender. § 2-602. Failure to notify the seller of the specific defects may result in waiver of those defects as a basis for rejection. § 2-605.

    c) In circumstances where the seller fails to timely cure the defect, or has no right to cure, the buyer is entitled to cancel the contract, to receive a prompt refund of any of the purchase price already paid, and to receive damages associated with "covering" the breach with goods from another seller, including incidental and consequential damages.

2. Buyer's remedies following acceptance. § 2-714.

    a) The buyer may revoke acceptance of non-conforming goods under two circumstances: (1) when he accepted the goods assuming that the seller would cure the non-conformity and the seller has failed to do so; or (2) when he accepted the goods because of the seller's assurances or because discovery of the non-conformity at the time of delivery was unreasonable, i.e. latent defect.

    b) Following a proper revocation, the buyer's remedies will be under § 2-711, above.

    c) When the buyer's time for revocation has passed, the buyer may still be entitled to damages for breach of warranty, provided the buyer has given timely notice to the seller of the suspected breach. § 2-607(3).

        (1) Following acceptance, the buyer has the burden of proving the goods failed to meet the warranty standard. § 2-607(4).

(2) The buyer's damages may be determined in any manner which is reasonable, but are generally equal to "the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been as warranted, unless special circumstances show proximate damages of a different amount." § 2-714.

3. Types of damages for breach of warranty.

a) General damages. UCC § 714. Generally this is the difference at the time of acceptance between the value of the goods as accepted and the value the goods would have had if as warranted.

b) Incidental damages. UCC § 2-715(1). Damages directly and immediately resulting from seller's breach pertaining to the goods themselves (e.g. inspection, transportation). These are the direct costs to the buyer of the breach - like the cost of transportation of the goods, or their inspection

c) Consequential damages. UCC § 2-715(2). Damages resulting less directly and less immediately from the breach and generally pertain to the buyer's circumstances. These are the damages that flow only from the consequences of the goods not being acceptable such as lost deliveries due to the failure to deliver a working delivery truck etc.

d) Punitive damages. General rule, punitive damages are unavailable. May be available if the conduct is egregious enough to amount to an independent tort (i.e. willful, wanton and malicious disregard for the rights of buyers).

e) Liquidated damages. May be included as a term of the contract, whether or not there is a readily available means to measure the damages in some more exact fashion. Liquidated damages must be reasonable in light of the anticipated or actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy. § 2-718.

f) Other remedies agreed to by the contracting parties. § 2-719.

g) Attorney's fees. Not recoverable as a general rule absent contractual or statutory authority.

4. Seller's possible defenses to a breach of warranty.

a) Buyer's conduct as to cause of damage or misuse of product.

b) Non-compliance with any conditions precedent to warranty coverage.

c) Expiration of the express warranty period.

IV. THE MAGNUSON-MOSS WARRANTY ACT (15 U.S.C. §§ 2301-2312).

A. Prior to passage of the Magnuson-Moss Warranty Act, consumers often had difficulty determining who the warrantor was, what was being warranted, who bore which expenses if the product was defective, the duration of the warranty, or who was entitled to enforce the warranty. The Magnuson-Moss Warranty Acts addresses each of these deficiencies.

B. Applicability of the Magnuson-Moss Warranty Act.

1. Purpose.

a) To regulate, simplify, and standardize warranties given by manufacturers.

b) The Act does not mandate warranties or warranty duration.

c) The Act does mandate certain disclosures if the seller gives a warranty.

d) The Act provides for damages if warranties given are breached.

2. The act applies to consumer products <u>manufactured</u> after 4 July 1975.

a) Consumer products are those "normally" used for personal, family, or household purposes. They do NOT have to be used exclusively for that purpose. 16 C.F.R. § 700.1. The Act applies to new and used products. Consumer products include

any tangible personal property which is distributed in commerce.

(1) Goods are "normally" used for consumer purposes if that use is "not uncommon."

(2) "Normally" does not mean that consumer use is the predominant use, just that this use is not atypical.

(3) Ambiguities are resolved in favor of coverage.

(4) Whether a product is normally used for personal, family or household good purposes is a question of fact. A $500,000 airplane is not a consumer product. *See Cinquegrani v. Waypoint Aviation Servs.*, Inc., 2001 U.S. Dist. LEXIS 7802 (N.D. Ill. June 7, 2001).

b) Must be *tangible* property. The Act does not apply to goods supplied incident to a service contract, i.e. the doors, lights, carpet, etc. provided incident to a remodeling contract.

c) Must be *personal*, not real property.

(1) Some things that may become fixtures are still personal (e.g., air conditioners, insulation, siding, dropped ceilings, etc.).

(2) If the item is integrated into a structure at the time of purchase, however, it is not a consumer product (e.g., beams, wallboard, wiring, plumbing, etc.)

(3) Mobile homes are personal property.

d) Does NOT apply to services unless it covers both the parts and the labor (e.g. rebuilding a engine and parts).

e) Leases. The Act has recently been interpreted to include leases of consumer products such as automobiles on the rationale that a lessee is a consumer to whom the vehicle has been transferred, regardless of whether a sale has occurred. *See, e.g., Cohen v. AM Gen. Corp.*, 264 F. Supp. 2d 616 (N.D. Ill. 2003).

C. Parties Liable Under The Act.

1. Any supplier. "Supplier" is any person engaged in the business of making a consumer product directly or indirectly available to consumers. All entities in the chain of production and distribution of a consumer product including the manufacturer, component supplier, distributor, wholesales, and retailer.

2. Any warrantor. A "warrantor" is any supplier or other person who gives or offers to give a written warranty or who is or may be obligated under an implied warranty. (such as dealer who provides a written warranty, but if a dealer only passes on a manufacturer's warranty the dealer is not liable for a breech of that warranty, depends on factual investigation of dealer's involvement).

3. Any service contract provider.

4. "Other Person."

a) No privity of contract required.

b) Third party warrantors (like Good Housekeeping) who do not sell products but who offer warranties are covered.

D. Enforcing Implied and Written Warranties and Service Agreements.

1. The Act prohibits breaches of warranties

a) Implied warranty– Any warranty arising under state law in connection with the sale of a consumer product.

(1) Even if no written warranty is given!

(2) Applies to any warrantor, not just suppliers.

(3) Existence of the warranty is a matter of state law.

(4) Once warranty exists, however, the Act provides a federal remedy for breach of that warranty.

b) Written warranty.

(1) Provides a specific statutory remedy for breach of warranties.

(2) Provides a federal cause of action for damages and attorney's fees.

(3) State law privity requirements do not apply (see below).

c) Service contracts.

(1) Defined by the Magnuson-Moss Warranty Act as a "contract in writing to perform, over a fixed period of time or for a specified duration, services relating to the maintenance or repair (or both) of a consumer product." 15 U.S.C. § 2301(8).

(2) The Act specifically recognizes the right of a supplier or warrantor to enter into a service contract with the consumer in addition to or in lieu of a written warranty, as long as the service contract "fully, clearly, and conspicuously discloses its terms and conditions in simple and readily understood language." 15 U.S.C. § 2306(b).

(3) Act provides a federal cause of action for breaching requirements under the service contract.

2. Prohibitions on disclaimers and modifications of implied warranties.

a) The Act prohibits a supplier from disclaiming or modifying an implied warranty when the supplier has given a written warranty or a service contract within 90 days of the sale. Even if the seller gives a highly restrictive service contract or written warranty, the implied warranties cannot be disclaimed.

b) If the seller/supplier provides an express limited warranty, then the implied warranties may also be limited in duration to a period no less than the duration of the express written warranty.

3. Impact on privity of contract requirements.

a) Horizontal privity – Someone other than the retail buyer (someone who receives the product as a gift, subsequent purchases) seeks to sue the seller.

(1) Act protects any "consumer" damaged by a violation of the Act or by failure to comply with a written warranty, implied warranty or service contract. In this context, the word consumer includes the following:

(a) Buyers.

(b) Any person to whom the goods are transferred during the duration of the implied or written warranty, or service contract.

(c) Any other person protected under the terms of the warranty.

(2) Thus horizontal privity requirements imposed under state law are ineffective as to all owners of the product.

(3) Suppliers/warrantors may limit express warranties to the original owner by saying "for as long as you own your car." In this case look to implied warranties.

(4) "Limited" warranty providers may limit implied warranties to the original owner if a notice of this provision is prominently disclosed in the warranty.

b) Vertical Privity – Can the buyer sue someone up the distribution chain with whom the buyer did not actually enter a transaction?

(1) Written warranties. Magnuson-Moss virtually eliminates vertical privity requirements through the broad definitions of supplier, warrantor, and service contract provider.

(2) Implied warranties. State law MAY require vertical privity for implied warranty claims. Courts are mixed as to whether Magnuson-Moss supersedes these requirements. (AL, CT, FL, GA, IN, NY, OR all

require vertical privity.) One approach is to establish that the dealer is the manufacture's sales agent.

E. Restrictions on written warranties (full and limited).

1. Many provisions of the Act apply only if there is a written warranty.

a) A written warranty is:

(1) A written affirmation that the product is defect free or will meet a specified level of performance for a specified period, OR

(2) A written undertaking to refund, repair, replace or remedy a product **IF** it fails to meet specifications.

(3) Which written affirmation, promise, or undertaking becomes part of the basis of the bargain between a supplier and a buyer for purposes other than resale of such product.

b) A certificate of quality assurance stating that a mobile home has been carefully inspected to ensure quality was a written warranty. *See Horton Homes, Inc. v. Brooks*, 2001 Ala. LEXIS 431 (Ala. Nov. 30, 2001).

c) Whether the written warranty remains in effect is the most difficult question for used products.

2. Tie-ins are prohibited. This provision provides that sellers/warrantors:

a) Cannot condition warranty applicability on using a particular part or certified product.

b) Cannot limit to factory servicing.

c) Cannot mandate a specific brand name.

d) CAN mandate a particular grade of product. For example, cannot say Quaker State Motor Oil, but CAN say 10W-40 motor oil.

e) There are only two exceptions:

(1) The manufacturer provides a product or service that is free of charge, OR

(2) The FTC approves a waiver in the public interest.

3. The warrantor cannot be the final arbiter of warranty disputes. A warrantor cannot grant itself the sole authority to determine whether a defect or nonconformity within the scope of the written warranty exists or to have the final or binding decision in a dispute.

4. Warranty registration cards.

a) Full Warranty coverage MAY NOT be conditioned on the consumer returning a completed warranty card.

b) Limited Warranty coverage MAY be conditioned on the return of the card so long as that fact is disclosed in the warranty.

c) Implied Warranties – the act is silent on this, but requiring the return of a warranty card should be considered an invalid limitation on an implied warranty.

F. Requirements applicable to only "full" warranties.

1. The Act requires that every warranty be labeled as "full" or "limited."

2. To be labeled "full," the warranty must comply with the following:

a) It cannot restrict the rights of subsequent owners during the warranty period.

b) It must promise to remedy defects within a reasonable time and without charge.

c) It cannot limit the duration of any implied warranty.

d) It cannot limit consequential damages unless the limit is conspicuously present on the face of the warranty.

e) It MUST permit the consumer to elect a refund or replacement after a reasonable number of attempts by the manufacturer to fix the problem; AND

f) It must require no duty of the consumer other than notice of the defect, unless the duty is "reasonable." For example, to use product in a reasonable manner and perform any necessary maintenance.

3. Any warranty that does not meet the requirements above must be labeled "limited."

G. Disclosure Provisions.

1. Although the Magnuson-Moss Warranty Act does not require that any consumer product be warranted, it does provide for certain disclosures if the manufacturer of a product chooses to give a written warranty:

2. If the product costs more than $10, the warrantor must properly designate the warranty as a "full" or "limited" warranty (in compliance with federal minimum warranty standards.)

a) The designation must be a caption or prominent title, clearly separated from the warranty text.

b) For a Full Warranty ONLY, there must be a reference in the caption/designation to the duration of the warranty.

c) Examples of PROPER designations: "full one-year warranty;" "limited warranty;" "limited 60-day warranty;" "limited warranty for as long as you own your car."

d) Note that a warrantor can give BOTH a full and a limited warranty on the same product as long as it is properly differentiated (clear and conspicuous). For example, full three-year warranty against mechanical defects, limited rust-through warranty on same car.

3. General disclosure principles.

a) The disclosures must be in a single document.

b) The language must be “simple and readily understood.”

c) The disclosure must be made clearly and conspicuously.

d) Consumer reading the warranty should be able to see exactly what is and is not covered by the warranty.

e) Must include the specific duration of the warranty.

f) The warranty must be made available to the consumer before the decision to buy is made. The seller may comply by:

(1) Providing a Copy with every product; OR

(2) Clearly and conspicuously displaying the text of the warranty "in close conjunction to" the warranted product, and/or

(3) Maintaining readily available binders containing copies of the warranties for the products sold in each department of the seller's store, and/or

(a) not unusual in locations such as Sears to look on the wall and you will see the sign that says the warranty is available for inspection.

(4) Displaying the package of a warranted consumer product in such a way that the printed text of the warranty on the package is clearly visible to prospective buyers at the point of sale, and/or

(5) Placing a notice containing the text of the warranty in close proximity to the warranted consumer product, in a manner that clearly indicates to prospective buyers the product to which it applies.

g) Special rules for mail order or catalog sales. These sellers must disclose the warranty:

(1) On the same page as the product; OR

(2) On the page facing that page; OR

(3) In a clearly referenced information section; OR

(4) By disclosing the address where the consumer can get a copy free of charge.

4. Specific disclosure requirements. All written warranties, full or limited, on consumer products costing more than $15 are required to disclose the following:

a) *Parties who can enforce the warranty:* The identity of the parties to whom the warranty is extended, including any limitations (such as to the original purchaser of the product).

b) *Warranty Coverage:* A clear description and identification of products, parts, characteristics, components, or properties covered by the warranty.

c) *Warrantor's Performance Obligations:* A statement of what the warrantor will do in the event of a defect, malfunction, or failure to conform to the written warranty.

d) *Warranty Duration:* The point at which the warranty term commences, if different from the purchase date, and the time period or other measurement of warranty duration.

e) *Consumer's Duties to Exercise the Warranty:* A step-by-step explanation of the procedure that the consumer should follow to obtain performance of any warranty obligation.

f) *Registration Cards*: Whether the return of any registration is required (if allowed).

g) *Informal Dispute Resolution:* Information about the availability of any "informal dispute settlement mechanism" elected by the warrantor.

h) *Duration Limitation on Implied Warranties:* Any limitations on the duration of implied warranties.

i) *Any exclusions of or limitations* on relief available to the consumer, such as incidental or consequential damages.

j) The following statement: "This warranty gives you specific legal rights, and you may also have other rights which vary from state to state."

H. Relationship Between Various Warranty Protections.

1. Nothing in the Act "shall invalidate or restrict any right or remedy of the consumer under State or federal law." 15 U.S.C. § 2311(b)(1). The Act does not preempt the UCC or state UDAP statutes.

2. Because some states have special consumer warranty statutes which may give the consumer greater protection than the Magnuson-Moss Warranty Act, and thus take precedence over that Act, the FTC has required that all written warranties covered by the Act must clearly and conspicuously disclose from one to three additional provisions.

a) All such warranties must say: "This warranty gives you specific legal rights, and you may also have other rights which vary from state to state." 16 C.F.R. § 701.3(a)(9).

b) In addition, if the written warranty contains any limitations on the duration of implied warranties, such limitations must be disclosed on the face of the warranty accompanied by the following statement: "Some states do not allow limitations on how long an implied warranty lasts, so the above limitation may not apply to you." 16 C.F.R. § 701.3(a)(7).

c) Any limitations on remedies for breach of warranty, such as exclusion of incidental or consequential damages, must be accompanied by the following statement: "Some states do not allow the exclusion or limitation of incidental or consequential damages, so the above limitation or exclusion may not apply to you."

I. Who can sue?

1. Anyone who buys a consumer product for purposes other than resale.

2. Anyone to whom the product is transferred during the life of a written or implied warranty.

J. Remedies.

1. The U.S. Attorney General and the FTC have authority to pursue preliminary and permanent injunctions, as well as cease and desist orders, restitution and civil penalties.

2. Private civil relief under the Magnuson-Moss Warranty Act.

    a) Negotiation and/or mediation through an informal dispute settlement mechanism. All domestic manufactures and most importers include an informal dispute resolution mechanism as a precondition to suit. Although a warrantor need not provide this nonjudicial alternative for the resolution of warranty disputes, if such a mechanism is available a consumer can be required to use the mechanism before beginning civil action provided:

        (1) The mechanism and its implementation meet the requirements established by the FTC. For example, it must be:

            (a) Free of charge;

            (b) Sufficiently funded & competently staffed;

            (c) Provide quick and fair resolution; and

            (d) Have no undue influence by warrantor.

        (2) The warrantor incorporates into the written warranty the requirement that the consumer resort to the mechanism before pursuing any legal remedy under the Magnuson-Moss Warranty Act. *See*16 C.F.R. Part 703 for more details.

    b) Industry complaint bureaus.

    c) Consumers can sue for damages and other legal and equitable relief in either state or federal court. State court is the predominant jurisdiction.

    d) The amount in controversy for suit in federal court must exceed $50,000 for both individual and class actions.

e) Personal injury damages.

(1) Typically, private actions for breach of warranty may be brought under the Magnuson-Moss Warranty Act only for direct economic damage.

(2) Consequential damages, such as personal injuries, cannot be recovered unless there has been a violation of certain of the Act's substantive provisions.

f) Punitive damages may be recovered in suits brought under the Act if available under state law.

g) Damages for emotional distress can be recovered under the Act if they are available in breach of warranty actions under state law.

h) Attorneys' fees and court costs are allowable if the consumer prevails in the action.

SPECIFIC PROTECTIONS FOR AUTOMOBILES

NEW CARS

V. STATUTORY WARRANTIES IN AUTO SALES: "LEMON LAWS"

A. Introduction. All 50 states and the District of Columbia have some form of "lemon law." See Appendix B.

B. Impact of typical state "lemon" law.

1. Creates a new statutory warranty that modifies every manufacturer's warranty. Lemon laws were enacted to overcome the inadequacies of the warranty provisions of the UCC.

2. Sets standards for consumers and manufacturers in determining when a seller must refund the buyer's money and take back the vehicle ("buy-back") must be awarded.

3. State lemon laws may be applied to automobiles purchased before the law went into effect if the warranty period has not expired at the time relief is sought under the law's provisions.

4. Common provisions. Although there is a great deal of variety among the various "lemon" laws, many include the following common provisions.

a) Most lemon laws apply only to new cars, although some also apply to used cars, motorcycles, off road vehicles, mobile homes and leased cars. *See, e.g.*, N.Y. Gen. Bus. Law § 198-b (1990) (used cars with less than 36,000 miles are covered if they are sold by persons selling three or more used cars per year and they develop serious problems in the first 60 days or 3,000 miles, which ever comes first; cars with more than 36,000 are covered for 30 days or 1,000 miles). Some states may apply these laws to leased vehicles.

b) Many statutes provide that the manufacturer must allow the consumer to return the car for a full refund or a replacement vehicle if the following conditions are met:

(1) The consumer reports the defect within the warranty period or within one year of the date of actual delivery of the vehicle, whichever is earlier.

(2) A substantial defect in a new automobile cannot be repaired in a reasonable number of attempts.

(a) Three or four attempts to correct the same or substantially the same defect is normally "reasonable."

(b) Some statutes allow the consumer the benefit of the statute if the car is out of use for 30 or more days. Some use calendar and others use business days.

c) All state lemon laws contain an explicit "savings clause" that preserves consumers' rights under all other laws.

d) The buyer need not show that the defect causes a safety hazard. *See Mooberry v. Magnum Mfg., Inc*., 32 P.3d 302 (Wash. Ct. App. 2001)

e) The good faith of the dealer in attempting to repair the vehicle does not defeat the consumer's right to relief under a lemon law if the malfunction goes uncorrected. *See, e.g.*, *Muzzy v. Chevrolet Div., General Motors Corp.*, No. 87-272 (Vt. Dec 1, 1989) (in five separate attempts, dealer was unable to correct stalling problem and rough running engine; dealer then installed valve that it said corrected problem--court affirmed refund of portion of purchase price and other expenses: statutory criteria was three repair attempts and satisfaction (subjective) of customer).

f) Under most lemon laws, the repair attempts must be made even after the manufacturer's warranty expires, as long as the defect was first reported within the warranty period.

g) Lemon laws generally are limited to defects covered by the manufacturer's written warranty, so the malfunction must be shown to have resulted from a defect in material or workmanship.

h) Manufacturers are seldom held liable for defects resulting from the consumer's abuse, neglect or unauthorized modifications. The abuse should be abnormal, unforeseeable conduct and not conduct that merely puts the warranty to the intended test.

i) Under all lemon laws, the consumer must give notice of the defect, but the notice provisions vary greatly.

(1) Most allow notice to the manufacturer, its agent, or an authorized dealer.

(2) However, it is wise to provide written notice to the manufacturer by certified mail.

j) No lemon law requires that after the consumer notifies the dealer or manufacturer of the substantial defect the consumer discontinue use of the vehicle while awaiting the dealer's repair attempts.

k) Most lemon laws permit the dealer an affirmative defense if:

(1) The defect or nonconformity does not substantially impair the value or use of the vehicle.

(2) The consumer's abuse, neglect, or unauthorized modifications or alterations cause the defect.

l) Offsets. Almost all state laws provide that the consumer will pay the dealer an offset:

(1) This is usually a reasonable allowance for use of the vehicle.

(2) An example is a formula used in several states which is (# of miles driven)/100,000 x (the cost of the vehicle).

5. Remedies available under lemon laws.

a) Most lemon laws require consumers first to resort to an informal dispute settlement mechanism (IDSM) designated by the manufacturer, if the IDSM complies with FTC guidelines

contained in 16 C.F.R. § 703, before being eligible to receive a full refund or a replacement vehicle.

(1) The lemon laws of some states require that the consumer use the manufacturer's IDSM only if the IDSM complies with the FTC guidelines "completely," while others require that the consumer comply with the IDSM if it complies with the FTC guidelines "substantially."

(2) States vary as to which programs they find consistent with FTC guidelines, and the court may ultimately make this determination.

b) Some states provide state-organized and funded IDSM mechanisms. *See e.g.*, Hawaii Rev. Stat. § 490:2-313.2; N.Y. Gen. Bus. Law § 198-a(g).

c) The basic remedy of refund of the purchase price includes, in most states, all taxes, preparation fees, and other charges or fees paid by the consumer.

d) Most states also require deduction of the reasonable value of the consumer's use of the automobile up to the first time the car was submitted for correction of the defect.

e) Attorneys' fees and court costs may be made available for consumers who successfully sue to obtain lemon law remedies.

f) Some lemon laws include prohibitions against waiver of lemon law protection and resale of a returned lemon unless full disclosure of the car's history is made to the buyer.

g) Some lemon laws permit consequential and incidental damages.

h) Under a few statutes, manufacturers who are sued in bad faith or without substantial justification are entitled to recover legal expenses from the consumer.

VI. LATENT DEFECTS (After Lemon Law Period Expires)

A. Discovery During the Written Warranty Period. (See Warranty Law Above.)

1. Use the Magnuson-Moss Act to bring a suit for damages for breach of the warranty.

2. Revoke acceptance under the UCC.

B. Discovery After the Warranty Period Expires.

1. Secret Warranties: A strategy where the manufacturer pays for repair of defects after the warranty period, but only for those consumers who complain.

a) These policies are "secret" because they are normally passed only to regional offices and never to buyers.

b) Secret warranties cover certain components, or systems that malfunction or defects which the manufacturers have found occurring in a wide spread pattern.

c) These are tough to find and document. The only strategy is to complain long and loud. Legal assistance attorneys may be able to help in dealing with the manufacturer's regional office.

d) An important resource here is The Center for Auto Safety, 2001 S Street, NW, suite 410, Washington, DC 20009, (202) 328-7700. http://www.autosafety.org They have information on secret warranty programs for specific model cars.

3. UDAP Violations. Failure to disclose a latent defect when the manufacturer knows about it should almost certainly be a UDAP violation.

USED CARS

VII. AVOIDING "AS IS" SALES

A. Find Express Warranties (*See also* Warranty Law Above) because express warranties cannot be disclaimed.

1. Manufacturer's warranties. Written warranties apply to subsequent purchasers unless expressly limited to first purchaser. Note that certain parts (drive train, emission control, etc.) may be covered even if the entire vehicle is not.

2. Dealer's warranties.

   a) Descriptions of the make, model, year, options, odometer reading etc. in sales agreement.

   b) Oral representations by sales personnel. Note that dealers often try to avoid these by merger clauses in the sales agreement. These types of waivers are often ineffective. *See McGregor v. Dimou,* 101 Misc. 2d 756, 422 N.Y.s. 2d 806 (Civ Ct. 1979) (in very good condition and had not been in an accident)

   c) Advertising about vehicle.

   d) Dealers may argue that the FTC Used Car Rule (see below) Buyer's Guide supersedes these warranties when it says, "As Is." The FTC Rule only requires disclosure of certain listed types of warranties so this argument should not be effective.

B. Implied Warranties.

1. Disclaimer limitations. Implied warranties cannot be disclaimed if the dealer gives a written warranty or "enters into" a service contract. When a dealer sells a service contract along with the vehicle, the FTC Used Car Rule requires that the dealer check the box marked "WARRANTY" on the buyer's guide and also a box stating that implied warranties may give buyer additional rights.

   a) May be an issue about whether dealers "enter into" a service contract if they do not provide the service themselves, but simply offer a third party service contract.

   b) The Magnuson-Moss Act has limited applicability if the state regulates service contracts.

2. State Law limitations. A number of states restrict the disclaimer of implied warranties including AZ, CA, DC, IL, KS, LA, ME, MD, MA, MN, MS, NH, OR, RI, WA, WV, and WI.

C. Adequate Disclosure of "AS IS" Disclaimer.

1. Available to consumer before purchase?

2. Conspicuous – either a larger type size or otherwise set out from the rest of the K.

3. Must make plain that implied warranties are disclaimed.

D. Non-Warranty Claims.

1. UDAP – *See* Chapter 3. Deception, misrepresentation or the like.

2. Traditional legal theories: fraud, tort liability (negligence, strict liability).

VIII. CAR'S TRUE HISTORY NOT DISCLOSED

A. The Motor Vehicle Information and Cost Savings Act commonly referred to as The Federal Odometer Act concerns inaccurate Odometer Readings

1. Resources.

a) 49 U.S.C. §§ 32701-32711.

b) 49 C.F.R., Part 580.

c) NATIONAL CONSUMER LAW CENTER, AUTOMOBILE FRAUD (2d ed. 2003 and Supp. 2006).

2. Congressional findings and purposes. (49 U.S.C. § 32701)

a) Findings.

(1) Buyers of motor vehicles do and are entitled to rely heavily on the odometer reading as an index of the condition and value of a vehicle.

(2) An accurate indication of the mileage assists a buyer in deciding on the safety and reliability of the vehicle.

b) Purposes of the Federal Odometer Act.

(1) To prohibit tampering with motor vehicle odometers (any vehicle with an odometer); and

(2) To provide safeguards to protect purchasers in the sale of motor vehicles with altered or reset odometers. Requires that any car transfer include an odometer disclosure statement.

c) Who must comply with the Act.

(1) Any person or business that violates any section of that act may be liable, including private individuals who sell a car to another consumer. Disclosure statement requirements are more limited in scope.

3. Definitions (49 U.S.C. § 32702).

a) “Dealer" means a person that sold at least 5 motor vehicles during the prior 12 months to buyers that in good faith bought the vehicles other than for resale.

b) "Leased motor vehicle" means a motor vehicle leased to a person for at least 4 months by a lessor that leased at least 5 vehicles during the prior 12 months.

c) "Odometer" means an instrument for measuring and recording the distance a motor vehicle is driven, but does not include an auxiliary instrument designed to be reset by the operator of the vehicle to record mileage of a trip.

d) "Transfer" means to change ownership by sale, gift, or any other means.

4. Primary protections of the odometer act.

a) Prohibition on odometer tampering (49 U.S.C. § 32703). A person may not--

(1) advertise for sale, sell, use, install, or have installed, a device that makes an odometer of a motor vehicle

register a mileage different from the mileage the vehicle was driven, as registered by the odometer within the designed tolerance of the manufacturer of the odometer;

(2) disconnect, reset, alter, or have disconnected, reset, or altered, an odometer of a motor vehicle intending to change the mileage registered by the odometer;

(3) with intent to defraud, operate a motor vehicle on a street, road, or highway if the person knows that the odometer of the vehicle is disconnected or not operating; or

(4) conspire to violate this section.

b) Disclosure requirements (49 C.F.R. § 580.5).

(1) Each title, at the time it is issued to the transferee, must contain the mileage disclosed by the transferor when ownership of the vehicle was transferred and contain a space to provide odometer disclosures at the time of future transfer.

(2) Any documents that are used to reassign a title shall contain a space for the required odometer disclosures at the time of transfer of ownership.

(3) Written disclosure.

(a) Made on the title or on the document used to transfer ownership. Transferors must sign this written disclosure and include their printed name. In addition, the written disclosure must contain the following information:

(i) The odometer reading at the time of transfer (not to include tenths of miles);

(ii) The date of transfer;

(iii) The transferor's name and current address;

(iv) The transferee's name and current address; and

(v) The identity of the vehicle, including its make, model, year, and body type, and its vehicle identification number.

(b) The statement shall refer to the Federal law and shall state that failure to complete or providing false information may result in fines and/or imprisonment. Reference may also be made to applicable State law.

(c) Certification by the owner that either,

(i) To the best of his knowledge the odometer reading reflects the actual mileage, or;

(ii) If the transferor knows that the odometer reading reflects an amount of mileage in excess of the designed mechanical odometer limit, he shall include a statement to that effect; or

(iii) If the transferor knows that the odometer reading differs from the mileage and that the difference is greater than that caused by odometer calibration error, he shall include a statement that the odometer reading does not reflect the actual mileage, and should not be relied upon. This statement shall also include a warning notice to alert the transferee that a discrepancy exists between the odometer reading and the actual mileage.

(d) If the vehicle has not been titled, or if the title does not contain a space for the information required, the written disclosure shall be executed as a separate document.

c) Other Requirements.

(1) If the odometer must be repaired, serviced, or replaced, the mileage must be set the same as before the service or set to 0 and a notice attached to the left door frame reflecting the prior mileage, date of service and whether replacement or repair. (49 U.S.C. § 32704)

(2) Act prohibits parties from conspiring to violate any of the act's provisions.

(3) Unlike many consumer statutes that require disclosures be given only to consumers, odometer disclosures are required for any change of title, no matter the nature of the parties involved in the transfer.

(4) Some transfers of vehicles are exempt thus no disclosure necessary, however if they do give a disclosure it cannot be false. The regulation exempts these 5 types of transfers:

(a) A vehicle that is 10 years old or older.

(b) A new vehicle before its first transfer for a purpose other than resale.

(c) Vehicles with gross weight over 16,000 pounds.

(d) A vehicle that is not self-propelled.

(e) New vehicles sold directly to U.S. agency.

5. Penalties and enforcement (49 U.S.C. § 32709).

a) **Civil penalty.** Liable to the United States Government for a civil penalty of not more than $2,000 for each violation. A separate violation occurs for each motor vehicle or device involved in the violation. The maximum penalty under this subsection for a related series of violations is $100,000. In determining the amount of a civil penalty under this subsection, the Secretary shall consider--

(1) the nature, circumstances, extent, and gravity of the violation;

(2) with respect to the violator, the degree of culpability, any history of prior violations, the ability to pay, and any effect on the ability to continue doing business; and

(3) other matters that justice requires.

b) **Criminal penalty.** A person who knowingly and willfully violates this chapter or a regulation prescribed or order issued under this chapter shall be fined under title 18, up to $50,000, imprisoned for not more than 3 years, or both.

c) **Civil actions by Attorney General.** The Attorney General may bring a civil action to enjoin a violation of this chapter or a regulation prescribed or order issued under this chapter.

d) **Civil actions by States.** The chief law enforcement officer of the State in which the violation occurs may bring a civil action--

(1) to enjoin the violation; or

(2) to recover amounts for which the person is liable under section 32710 of this title for each person on whose behalf the action is brought.

6. Civil actions by private persons (49 U.S.C. § 32710).

a) Violation and amount of damages.

(1) Violates with intent to defraud.

(2) Liable for 3 times the actual damages or $1,500, whichever is greater.

(3) The court shall award costs and reasonable attorney's fees to prevailing consumers.

b) **Statute of Limitations.** The action must be brought not later than 2 years after the claim accrues. The claim "accrues" when the particular plaintiff (and not prior purchasers) has reason to know of the violation. *John Watson Chevrolet, Inc. v. Willis*,

890 F. Supp. 1004 (D. Utah 1995). *See also Ferris v. Haymore*, 967 F.2d 946 (4th Cir. 1992). Gordon v. Stickney, 2000 Del. Super. LEXIS 209 (Del. Super. Ct. May 11, 2000).

B. Lemon Laundering.

1. Defined: "the practice of manufacturers reselling cars returned to them as lemons, without informing the ultimate consumer buyer about the car's repair history." NCLC, CONSUMER WARRANTY LAW, § 15.7.3.1. (3d ed. 2006).

2. Even if the manufacture has repaired the defects, the cars will sell for more if the defect history is not disclosed.

3. Lemon Laundering is being conducted by manufactures on a wholesale basis. More recently manufactures will sell car to a dealer or wholesaler and disclose the defect and state the defect has been corrected. However, there are risks that the defect was not permanently fixed or could lead to other defects. There could also be several defects and the manufacturer only discloses one defect although their records have proof of all the defects.

4. Dealers also buy back the vehicle before it is required under their state law and call this a "goodwill" buy back and thus they never disclose the lemon history to the dealer.

5. State statutory protection. Most states have statutes governing this practice.

6. Statutes require disclosure of the prior history on the title or other sale documents. Some states mandate a warranty.

7. Under Magnuson Moss Warranty Act, subsequent buyer can generally enforce the original warranty despite the lack of horizontal privity.

8. Examining a vehicles title history can help undercover lemon laundering. A car returned to a manufacturer particularly during first 12,000 miles is usually a lemon (unless shot-term lease) or if in the first years sold back to original dealer. Try to locate original consumer if you are filing a suit.

9. If there is no lemon history on title than it is an expressed warranty that it is not a lemon buy back.

C. Salvage Vehicles. Similar to Lemon Laundering, selling rebuilt cars or vehicles assembled from salvaged parts, without disclosures, will often violate a specific state statute, the more general state UDAP statute, or amount to common law fraud.

IX. THE FTC USED CAR RULE

A. The FTC issued a trade practice rule, effective 9 May 1985, in an attempt to reduce oral misrepresentations, particularly with respect to warranty coverage. 16 C.F.R. Part 455.

B. While the rule does not require that used cars be sold with a warranty, it does require disclosure, through the use of a mandatory "Buyers Guide" window sticker, of the existence of any warranty coverage which does exist. *See Lawhorn v. Jospeh Toyota, Inc.*, 141 Ohio App. 153, 750 N.E.2d 610 (2001). The disclosure that the Buyer's Guide is incorporated into the contract must be conspicuously displayed and it is a violation of the rule if it is only included in the fine print boiler plate of the contract. The Guide MUST disclose:

1. Make, model, year, and VIN

2. Name & address of dealer (or other party who will accept complaints)

3. A warning that all promises from dealer should be in writing because spoken promises are hard to prove.

4. The meaning of the term "As Is"

5. Clear Disclosure of Warranty Coverage. Either

   a) AS-IS – NO WARRANTY

   b) WARRANTY

   c) IMPLIED WARRANTIES ONLY (If dealer chooses not to disclaim them or state law prohibits them from doing so.)

6. Availability of Service Contracts

7. A suggestion to the consumer to ask the dealer whether a pre-purchase independent inspection is permitted.

8. On the back, a list of the 14 major mechanical and safety systems of a car and a partial list of defects likely to occur within those systems in used cars.

C. Deceptive acts and practices.

1. Pursuant to the rule, it is a deceptive act or practice for a used car dealer to:

a) Misrepresent the mechanical condition of a used vehicle.

b) Misrepresent the terms of any warranty offered in connection with the sale of a used vehicle.

c) Represent that a used vehicle is sold with a warranty when the vehicle is sold without any warranty.

2. Pursuant to the rule, it is an unfair practice for a used car dealer to:

a) Fail to disclose, prior to sale, that a used vehicle is sold without any warranty.

b) Fail to make available, prior to sale, the terms of any written warranty offered in connection with the sale of a used vehicle.

3. No private right of action for FTC Rule violation, but:

a) Rule violations may be remedied using state UDAP statutes

b) Might argue violation of Rule is automatic violation of Magnuson-Moss Act, which authorizes private action for damages and attorney fees. See Currier v. Spencer, 299 Ark. 182, 772 S.W.2d 309 (1989). Trial court apparently awarded Magnuson-Moss attorney's fees for violation of FTC Used Car Rule. Arkansas Supreme Court, without discussing whether Magnuson-Moss Act can be used to challenge FTC Used Car Rule violations, affirmed trial court award.

X. STATE USED CAR "LEMON LAWS"

A. Some states have passed used car lemon laws. These states are currently:

1. Hawaii (Haw. Rev. Stat. §§ 481J-1 to 7).

2. New York (N.Y. Gen. Bus. Law § 198-b)(McKinney).

3. Rhode Island (R.I. Gen. Laws § 31-5.4).

4. Massachusetts (Mass. Gen. Laws. Ann. Ch. 90 § 7N ¼).

5. Minnesota (Minn. Stat. Ann. § 325F.662).

6. New Jersey (N.J. Rev. Stat. Ann. § 56:8-67 to 80 (West).

B. Most state lemon laws, although designed primarily to protect new car owners, also cover subsequent purchasers of warranted vehicles during the warranty period.

C. Most used car lemon laws only apply to "dealers."

1. A dealer is usually defined as one who has sold or offered to sell at least three vehicles in the prior twelve months.

2. This will usually include even unlicensed "backyard" dealers.

D. Basic Protections.

1. States that have a lemon law mandate certain warranty protections and specify the duration of the protection.

2. The duration is normally tied to the number of miles on the car at purchase.

3. Remedies. If the warranty is breached during the period the statutes provide that:

a) If the dealer is notified of the defect, AND

b) Fails to remedy the problem in a reasonable number of attempts; AND

c) The defect substantially impairs the value of the car; then

d) The dealer will accept return of the car and, at the consumer's option,

(1) replace it with a comparably priced vehicle OR

(2) Refund the purchase price less certain adjustment.

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CHAPTER 5

PROTECTIONS BASED UPON THE TYPE OF PAYMENT

(FEDERAL CONSUMER CREDIT PROTECTIONS)

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I. TRUTH IN LENDING ACT (TILA).

A. References.

1. Truth in Lending Act, 15 U.S.C. §§ 1601-1666j (2000).

2. Regulation Z, 12 C.F.R. Part 226.

3. Official Staff Commentary on Regulation Z (12 C.F.R. Part 226.101).

4. NATIONAL CONSUMER LAW CENTER, TRUTH IN LENDING (6th. ed. 2007 and Supp. 2008).

5. Alperin and Chase, Consumer Law: Sales Practices Credit Regulation, Vol. I & II, (West Pub. Co. 1986) with Supplements 2008-2009.

6. Credit Card Accountability, Responsibility, and Disclosure (CARD) Act of 2009.

B. Purpose.

1. Economic stabilization and competition is strengthened by informed use of credit by consumers.

a) TILA requires "meaningful disclosure of credit terms."

b) TILA also designed to protect consumer against inaccurate and unfair credit billing and credit card practices.

2. TILA is to be liberally construed in favor of consumers, with creditors who fail to comply with TILA in any respect becoming liable to the consumer regardless of the nature of violation or the creditor's intent.

3. Congress enacted TILA to ensure that consumers receive accurate information from creditors in a precise and uniform manner that allows them to compare the cost of credit.

4. The Act is in Title I of the Consumer Credit Protection Act and is implemented by the Federal Reserve Board via Regulation Z (12 C.F.R. Part 226).

a) The Regulation has effect and force of federal law. (*Gray-Taylor, Inc. v. Tennessee*, 587 S.W.2d 668 (Tex. 1979).

b) But see, *Porter v. Hill*, 838 P.2d 45 (Or. 1992) (While regulations promulgated by the FRB pursuant to its authority to construe provisions of TILA are not binding on courts, they are entitled to substantial deference, since agency has interpretive powers).

C. Method of Analysis.

1. Collect all documents related to the extension of credit.

a) Note or contract.

b) TIL disclosure statement.

c) Itemization of amount financed or HUD-1 statement.

d) Notice of right to rescind, if applicable.

2. Evaluate the accuracy of the numerical disclosures on their face.

3. Determine if the numerical disclosures were made IAW TILA.

4. Evaluate the adequacy of the non-numerical disclosures under TILA.

5. Determine if there is applicable state law and whether its provisions have been complied with.

D. Scope.

1. TILA applies to:

a) Each individual or business that offers or extends credit when four conditions are met:

(1) Credit offered or extended to consumers,

(2) Done "regularly" - extends credit more than 25 times (or more than 5 times for transactions secured by dwelling) per year,

(a) For example – If a person extends credit 26 times in 2002, he is a creditor for at least the 26th extension of credit in 2002 and for all of 2003.

(3) Subject to a finance charge or is payable by written agreement in more than 4 installments, and

(4) Primarily for personal, family, or household purposes.

(a) A person in whose name a credit card is issued is a customer under TILA even if the card was issued to an imposter.

b) If a credit card is involved, however, certain provisions apply even if the credit is not subject to a finance charge, is not payable by agreement in more than 4 installments, or if the credit card is used for business purposes. Also, certain requirements apply to persons who are not creditors but who provide applications for home equity plans to consumers.

2. TILA is inapplicable to:

a) Creditors who extend credit primarily for business, commercial, agricultural, or organizational purposes or other purposes that are otherwise regulated, such as securities brokers. TILA specifically exempts credit granted to "organization." *See Prifti v. PNC Bank*, 2001 WL 1198653 (E.D. Pa. Oct. 9, 2001) (corporations and organizations cannot be considered consumers regardless of the purposes for which credit was used)

b) The inclusion of the Holder in Due Course language required by the FTC is not sufficient, by itself to subject an assignee to liability. Pursuant to "§ 1641(a), assignees can be liable only for violations that are apparent on the face of the disclosure statement."

c) Student Loan Programs.

d) Credit transactions over $25,000.00, except those involving a security interest in real property, or in personal property used or expected to be used as the principal dwelling of the consumer.

e) Car dealerships who work with auto manufacturer financiers are "credit arrangers," not "creditors." *Riviere v. Banner Chevrolet, Inc.*, 158 F.3d 335 (5th Cir. 1998), *citing Ford Motor Credit Co. v. Cenance*, 452 U.S. 155, 101 S.Ct. 2239 (1981).

(1) The district court found that Banner was not a creditor under the current version of TILA: Banner does not meet the first condition that the individual or business must offer or extend credit. Although Banner has a credit department, it investigates credit histories, and it prepares forms; ultimately, Banner assigns the loan to GMAC, FMC, or another entity. It is that entity that "lends" the money to the consumer to enable him to purchase a vehicle. If a vehicle buyer defaulted on monthly payments, Banner would have no right to repossess the vehicle, or to sue for the balance unpaid. That right would belong to the lien holder or the extender of credit; GMAC is the sole lender/creditor in the transaction.

E. Electronic Disclosures.

1. The Electronic Signatures in Global and National Commerce Act, effective October 1st 2000, was enacted to validate electronic signatures, documents and disclosures. If the consumer consents under the act it overrides TILA's requirement that disclosures made in writing.

2. There is a potential for abuse in open-end transactions because there are ongoing disclosure requirements, for example periodic statements, change of terms of notices, annual billing statements. The creditor will want to get the consumer's approval to give these dislusures electronically in hope that the consumer will not see them or will just ignore them.

F. Material Disclosures Required.

1. Required disclosures must be made clearly and conspicuously, in meaningful sequence, in writing, and in a form the consumer may keep.

2. FRB promulgates model disclosure forms, but where they would be misleading, lenders should provide tailored notice consistent with TILA.

3. States also regulate credit disclosure:

    a) Check cashing companies.

        (1) *Virginia v Allstate Express Check Cashing, Inc.*, No. HC-44-1; *Virginia v Foremost Group, Inc.*,No. HC-1234-1; *Virginia v Ameracheck Corp.*, No. HC-1232-1 (Cir. Ct., Richmond Sep. 1993) - Check-cashing companies violated Virginia Consumer Finance Act by making short-term advances to customers who write personal checks in return for substantially smaller amounts of on-the-spot cash in transactions amounting to short term loans with annual percentage rates sometimes higher than 2,000%. (Cases cited in BNA Antitrust & Trade Reg. Daily (Oct. 7, 1993).

        (2) *Turner v. E-Z Check Cashing*, 35 F. Supp. 2d 1042 (M.D. Tenn. 1999) for a description of the mechanics of a check advancement loan; *White v. Check Holders, Inc.*, 996 S.W. 2d 496 (Ky. 1999)(holding check advancement transactions are loans for purposes of state usury laws); *Smith v. The Cash Store*, 295 F. 3d 325 (7th Cir. 1999)(applying TILA to check advancement loans).

        (3) The Federal Reserve Board commentary to Regulation Z makes it clear that TILA applies to cash advance in exchange for personal check, where parties agree either that the check will not be cashed or that the customer's deposit account will not be debited until a later date.

        (4) Attempts to get around TILA. Sometimes check cashing companies disguise their fees as payment for useless gift certificates or for advertisements. See *Henry v. Cash Today Inc*., 1999 F.R.D. 566 (S.D. Tex 2000). Check cashing companies also disguise their

fees as payment for useless internet access and very expensive phone cards.

b) Bounce protection plans.

(1) Banks promote aggressively and tell consumers they can pay back at their discretion, skirting the Truth in Lending Act because the transaction does not meet the requirement of requiring payment in more than 4 installments.

(2) Cover overdrafts up to certain limit.

(3) Charge bounced check fee $20-$35 each.

(4) Charge $2 to $5 a day until positive balance.

(5) Many times consumers do not affirmatively agree to these programs, instead the bank imposes coverage on all account holders as a "courtesy."

(6) Not given TILA disclosures which can be over 500% APR.

(7) Send consumer thank you notes for using the service.

(8) Bank computers are programmed to clear the largest checks first, a bank is able to bounce a larger number of smaller checks than it would if the smallest checks were cleared first.

c) Large ticket items.

(1) The deceptive use of open-end credit to finance large ticket items (such as satellite dishes) can be attacked under UDAP and fraud theories. *See Carlisle v. Whirlpool Fin. Nat'l Bank, Clearinghouse,* No. 52,516, Civil Action No. CV 97-068 (Circuit Court, Hale County, Ala., Post Trial Order, Aug. 25, 1999). A jury awarded $580 million, finding that the evidence revealed a malicious sale practice designed to target and take advantage of the poor, uneducated, elderly and African-American citizens. The lender structured the

loans as open ended making the payments last 8 years, instead of 36 months at $34 each, which the consumers thought was the arrangement.

d) Tax refund anticipation loans.

(1) *North Carolina Ass'n of Electronic Tax Filers v Graham*, 429 S.E.2d 544 (N.C. 1993) (North Carolina's Refund Anticipation Loan Act (N.C. Gen. Stat. §§ 53-245-254) which imposes registration and disclosure requirements on and otherwise regulates tax refund anticipation loans does not violate U.S. Constitution and was not preempted by federal tax and banking laws. State law ensured residents were fully informed as to difference between refund anticipation loan and simple electronic filing of returns and as to potentially high cost of refund loan.

(2) Texas Attorney General settled deceptive trade practices lawsuit with H&R Block, Inc. forcing tax return company to advertise its "Rapid Refund" program is actually a loan program charging customers up to 150% in annual interest. Filed as UDAP suit. [Case reported in National Association of Attorneys General Consumer Protection Report (Sep. 1993)]

(3) *Cades v. H. & R Block, Inc.*, 43 F.3d 869 (4th Cir. 1994), cert. Denied, 515 U.W. 1103 (1995); *Zawikowski v. Beneficial National Bank*, 1999 WL 35304 (N.D. Ill. 1999)(applying TILA to refund anticipation loan); *Affatato v. Beneficial Corp.*, 1998 WL 472404 (E.D.N.Y. 1998)(discussing timing of refund anticipation loan disclosures); *Basile v. H & R Black, Inc.*, 897 F. Supp. 194 (E.D. Pa. 1995). *State ex. Rel. Salazar v. The Cash Now Store*, 31 P. 3d. 161 (Colo. 2001) (rejecting lender's argument that a tax refund is not a loan).

(4) *But see Cullen v. Bragg*, 350 S.E.2d 798 (Ga. App. Ct. 1986) (holding TILA inapplicable to refund anticipation transactions because the consumer had no obligation to repay.

e) Pawn transactions / auto pawn

(1) *Burnett v. Ala Moana Pawn Shop*, 3 F.3d 1261 (9th Cir. 1993) (decision extensively discusses factors considered, including, e.g., fact that 75% of customers "repurchased" the goods; parties' intent; title to property did not pass until end of repurchase option period, which could be extended for a fee, which court held analogous to charging interest; "sales" prices related to amount customer needed, rather than fair market value of goods).

(2) *Pendleton v. American Title Brokers, Inc*., 754 F. Supp. 860 (S.D. Ala. 1991) (where the ad read, "Pawn your title, keep your car;" the borrower signed a "pawn ticket/loan" contract, repayable with interest in weekly installments and executed a leaseback of the automobile, to run concurrently with the loan repayment, for a weekly rental amount equal to 10% of the loan; also included a provision granting the creditor the right of repossession in the event of default. This was a credit transaction, therefore TILA applied and since the proper disclosures were not made, TILA was violated). Good example of a disguised credit sale. See also *Bumpus v. Vandeford*, Clearinghouse No. 54, 570, Civil Action No. 1:99 CV070-5AA (N.D. Miss. Mar. 27, 2002) (Loan was structured as a conditional sale with a right to rescind the sale upon payment of weekly "extension fees," weekly fees were 10% of loan amount.)

G. Open-end Credit Transactions.

1. Definition: Open-end credit includes bank and gas company credit cards, stores' revolving charge accounts, telephone credit cards, and cash-advance checking accounts.

a) Typical features: (12 C.F.R. § 226.2(a)(20)).

(1) Creditors reasonably expect the consumer to make repeated transactions.

(2) Creditors may impose finance charges on the unpaid balance.

(3) As the consumer pays the outstanding balance, the amount of credit is once again available to the consumer.

b) Required disclosures:

(1) Annual percentage rate including applicable variable-rate disclosures,

(a) Creditors must disclose each periodic rate that may be used to compute the finance charge on an outstanding balances, for cash advances, or balance transfer in 18-point type. When they use teaser rates or introductory rates they must disclose regular rate in at lest 18 point type.

(2) Method of determining finance charge and balance upon which finance charge imposed, as explained in 12 C.F.R. § 226.6,

(3) Amount or method of determining any membership or participation fees,

(4) Penalty rate and what triggers the penalty rate for example 22% if more than 60 days late,

(5) Grace period for purchases to avoid any finance charge if the consumer pays the debt before the grace period ends,

(6) Methods of computing the balance on which finance charges will be calculated to the purchases of goods and services,

(7) Any balance transfer fees,

(8) Security interests if applicable to transaction, and

(a) Most cards are unsecured but typically 3 ways to take collateral.

(i) Items purchased with card.

(ii) Secured by a bank deposit.

(iii) Home equity loan.

(9) Statement of billing rights.

c) Other requirements include furnishing consumer with a periodic statement of the account.

(1) 12 C.F.R. § 226.12 details special credit card provisions, including liability of cardholder and assertion of claims and defenses against card issuer (see Fair Credit Billing Act outline).

(2) 12 C.F.R. § 226.13 details billing error resolution (see Fair Credit Billing Act outline).

H. Closed-end Credit Transactions.

1. Definition: "other than open-end credit." Credit is advanced for a specific time period and, the amount financed, finance charge, and schedule of payments are "agreed upon" by the creditor and the consumer. (See 12 C.F.R. § 226.2(a)(10)).

2. Required disclosures:

a) Identity of the creditor,

b) Amount financed,

c) Itemization of amount financed,

d) Annual percentage rate, including applicable variable-rate disclosures,

e) Finance charge,

f) Total of payments,

g) Payment schedule,

h) Prepayment/late payment penalties, and,

i) If applicable to the transaction:

(1) Total sales cost,

(2) Demand feature,

(3) Security interest,

(4) Insurance,

(5) Required deposit, and

(6) Reference to contract.

I. Violations of TILA.

1. Creditors are liable for violation of the disclosure requirements, regardless of whether the consumer was harmed by the nondisclosure, **UNLESS**:

a) The creditor corrects the error within 60 days of discovery and prior to written suit or written notice from the consumer, or,

b) The error is the result of bona fide error. The creditor bears the burden of proving by a preponderance of the evidence that:

(1) The violation was unintentional.

(2) The error occurred notwithstanding compliance with procedures reasonably adapted to avoid such error (error of legal judgment with respect to creditor's TILA obligations not a bona fide error).

2. Civil remedies for failure to comply with TILA requirements:

a) Action in any U.S. district court or in any other competent court within one year from the date on which the violation occurred. This limitation does not apply when TILA violations

are asserted as a defense, set-off, or counterclaim, except as otherwise provided by state law.

b) Private remedies - applicable to violations of provisions regarding credit transactions, credit billing, and consumer leases.

(1) Actual damages in all cases.

(2) Attorneys' fees and court costs for successful enforcement and rescission actions.

(3) Statutory damages.

(a) Individual actions - double the correctly calculated finance charge. For closed end transactions secured by real property – not less than $200 or more than $ 2,000.

(b) Class actions - an amount allowed by the court with no required minimum recovery per class member to a maximum of $500,000 or 1% of the creditor's net worth, whichever is less.

(c) Can be imposed on creditors who fail to comply with specified TILA disclosure requirements, with the right of rescission, with the provisions concerning credit cards, or with the fair credit billing requirements.

c) Enforcement by administrative agencies.

(1) Who:

(a) Banks - Federal Reserve Board, the Federal Deposit Insurance Corporation, and other agencies.

(b) Others not subject to the authority of any specific enforcement agency - Federal Trade Commission.

(c) 9 separate agencies currently have enforcement responsibilities.

(2) What enforcement agencies can do:

(a) Issue cease and desist orders or hold hearings pursuant to which creditors are required to:

(i) Adjust debtors' accounts (15 U.S.C. § 1607(e)(4)(A), (B)) to ensure that the debtor is not required to pay a finance charge in excess of the finance charge actually disclosed or,

(ii) the dollar equivalent of the annual percentage rate actually disclosed, whichever is lower.

(b) If the FTC determines in a cease and desist proceeding against a particular individual or firm that a given practice is "unfair or deceptive," it may proceed against any <u>other</u> individual or firm for knowingly engaging in the forbidden practice, even if that entity was not involved in the previous proceeding.

3. Criminal penalties - Willful and knowing violations of TILA permit imposition of a fine of $5,000, imprisonment for up to 1 year, or both.

4. Rescind the contract (see below).

J. Truth In Lending Act Rescission Rights.

1. 3-Day Cooling Off Period (15 U.S.C. § 1635; 12 C.F.R. § 226.15).

2. General. In addition to remedies described above, consumers who enter into certain home equity loans may also have rescission rights as described below.

a) Under TILA, a consumer may rescind a consumer credit transaction involving a “non-purchase money” security interest in the consumer's principal dwelling;

(1) Within 3 business days (excludes Sunday and most Federal holidays) if all TILA disclosure requirements are met, or

(2) During an extended statutory period for TILA disclosure violations:

(a) Failure to give adequate notice of right to rescind, clearly and conspicuously in a form the consumer may keep.

(b) Failure to give adequate TILA credit term disclosures.

b) Rescission voids the security interest in the principal dwelling.

c) Consumer must have ownership interest in dwelling that is encumbered by creditor's security interest. Consumer need not be a signatory to the credit agreement.

d) TILA rescission rights do not apply to business credit transactions, even if secured by consumer's principal dwelling.

2. Scope of Rescission Rights (WHAT).

a. Applies to loan involving a <u>non-purchase money security interest</u> in consumer's principal residence (i.e., home equity loans/lines of credit/home improvement loans, etc.).

b. A consumer can have only <u>one</u> principal dwelling at a time. A vacation or other second home is not a principal dwelling. A transaction secured by a second home cannot be rescinded even if the consumer plans to reside there in the future.

3. Time to Exercise Right to Rescind.

a. Right to rescind until midnight of third business day following the later of:

(1) Consummation of transaction,

(a) In the case of closed-end credit, when the credit agreement is signed.

(b) In the case of open-end credit, the occurrence giving rise to the right to rescind.

(i) Opening the plan,

(ii) Each credit extension above previously established credit limit,

(iii) Increasing the credit limit,

(iv) Adding to an existing account a security interest in the consumer's principal dwelling, and

(v) Increasing the dollar amount of the security interest taken in the dwelling to secure the plan.

(2) Delivery of the required rescission right notice, or

(3) Delivery of all material disclosures.

b. Extended right to rescind.

(1) Continuing right to rescind if required disclosures not made or made incorrectly, but . . .

(2) Statutory cut-off of extended right to rescind at 3 years after consummation.

(3) Will be cut off earlier by transfer of all of the consumer's interest in the property (including involuntary transfer such as foreclosure), or sale of the property.

(4) Violations Giving Rise to An Extended 3-Year Right to Rescind.

(a) Failure to give proper rescission notice.

(b) Creditors are required to deliver two copies of the right to rescind to each consumer entitled to rescind.

(c) Notice must disclose the following:

(i) The retention or acquisition of a security interest in the consumer's principal dwelling,

(ii) The consumer's right to rescind,

(iii) How to exercise the right to rescind, with a form for that purpose, setting forth the creditor's business address,

(iv) The effects of rescission, and

(v) The date the rescission period expires. Sometimes there is an error with failure to fill in expiration date or if the closing is postponed and seller does not change notice.

(d) Proof of Delivery. Because there are such serious consequences for not giving proper disclosures, disputes arise over whether they were given. If debtor testifies that disclosures were not given then the creditor has the burden to produce some positive evidence (testimonial or documentary) that the disclosures were provided.

(5) Running of the 3-year time period for rescission extinguishes the right. *Beach v. Ocwen Federal Bank*, 523 U.S. 410, 118 S.Ct. 1408 (1998).

(a) "Three-year period for rescinding loan agreement under Truth-in-Lending Act (TILA) clearly precluded right of action after specified time; accordingly, it [3-yr time to rescind] was not a statute of limitation, and mortgagors could not assert right to rescind as recoupment defense

in foreclosure action brought by mortgagee more than three years after consummation of loan transaction."

(b) **"**[T]he filing of a lawsuit can be sufficient written notice of rescission under TILA so long as the complaint seeks rescission." *Jones v. Saxon Mortgage Incorporated*, 161 F.3d 2, 1998 WL 614150 (4th Cir.) (unpublished opinion).

(c) "[W]e hold that § 1635(f) is an absolute time limit and cannot be tolled to allow a party to rescind after a foreclosure sale." Id.

(i) Home Improvement Application. Consumer had a three-year extended right to rescind a home improvement contract where notices required by the TILA were not properly given by the third party financing company and where the work began prior to the completion of the rescission period. *Taylor v. Domestic Remodeling, Inc.*, 97 F.3d 96 (5th Cir. 1996).

4. Waiver of the Right to Rescind.

a. Consumers may modify or waive the right to rescind the credit transaction if extension of credit is needed to meet a bona fide personal financial emergency before end of rescission period. Waiver must be knowing and voluntary. *See Wiggins v. Avco Fin. Servs.*, 62 F. Supp. 2d 90 (D.D.C. 1999) (use of preprinted form to waive the right to rescind was a violation of the TILA)

b. Consumer must provide creditor with dated written statement describing emergency.

(1) Specifically modifying or waiving right, and

(2) Signed by all consumers entitled to rescind.

5. Delay of Performance.

a) Unless the rescission period has expired and the creditor is reasonably satisfied that the consumer has not rescinded, the creditor must not, either directly or through a third party,

(1) Disburse advances to the consumer or others,

(2) Begin performing services for the consumer, or

(3) Deliver materials to the consumer.

b) During the delay period, a creditor may:

(1) Prepare cash advance check (or loan check in the case of open-end credit),

(2) Perfect the security interest, and/or

(3) Accrue finance charges,

(4) In the case of open-end credit, prepare to discount or assign the contract to a third party.

c) Delay beyond rescission period.

(1) Creditor must wait until he/she is reasonably satisfied consumer has not rescinded.

(2) May do this by:

(a) Waiting reasonable time after expiration of period to allow for mail delivery, or

(b) Obtaining written statement from all eligible consumers that right not exercised.

6. Mechanics of Rescission Process.

a) Consumer sends or delivers written notice to creditor.

b) When consumer rescinds, the security interest becomes void and consumer is not liable for any amount, including finance charges.

(1) Within 20 calendar days after receiving notice of rescission, creditor must:

(a) Return any property or money given to anyone in connection with the transaction,

(b) Take whatever steps necessary to reflect termination of the security interest.

(2) When creditor meets its obligations, consumer must tender the money or property to creditor, or if tender not practicable, it's reasonable value.

(3) If creditor fails to take possession of tendered money or property within 20 days, consumer may keep it without further obligation.

c) Court may modify procedures.

(1) Court has power to exercise equitable discretion and condition rescission of a loan upon the return of the loan proceeds.

(2) *See Family Financial Services v. Spencer*, 677 A.2d 479 (Conn. App. 1996) (creditor's failure to honor the rescission nullified the security interest, barring foreclosure, and the consumer was not required to tender back the proceeds).

(3) *See Reynolds v. D & N Bank*, 792 F. Supp. 1035 (E.D. Mich. 1992). Consumer canceled home improvement contract 14 months after signed; 4 TILA violations; creditor failed to respond (did not return money or cancel security interest); consumer sued to enforce rescission, obtain damages, and keep value of property purchased rather than tender it to creditor. Court gave creditor 20 days to comply with its obligations, which creditor then failed to do. Court, in unreported opinion, then granted consumer's request. Creditor blew second

chance! (See NCLC Reports, Vol. 11, March/April 1993).

7. Particular Types of Transactions.

a) Refinancing and Consolidation.

(1) Rescission rights **do not** apply to refinancing or consolidation by same creditor of an extension of credit already secured by consumer's principal dwelling.

(2) Rescission rights **do** apply to extent new amount exceeds unpaid balance, any earned unpaid finance charges on existing debt, and amounts attributed solely to costs of refinancing or consolidation.

b) Open-end line of credit secured by home used to pay off loan **not** originally secured by home requires complete rescission rights.

c) Door-to-door sales.

(1) When home solicitation sale is financed with second mortgage loan, consumer may be entitled to two separate rights to cancel when the transactions are independent.

(2) When consumer offers to obtain his/her own financing independent of assistance or referral from seller, sale and financing are separate transactions.

(3) When there are separate transactions,

(a) FTC Rule (Cooling Off Period for Door-to-Door Sales) applies.

(b) TILA requires 3-day rescission period (unless extended for TILA violation).

(c) Seller bound by consumer's timely cancellation regardless of which party receives notice of cancellation.

(4) For single transactions (seller arranged financing), look to state home solicitation law to determine whether transaction still covered by state's home solicitations statute 3-day cooling off period.

(a) When seller finances or arranges financing with second mortgage, this is considered a single transaction.

(b) When there is a single transaction, TILA rescission rights apply, but not FTC Rule 3-day cooling off period.

(i) FTC Rule does not apply to transactions in which there are a TILA right to rescind (i.e., second home mortgage transactions).

(ii) Therefore, consumer has only TILA right to rescind and not the 3-day cooling off period rights under FTC Rule.

(c) <u>But</u>, state cooling off periods may apply even when TILA rescission rights are available. If there is a state statute that is not inconsistent with TILA, both must be complied with.

8. Post-consummation events do not trigger additional TILA disclosure requirements.

a) *Begala v. PNC Bank, Ohio, National Association*, 163 F.3d 948 (6th Cir., 1998).[U]nder TILA, a creditor's principal disclosure obligations arise before the credit transaction is consummated. In closed-end transactions . . ., the required disclosures under TILA are to be made as of the time that credit is extended, 15 U.S.C. § 1638(b), and it is as of that time that the adequacy and accuracy of the disclosures are measured.

9. Statute of Limitations.

a) The TILA 1-year statute of limitations for filing civil actions is NOT jurisdictional. Therefore it is subject to equitable tolling.

b) *Ramadan v. The Chase Manhattan Corporation*, 156 F.3d 499 (3d Cir. 1998). The purpose underlying TILA is "to assure meaningful disclosure of credit terms ... and to protect the consumer against inaccurate and unfair" practices. 15 U.S.C. § 1601. Thus Congress enacted TILA to guard against the danger of unscrupulous lenders taking advantage of consumers through fraudulent or otherwise confusing practices. As the Burnett Court noted, the main inquiry is whether allowing tolling of the statute of limitations is consistent with this policy. We believe that it is.

c) *Ellis v. General Motors Acceptance Corporation*, 160 F.3d 703 (11th Cir. 1998). "Equitable tolling" is the doctrine under which plaintiffs may sue after the statutory time period has expired if they have been prevented from doing so due to inequitable circumstances. The issue of whether TILA is subject to equitable tolling is one of first impression in this circuit. Every other circuit that has considered the issue has held that TILA is subject to equitable tolling. In this case, we examine TILA, a consumer protection statute which . . . is remedial in nature and therefore must be construed liberally in order to best serve Congress' intent. [W]e apply the general rule that equitable tolling applies to all federal statutes unless the statute states otherwise. We therefore agree with the Third, Sixth, and Ninth Circuits that the statute of limitations in TILA is subject to equitable tolling.

K. Reverse Mortgages. 15 U.S.C. § 1648, 12 C.F.R. § 226.33

1. Consumer agrees to mortgage property to bank in return for payments from lender. At death, transfer, or the consumer ceasing to occupy the property as a principal dwelling, the lender assumes full ownership in fee of the property.

2. Reverse mortgage loans are becoming more widely available for elders so they can tap home equity into their property without a repayment requirement while they continue to live in the home

3. Regulation under the TILA.

a) Disclosure to the consumer of the following information:

(1) Calculate the APR using three different appreciation models for three different credit models. The credit

models include a conventional short-term mortgage, a mortgage with a term equal to the actuarial life expectancy of the mortgagor and a third method determined by the Federal Reserve Board.

(2) That the consumer is granting a security interest in the home.

(3) A number of other specific disclosures

b) All disclosures must be made no less than 3 days before the loan closing.

4. Don't Forget Preventive Law to Your Retiree Population.

L. High Cost Mortgages under TILA Home Ownership and Equity Protection Act (HOEPA)15 U.S.C. § 1639, 12 C.F.R. § 226.32.

1. Applicability. The act applies to a closed end credit transaction secured by the consumer's principal residence if:

a) Mortgages with an interest rate 10 percentage points higher than the federal treasury securities of comparable term, or

b) In which the closing cost exceeds $441.00 or 10% of the loans value. The points and fees paid by the consumer exceed the greater of 8% of the loan amount or $465.00. This amount is updated annually based upon the CPI.

c) Does NOT apply to:

(1) Residential mortgages (initial purchase or construction)

(2) Reverse mortgages as defined above

(3) Open-end credit

2. The Section Mandates Certain Disclosures.

a) The CFR mandates a verbatim statement in the notices:

"You are not required to complete this agreement merely because you have received these disclosures or have signed a loan application. If you obtain this loan, the lender will have a mortgage on your home. You could lose your home, and any money you have put into it, if you do not meet your obligations under the loan."

b) Must be given three days before closing.

c) Must be conspicuous and in a certain type size. 15 U.S.C. § 1639(a)(1).

3. Restrictions.

a) No negative amortization. A situation where the amount financed actually increases over time because each monthly payment is less than the interest, which accrued each month.

b) Limits the inclusion of a prepayment penalty in the loan terms.

c) May not include a term, which increases the interest rate in the event of default.

d) Lender may not engage in lending without regard to the borrower's ability to pay.

e) Home Improvement Contracts are limited.

M. Home Equity Lines of Credit (HELCs).

1. Home Equity Loan Consumer Protection Act, passed in 1988, amended TILA to require disclosure of certain information earlier than is required for most open-ended credit transactions. The Act applies to HELC plans entered into after 7 November 1989.

2. HELC rules apply to open-end credit plans secured by the consumer's "principal dwelling." The definition of "principal dwelling" under HELC is more expansive than under TILA. Under HELC, the rules apply to consumer's second or vacation home, as well.

3. Disclosures required at time of application.

a) Disclosures.

(1) Consumer should keep a copy of the disclosures.

(2) Right to obtain a refund of fees if terms change and they decide not to enter into the contract.

(3) They risk the loss of the dwelling in the event of default.

(4) Creditor may terminate a plan or suspend future advances under certain circumstances.

b) Disclosure required at plan opening.

(1) Conditions under which the creditor may terminate the plan or change its terms.

(2) Payment terms of the plan.

(3) Negative amortization.

(4) Transaction requirements.

(5) Tax implications.

(6) Fact that APR does not include costs other than interest.

(7) Example showing how long it would take to repay a hypothetical balance of $10,000 if only making minimum payments.

(8) Variable-rate disclosures, including the "worst case" scenario.

4. In addition to disclosure mandates, there are substantive limitations that apply to the draw period of a HELC, the repayment period, and any renewal or modification of the HELC agreement.

a) Creditors may not terminate a HELC and accelerate payment of the outstanding balance before the scheduled expiration of the HELC plan, unless

(1) Consumer fraud or material misrepresentation in connection with the plan.

(2) Consumer has failed to meet the repayment terms of the agreement.

(3) Consumer action or inaction that adversely affects the creditor's security for the HELC.

b) A creditor may not unilaterally change the terms of an HELC plan after the account has been opened, unless

(1) The contract contained the change contemplated on the occurrence of an event, or

(2) Consumer expressly agrees in writing to the change.

(3) (3) In a variable-rate HELC, the index and margin used under the plan may be changed if the original index becomes unavailable, or

(4) The change unequivocally benefits the consumer or is insignificant.

5. Remedies. TILA remedies are available for most violations of HELC.

N. Credit Card Accountability, Responsibility, and Disclosure (CARD) Act of 2009

1. On 22 May 2009, the President signed H.R. 627, the "Credit Card Accountability, Responsibility, and Disclosure Act of 2009," otherwiseknown by the clever acronym the "CARD Act." This Act has now been codified as Public Law 111-24 and amends parts of TILA.

2. This Act was designed to curb some of the more controversial business practices used by many of the major credit card companies in the United States. Some of the most significant changes are detailed

below. While the Act will not be fully implemented until early 2010, many credit card companies are already adjusting their policies to comply with the CARD Act. The new law will:

a) prohibit arbitrary interest-rate increases;

b) restrict additional fees charged by credit card companies;

c) create additional rules on the payment of credit-card debts;

d) restrict the opening of credit accounts to consumers under 21 by requiring a parent or guardian as a co-signer, or requiring the minor applicant to show an independent source of income, to repay his/her credit obligations; and

e) mandate that merchant gift cards be valid for a period of at least 5 years from the date of purchase, and sharply restricts the use of inactivity fees by requiring notice and a minimum dormancy period of one year

II. FAIR CREDIT BILLING ACT (FCBA) & ELECTRONIC FUNDS TRANSFER ACT

A. References.

1. Fair Credit Billing Act, 15 U.S.C. § 1601 et. seq. (2000).

2. 15 U.S.C. § 1666

3. 12 C.F.R. § 226.13

4. Electronic Funds Transfer Act, 15 U.S.C. § 1693 (2000).

5. 12 C.F.R. Part 205.

6. NATIONAL CONSUMER LAW CENTER, TRUTH IN LENDING (6th ed. 2007 and Supp. 2008).

7. NATIONAL CONSUMER LAW CENTER, CONSUMER BANKING AND PAYMENT LAWS (3d ed. 2005 and Supp. 2008).

B. Introduction. The two referenced acts provide similar types of protections to different types of transactions. Consequently, we will look at them side-by-side in the table below.

C. The Basics.

	Fair Credit Billing Act	Electronic Fund Transfer Act
Applicability	✓ Open-end consumer credit transactions (i.e., credit cards, store charge accounts, telephone charge cards).	✓ Electronic Transfer: Any transfer of funds, other than a transaction by check, draft, or similar paper instrument, that is initiated through an electronic terminal, telephone, or computer or magnetic tape for the purpose of ordering, instructing, or authorizing a financial institution t**o debit or credit an account**. ✓ The term includes, but is not limited to: ❑ Point of sale transfers, ❑ ATM transfers, ❑ Direct deposit or withdrawal of funds, and ❑ Transfers initiated by telephone. ❑ The term includes all transfers resulting from debit card transactions. ❑ Applies to direct deposit ❑ A simple telephone call may be covered ✓ The Act does not apply to the following: ❑ Check guarantee or authorization services that do not result directly in a debit or credit to consumer's account. ❑ Wire transfers used primarily for transfers between financial institutions or businesses. ❑ Certain automatic transfers, ❑ Between consumer's accounts within the institution, ❑ Into a consumer's account by the institution, such as the crediting of interest, ❑ From a consumer's account to an account of a family member whose account is within the same institution. ❑ Certain telephone-initiated transfers that are, ▪ Initiated by telephone conversation between consumer and employee of institution, and ▪ Are not under a telephone bill-paying or other prearranged plan or agreement in which periodic transfers are contemplated. ❑ Transactions with a stock brokerage (Institutions regulated by the Securities and

	Fair Credit Billing Act	Electronic Fund Transfer Act
		Exchange Commission Act).
Billing Errors (Defined)	✓ Bills for transactions that never occurred. ✓ Transactions by unauthorized people. ✓ Bills for erroneous amounts. ✓ Bills for goods/services that were not delivered or were not accepted. ✓ Failure to credit account properly. ✓ Computation errors. ✓ Bills sent to incorrect addresses, provided that the creditor received notice of the change of address at least 20 days before the end of the billing cycle for which the statement was sent out.	✓ An unauthorized electronic fund transfer, ✓ An incorrect electronic fund transfer to or from consumer's account, ✓ Omission from a periodic statement of an electronic fund transfer to or from consumer's account that should have been included, ✓ Computational or bookkeeping error made by financial institution relating to an electronic transfer, ✓ Consumer's receipt of an incorrect amount of money from an electronic terminal, ✓ An electronic fund transfer not identified in accordance with regulations, or, ✓ A consumer's request for any documentation required to be given by the financial institution, or additional clarification concerning an electronic transfer. Does not include routine inquiry about the balance of account.
Billing Error Procedure (Consumer)	✓ Consumer notifies card issuer IN WRITING w/i 60 calendar days of transmittal of periodic statement to the consumer. ❑ If the error was failure to transmit the billing statement, then the 60 days runs from the time when the creditor should have sent it. ❑ If the error is failure to credit a payment, 60 days begins to run when the credit should have appeared on the statement. ✓ The consumer's billing error notice must include: ❑ Sufficient information to enable the creditor to identify the consumer and his/her account number and, ❑ To understand the nature of the complaint. ✓ The creditor must disclose on the billing rights statement or on the periodic statement an address for billing error inquiries. The notice must be received at that place for notice to be effective. ✓ After the consumer gives notice, he/she may withhold payment of the disputed amount or pay the amount without waiving billing error rights. ❑ However, paying the disputed amount does waive assertion of claims and defenses against a credit card issuer.	✓ In order to limit liability, the consumer must furnish to the financial institution **WRITTEN OR ORAL** notice of the error within 60 days of the erroneous statement's transmittal. Notice should include: ❑ Consumer's name and account number. ❑ Consumer's belief that an error exists and the amount of the error. ❑ The reasons for the consumer's belief. ❑ Consumer must also allege unauthorized use. Can not just say it is loss or stolen (This is according to an FRB official staff interpretation and seems to be unsupported by the act.)

	Fair Credit Billing Act	Electronic Fund Transfer Act
Billing Error Procedure (Card/Access Device Issuer)	✓ Creditor must conduct a reasonable investigation, unless creditor corrects the account as requested or the consumer withdraws the complaint. ✓ Creditor shall mail or deliver written acknowledgment of the complaint to the consumer within 30 days of receiving a billing error notice, unless the creditor has complied with appropriate resolution procedures within that 30-day period. ✓ The creditor must comply with the resolution procedures within two billing cycles (but in no event, later than 90 days) after the creditor's receipt of the debtor's notice of error. ✓ If creditor determines that error has occurred, creditor shall, within the time limits above: ❑ Correct the error and credit the consumer's account with any disputed amount and associated finance charges, and, ❑ Mail or deliver a correction notice to consumer. ❑ Report to resolution to each credit agency notified of the delinquency. ✓ If, after conducting investigation, creditor determines no billing error occurred or that a different error occurred from that asserted, the creditor shall, within time limits above: ❑ Mail or deliver to consumer an explanation setting forth reasons creditor believes alleged error is incorrect in whole or part. ❑ Furnish copies of documentary evidence of consumer's indebtedness, if consumer so requests. ✓ If a different billing error occurred, correct the error and credit the consumer's account. ✓ Until the billing error is resolved under the FCBA procedures, creditors may not: ❑ Take any action to collect the amount in dispute. ❑ If the consumer keeps a deposit account with the creditor and has direct payment deducted automatically, the creditor may not deduct any part of the disputed amount or related finance charges if the notice of error is received any time up to 3 business days before the scheduled payment date.	✓ Upon notification: ❑ The institution has 10 business days (20 days if the consumer is overseas) to investigate and report the results of the investigation to the consumer. ❑ The institution, at its option, may extend the report period by provisionally re-crediting the account within 10 business days of the consumer's notice. Re-crediting gives the bank 45 days (90 days if the consumer is overseas) to investigate and report the results of the investigation to the consumer. ✓ Following completion of the investigation, the institution shall: ❑ Correct any errors within 1 business day. ❑ If no errors are found, so notify the consumer within 3 business days of end of investigation and forward copies of all documents relied upon if requested by the consumer. ❑ If there was no error discovered, and upon debiting a provisionally recredited amount, the financial institution shall orally report or mail notice to consumer of date and amount of debiting and fact they will honor checks, drafts, or similar paper instruments to 3d parties and preauthorized transfers from consumer's account for 5 business days after transmittal of notice. ❑ Institution need only honor items that it would have paid if the provisionally recredited funds had not been debited.

	Fair Credit Billing Act	Electronic Fund Transfer Act
	❑ Restrict or close the account in issue based on the debtor's failure to pay the disputed amount. ❑ Report or threaten to report adversely on the debtor's credit rating based on the disputed amount. ✓ Creditor **may** ❑ seek collection of unpaid, undisputed amounts. ❑ decrease credit limit by amount in dispute. ✓ If, after the creditor follows resolution procedures, and the consumer still claims there is an error, the creditor may report the delinquency to a credit reporting agency provided: ❑ Creditor also reports that the amount is in dispute. ❑ Mails or delivers to consumer the name and address of each person to whom creditor made the report, and, ❑ Promptly reports any subsequent resolution of reported delinquency to all persons to whom creditor made the report. ✓ A creditor who has fully complied with FCBA procedures is under no further responsibilities if consumer reasserts same billing error.	
Unauthorized Use (Definition)	Use with no actual, implied, or apparent authority from the cardholder. (Question of State Law) ✓ Not Unauthorized Use: ❑ Attempt to orally limit spending. *See, e.g., Martin v. American Express, Inc.*, 361 So.2d 597 (Ala. Civ. App. 1978). ❑ Use of card by authorized person for unauthorized purpose. *Master Card v. Town of Newport*, 396 N.W. 2d 345 (Wis. 1986). ▪ Letter to credit card issuer to limit credit limit did not shield cardholder from liability for excess charges by an apparently authorized person. *Id.* ▪ State law imposes no duty on issuer to mitigate despite cardholder notification that an authorized user is making unauthorized charges. *American Express v. Web*, 261 Ga. 480, 405 S.E.2d 652 (1991). ▪ But see *Standard Oil Co. v. Steel,*	✓ An electronic fund transfer from a consumer's account initiated by a person other than the consumer without **actual authority** to initiate the transfer **and** from which the consumer receives no benefit. ✓ Does not include: ❑ Transfers initiated by one furnished with the access device to the consumer's account by the consumer, unless the consumer has notified the financial institution involved that the transfers by that person are no longer authorized. ❑ Transfers initiated with fraudulent intent by the consumer or a person acting in concert with the consumer. ❑ Transfers initiated by the financial institution or its employees.

	Fair Credit Billing Act	Electronic Fund Transfer Act
	489 N.E. 2d 842 (Ohio Misc. 1985). Cardholder who voluntarily gave her card to a friend liable for all charges friend made before she notified card issuer of unauthorized use, but not for charges made after notification. ❑ *Society National Bank v. Kienzle*, 463 N.E.2d 1261 (OH App. 1983). The Court held that a husband's liability for his estranged wife's use of his credit card was limited by the FCBA to $50. The wife was never an authorized cardholder on the account and had apparently stolen the card. ❑ *See also Universal Bank v. McCafferty*, 88 Ohio App. 3d 556, 624 N.E.2d 258 (1993). Cardholder had issuer send card to friend's address so his wife would not find out about card. Friend kept card and used it. Court held consumer liable for only up to $50 of friend's charges. State law determines whether the use is authorized or unauthorized.	
Unauthorized Use (Conditions for Liability)	✓ A cardholder is liable for unauthorized use only if: ❑ The card is an accepted credit card (by the consumer), ❑ The liability is not in excess of $50.00, ❑ The card issuer gives the cardholder: ▪ adequate notice of the potential liability, ▪ a description of the means to notify the card issuer of the loss or theft of the card, ▪ a method whereby the user of the card can be identified as the person authorized to use it. ❑ The unauthorized use occurs before the consumer notifies the card issuer that an unauthorized use of the credit card has occurred or may occur as the result of loss, theft, or otherwise. ✓ Except as provided above, the cardholder incurs no liability from the unauthorized use of a credit card.	✓ A consumer is liable for any unauthorized electronic fund transfer only if: ❑ The card or other means of access utilized for such transfer was an accepted card or other means of access, and ❑ if the issuer of such card, code, or other means of access has provided a means whereby the user of such card, code, or other means of access can be identified as the person authorized to use it, such as by signature, photograph, or fingerprint or by electronic or mechanical confirmation. ✓ Restriction on liability. ❑ The EFTA imposes no liability upon a consumer for an unauthorized electronic fund transfer in excess of his liability for such a transfer under other applicable law or under any agreement with the consumer's financial institution. ❑ Except as provided in the EFTA, a consumer incurs no liability from an unauthorized electronic fund transfer.
Liability for Unauthorized Use	✓ $50 maximum ✓ In action to enforce liability, the burden of proof is upon the card issuer to show: ❑ that the use was authorized or,	✓ Three-Tiered Liability ❑ Maximum liability of $50 if the consumer reports the loss or theft of the debit card within 2 business days of discovering the

	Fair Credit Billing Act	Electronic Fund Transfer Act
	❑ if the use was not authorized, then issuer must show the conditions of liability have been met.	loss/theft. ❑ Maximum liability of $500 if consumer fails to notify institution within 2 business days and institution can show it could have stopped the unauthorized use if it had been notified. ❑ If consumer fails to report within 60 calendar days of transmittal of the periodic statement and institution can show it could have stopped the unauthorized use if it had been notified, consumer is liable for: • Up to $500 for the period between the discovery of the loss and 60 calendar days (like #2 above) to be calculated as follows: ➢ $50 maximum for transactions made during the first 2 business days, PLUS ➢ The amount of unauthorized transfers made between 2 business days and 60 calendar days from transmittal of the periodic statement up to the $500 maximum. (For example, if the consumer was liable for $50 of a $100 dollar transfer on business day 1, liability would be limited to $450 for the transfers after day 2 and out to the 60th day from transmittal of the statement.) • PLUS Unlimited liability for all unauthorized transfers made more than 60 calendar days following the transmittal of the periodic statement. ✓ The consumer **cannot waive** these limitations or any other protections provided by the Act. ✓ Financial institutions **cannot attempt to circumvent** the Act's protections by adding "fault" language in ATM agreements. ✓ For example, the financial institution MAY NOT try to limit its liability if the consumer is negligent in co-locating the ATM card with the PIN number and both are stolen and used.
Other Provisions	✓ Some claims & defenses that you have against the merchant may be asserted against the credit card issuer IF: ❑ The consumer has made a good faith effort to resolve the problem with the **merchant** honoring the card; ❑ The merchant is not controlled by or the same as the card issuer (e.g. Sears or J.C.	✓ Issuance of Access Devices. ❑ "Access device" means a card, code, or other means of access to a consumer's account. ❑ Financial institutions may only issue access devices to consumers, • In response to an oral or written request or application, or

	Fair Credit Billing Act	Electronic Fund Transfer Act
	Penney - store card) ❑ The contract is entered into w/i 100 miles or within the same state as billing address, and ❑ The contract is for >$50 ✓ Claims and defenses may include: ❑ Unauthorized use of the card, ❑ Dispute as to quality of merchandise. ❑ Nondelivery of goods, ❑ Claims that can be asserted under the billing error resolution procedures. ✓ Location of transaction ❑ A matter of state law; states differ on whether mail or telephone order occurred at consumer's home or seller's place of business. ❑ *See Lincoln First Bank v. Carlson*, 426 N.Y.2d 433, 103 Misc.2d 467 (1980) (no presumption that consumer gives up all defenses if transaction takes place at distance greater than 100 miles). . ✓ Once the criteria have been met, the consumer may withhold payment of the disputed amount to the extent of the credit outstanding on that transaction and any finance charges attributable thereto. ✓ Payment of the disputed amount waives right to assert claims or defense as to the card issuer. ✓ If only part of a single transaction is disputed (i.e., multiple purchases at the same time), payments shall be prorated according to prices and applicable taxes. ✓ Relationship to Billing Error Resolution procedures. ❑ Even though certain merchandise disputes, such as nondelivery of goods, may also constitute "billing errors," the protections operate independently. For example: ▪ A cardholder that asserts billing error involving undelivered goods may institute error-resolution procedures, but whether or not the card issuer has done so, the cardholder may assert claims or defenses, as well. ▪ Conversely, the consumer may pay a	• As a renewal of, or substitute for, an accepted access device. ❑ **Except**, may distribute access device to consumer on unsolicited basis if: • Access device is not validated, • Distribution is accompanied by ➢ A complete disclosure of consumer's rights and liabilities that will apply if device is validated, ➢ A clear explanation that access device is not validated and how consumer may dispose of it if validation not desired, and ➢ Access device is validated only in response to consumer's oral or written request or application and after verification of consumer's identity by any reasonable means such as photo, fingerprints, personal visit, or signature comparison. ✓ Access device considered validated when financial institution has performed all procedures necessary to enable consumer to use it to initiate an electronic transfer. ✓ Pre-Authorized Transfers From Consumer's Account - Consumer's Right To Stop Payment. ❑ Consumer must notify financial institution orally or in writing at any time up to 3 business days before the scheduled day of transfer. ❑ Financial institution may require written confirmation of the stop-payment order to be made within 14 days of an oral notification is made if, the requirement is disclosed to consumer along with address to which confirmation should be sent. ❑ If consumer does not provide written confirmation, stop-payment order ceases to be binding 14 days after it has been made.

	Fair Credit Billing Act	Electronic Fund Transfer Act
	disputed balance and thus have no further right to assert claims or defense, but still may be able to assert a billing error if notice of the error is given in the proper time and manner. ✓ State statutes may be more favorable to consumers. See Mass. G.L.A. c. 255, § 12F, which makes credit card issuers subject to all defenses a consumer may have arising from a sale or lease transaction without any condition or limitation.	
Remedies	✓ Because the FCBA is part of TILA, it carries the same remedies as TILA, except that the remedy of rescission is not available for failure to comply with billing requirements. 15 U.S.C. § 1640. ✓ In addition to the remedies available for TILA violations, if the creditor violates the billing error resolution procedures, the consumer recovers from creditor the disputed amount and any finance charges thereon up to $50. 15 U.S.C. § 1666(e). ✓ Also, consider UDAP action.	✓ Actual damages. ✓ Statutory damages of $100 to $1,000. ✓ Court costs and reasonable attorney's fees. ✓ Criminal penalties of up to 1 year's imprisonment and a $5,000 fine for knowing and willful noncompliance. ✓ Criminal penalties of up to 10 years' imprisonment and a $10,000 fine for violations affecting interstate or foreign commerce. ✓ Treble damages (3 times the consumer's actual damages) if: ❑ The account is not properly provisionally recredited. ❑ The institution fails to conduct a good faith investigation. ❑ The institution knowingly and willfully concludes that no error exists contrary to the available evidence.

D. Fair Credit Billing Act Cases.

1. Cardholders cannot ignore their statements! *Minskoff v. American Express Travel Related Services Company, Inc.*, 98 F.3d 703 (2d Cir. 1996). (1) [Company] president was not accountable for assistant's initial possession of fraudulently obtained corporate credit cards, but (2) president was liable for purchases assistant made after credit card statements were issued.

2. Credit Card Issuer May Have to Police Participating Merchants. *Citicorp Credit Services, Inc.*, FTC File No. 892 3033 (Nov. 10, 1992)(consent order). Credit card issuer continued to process credit card sales when it knew or should have known that seller engaged in deceptive sales practices (UDAP case).

a) Consent order said that Citicorp should have known about fraud by merchant due to high volume of consumer complaints, ongoing government investigations, and 25% charge-back rate (about 20 times national average). "Charge-back" is where credit charge removed from consumer's account and charged back to merchant.

b) Consent order included ways Citicorp could investigate a merchant, including reviewing merchant's advertising, sales scripts, promotional materials, goods and services offered, and truth of claims being made.

c) NCLC suggests that case provides a third remedy for defrauded consumers (in addition to claims and defenses and error resolution procedures under FCBA discussed above): "That a card issuer is liable under a UDAP statute for aiding and abetting a deceptive scheme by not adequately investigating the merchant."

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CHAPTER 6

THE DOWNSTREAM CONSEQUENCES OF USING CONSUMER CREDIT

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CHAPTER 6

THE DOWNSTREAM CONSEQUENCES OF USING CONSUMER CREDIT

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A. References.

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2. State Debt Collection Statutes. See Appendix B.

3. Federal Trade Commission Staff Commentary to FDCPA (non-binding).

4. NATIONAL CONSUMER LAW CENTER, FAIR DEBT COLLECTION (5th ed. 2004 and Supp. 2006).

B. Overview of the Debt Collection Process.

1. Creditors (those to whom the debt is owed) begin collection efforts with a series of form letters, graduate to phone calls or personal visits, then to repossession or referral to a collection agency or lawyer for suit.

a) Initial contacts usually consist of friendly "reminder" letters.

b) Subsequent letters request the consumer call to discuss the problem and suggest that nonpayment is serious.

(1) Phone calls may serve the legitimate purposes of determining why payments are late and resolving misunderstandings and disputes.

(2) Calls may be used illegally to harass the consumer in attempts to collect debt from a distressed consumer.

c) When payments are 30 to 60 days late, the creditor generally threatens to repossess collateral or foreclose on a mortgage.

2. At any stage of the process, the creditor may forgive the debt ("write off") either because the debt is obviously not collectible or because the creditor has internal rules that limit collection efforts in favor of favorable tax treatment.

3. The creditor may turn the account over to a lawyer or debt collector (one in the business of collecting debts for others).

   a) A lawyer may simply send or furnish creditor with dunning letter or series of letters for flat fee or pursuant to retainer. Lawyer may also be retained to initiate legal action, usually contingency fee, retaining portion of amount collected (i.e., 30-50%).

   b) Collection Agency may be retained for flat fee or retainer.

      (1) Many times, 50% contingency.

      (2) Seldom do collection agencies bother to get all documents related to debt from creditor -rather, they get name, address of consumer, and amount of debt.

      (3) Collection agencies must comply with the Fair Debt Collection Practices Act.

C. Fair Debt Collection Practices Act (FDCPA).

1. Purpose. Congress passed the FDCPA in 1982 in response to the abusive practices of debt collectors. The purposes of the statute are:

   a) To eliminate abusive debt collection practices.

   b) To ensure that those collectors who refrain from using abusive debt collection practices are not competitively disadvantaged.

   c) To promote consistent state action to protect consumers against debt collection abuses.

2. The FDCPA is found in Title VIII of the Consumer Credit Protection Act. The FTC interprets the FDCPA via non-binding interpretive commentaries.

3. Federal Trade Commission Formal Advisory Opinion in 2000. The advisory opinion to the American Collectors Association addressed two issues:

   a) Collectors may undertake collection activities during the thirty-day period during which a consumer may request the collector to validate debt as long as the collection activities do not over shadow or are not inconsistent with the notice of validation rights.

   b) FDCPA does not preempt state laws that do not allow the FDCPA validation notice to be included in the summons when it is the first collection communication. The FDCPA allows the validation notice to be sent separately within 5 days of the initial collection communication.

4. Definitions.

   a) A "debt collector" is a person who uses any instrumentality of interstate commerce or the mails in any business the principal purpose of which is the collection of any debts, or who regularly collects debts owed to others.

      (1) A corporate debt collector was liable for the misconduct of its attorney and its employees. *See Campion v. Credit Bureau Services, Inc*., 2000 U.S. Dist. LEXIS 20233 (E.D. Wash. 2000)

      (2) Includes a party based in the U.S. who collects debts owed by consumers residing outside the U.S. The residence of the consumer is irrelevant.

      (3) Repossessors are **usually not** debt collectors under the FDCPA. *Nadalin v. Automobile Recovery Bureau, Inc.*, 1999 WL 130194 (7th Cir. 1999).

         (a) The FDCPA regulates “debt collectors,” a term that is defined as excluding repossessors and other enforcers of security interests. 15 U.S.C. § 1692a(6).

         (b) A repossessor may not take or threaten to take, however, nonjudicial action to dispossess a

person of property if "there is no present right to possession of the property claimed as collateral through an enforceable security interest." 15 U.S.C. § 1692f(6)(A).

(c) Repossessors withheld personal property from owner of repossessed vehicle in order to collect their $25 bailment fee. These repossessors "did not seize the plaintiff's personal property for the purpose or with the likely effect of using it to satisfy the plaintiff's debt to [the repossessor]'s principal. The seizure was not a method of enforcing a debt owed to the lender. It was not an effort to claim and seize additional collateral for the loan. We can find no evidence that Congress in the debt collection statute meant to extinguish repossessors' common law rights and remedies, whatever they may be, as bailees, provided the repossessor is not seizing property as collateral for the lender's loan to the owner."

(d) Repossessors could be debt collectors if regularly demanded storage fees owed to the creditor bank as a condition of returning the vehicle. See *Purkett v. Key Bank USA, N.A.*, 2001 U.S. Dist. LEXIS 6126 (N.D. Ill. 2001).

(4) Delivery services CAN be indirect debt collectors subject to FDCPA liability. *Romine v. Diversified Collection Services, Inc.*, 155 F.3d 1142 (9th Cir. 1998).

(a) We conclude, however that Western Union's activities go beyond mere information gathering or message delivery, and are of the type that the FDCPA was designed to deter. The purpose of the FDCPA is to limit harassing, misleading, and fraudulent contacts and communications with or about consumer debtors.

(b) The stated purpose of the Act is to "protect consumers from a host of unfair, harassing, and deceptive debt collection practices...." Most of the "collection abuses" outlined in the legislative history involve improper contacts

with consumer debtors. In conjunction with its role in contacting debtors and obtaining and forwarding telephone numbers, another significant element is Western Union's advertised role in catalyzing debt collection by conveying a sense of urgency through the use of Western Union telegrams.

(5) Attorneys may meet the definition of "debt collector." 15 U.S.C. § 1692(a)(6)(F) (Supp. V 1987).

(a) U.S. Supreme Court resolved all debate about whether attorneys are covered under the Act in *Heintz v. Jenkins*, 115 S.Ct. 1489 (1995) (The FDCPA applies "to attorneys who 'regularly' engage in consumer-debt-collection activity, even when that activity consists of litigation."); but see *Chapman v. fisher*, 2001 U.S. Dist. LEXIS 18499 (N.D. Ill. 2001) (the court held that the FDCPA does not apply to attorneys engaged in litigation activity.)

(b) See also *Crossley v. Lieberman*, 868 F.2d 566 (3rd Cir. 1989) (attorney who wrote demand letters to debtor on behalf of a lending bank and engaged in debt collection activities for other banks was a debt collector for purposes of the FDCPA). But see *Porter v. Hill*, 838 P.2d 45 (Or. 1992) (attorney who brought action against former client to collect fees for legal services rendered was acting as a "debt collector" under state Unlawful Debt Collection Practices Act as a person who was attempting to enforce obligation that was allegedly owed to him as commercial creditor by consumer as result of consumer transaction).

(6) Persons Specifically Excluded form the Term "Debt Collector:

(a) Creditors' employees. Officers or employees of a creditor collecting debts for that creditor unless the creditor is using another name implying that a third party is the collector. See

Thomasson v. Bank One, N.A., 137 F. Supp. 2d 721 (E.D. La. 2001)

(i) A "creditor" is a person or organization to whom or to which a debt is owed. Generally, a creditor is not included within the definition of "debt collector" when collecting its own debts using its own name.

(ii) States may have statutes which limit conduct of creditors as well as debt collectors

(b) A commonly owned or afflicted corporate collector collecting only for its affiliates.

(c) State or federal officials performing their duties. Any officer or employee of the U.S. or any state to the extent collecting or attempting to collect is in performance of his/her duty. This means that a LAA would arguably not be considered a debt collector when contacting others in reference to debts owed to a client. It also means that AAFES is not a debt collector when trying to collect from soldiers. *See Hilman v. Secretary of the Treasury*, 2000 U.S. Dist LEXIS 4544 (W.D. Mich. 2000) (pro se litigant FDCPA case dismissed because the IRS was not subject to FDCPA).

(d) Process servers. Any person while serving or attempting to serve legal process in connection with judicial enforcement of a debt

(e) Non-profit consumer credit counseling services.

(f) Persons collecting debts as part of bona fide fiduciary or escrow arrangements

(g) Extender of credit collecting on behalf of another a debt it originally extended for example mortgages and student loans. A

retailer may assign a debt to a bank, but retains responsibility to collect delinquent accounts

(h) Persons collecting debts not in default when obtained. Any person collecting any debt owed another to the extent such activity...

(i) concerns a debt which was originated by such person, or

(ii) concerns a debt that is not yet in default at the time that the person obtained it. *See Barber v. National Bank*, 815 P.2d 857 (Alaska 1991) (mortgage service co. that obtained debt before default exempted from FDCPA coverage (not a debt collector)).

(a) Mortgage servicer who is collecting under a forbearance agreement that was not in default when acquired is NOT a debt collector under the FDCPA. *Bailey v. Security National Servicing Corporation*, 154 F.3d 384 (7th Cir. 1998).

(b) [D]ebtors [in these situations] end up with two agreements (the original one and the superseding forbearance agreement), making it important which one a creditor or his mortgage servicer seeks to collect. If he seeks to collect on the original note technically remaining in default -- meaning it's revived because the debtor defaulted again under the new agreement -- then he is a "debt collector" under the Act so long as the debt was in default at the time he obtained or purchased it.

(c) If, on the other hand, he seeks to collect on payments currently due under the new superseding agreement, then he is not a "debt collector" under the Act (but more akin to a credit card company sending out monthly statements to its customers) because the debtor is not in default under that agreement.

(iii) Enforcer of a security interest in an account as collateral for a commercial loan. Retailers and lenders sometimes use consumer accounts receivable as collateral for their own commercial financing. Upon default the secured parties may collect the amounts due on the consumer accounts.

b) A **"debt"** is any obligation or alleged obligation of a consumer to pay money arising out of a transaction in which the money, property, insurance, or services which are the subject of the transaction are primarily used for personal, family, or household purposes, whether or not the obligation has been reduced to judgment (i.e., overdue obligations on bills, dishonored checks used to pay for goods or services intended for personal, family, or household purposes, student loans).

(1) Ultimatums about unpaid rent fall under the Fair Debt Collection Practices Act. *Romea v. Heiberger & Associates*, 988 F.Supp. 712 (S.D.N.Y. 1997), *permission for interlocutory appeal granted Romea v. Heiberger & Associates*, 988 F.Supp. 715 (S.D.N.Y. 1998).

(2) Bad checks are debts under the FDCPA. *Bass v. Stolper, Koritzinsky, Brewster & Neider, S.C*, 111 F.3d 1322 (7th Cir. 1997); *Charles v. Lundgren & Associates, P.C.*, 119 F.3d 739 (9th Cir. 1997).

(3) If the purpose for acquiring the goods or services changes, then the original purpose is determinative. *See Miller v. McCalla, Raymer, Padrick, Cobb, Nicholas, &*

Clark, L.L.C., 214 F.3d. 872 (7th Cir. 2000) (The debt for a house purchased as the buyer's residence and then rented was a consumer debt originally, the subsequent use of the collateral would not alter the applicability of the FDCPA.)

5. Requirements imposed by the FDCPA.

a) Within 5 days after initial communication with a consumer in connection with collection of a debt, the debt collector must send the consumer a written notice containing the following:

(1) The amount of the debt.

(a) Summary Judgment was granted for consumers when their notification collection letter demanded a sum "plus accrued interest and /or late charges, and attorney fees, exact amount to be determined by an agreement between you and us or by the court." See *Bawa v. Bowman, Heintz, Boscia & Vician*, 2001 U.S. Dist. LEXIS 7842 (S.D. Ind. 2001).

(2) The name of the creditor to whom the debt is owed.

(3) A notice to the consumer that they may request verification of the debt, and that if the consumer does not send such a request within 30 days, then the debt collector will assume the debt is valid.

(a) Debt collectors are only required to show that they SENT a validation notice to consumers. Once they do, consumers have 30 days to request verification of the debt. *Mahon v. Credit Bureau Of Placer County Incorporated*, 1999 WL 123725 (9th Cir. 1999) ("We hold that section 1692g(a) requires only that a Notice be "sent" by a debt collector. A debt collector need not establish actual receipt by the debtor.")

(b) Requires validation of debts. Upon request, the debt collector must notify the debtor of the nature of the debt, the identity of the creditor, and must cease collection efforts until

verification of the debt is completed. All the consumer has to do is send written notice "I dispute the debt"

(c) "[A] debt collector must provide verification of the debt to the debtor, upon written request made by the debtor within 30 days after receipt of the initial Notice. 15 U.S.C. § 1692g(b). If no written demand is made, 'the collector may assume the debt to be valid.' *Avila v. Rubin*, 84 F.3d 222, 226 (7th Cir.1996); 15 U.S.C. § 1692g(a)(3)."

(i) Thirty days from the date of receipt of the notification. Practice tip: The time for verification has often passed but request verification anyway.

(d) A tardy request for verification does NOT trigger the debt collector's obligation to verify the debt.

(e) Adequate verification varies depending on the reason for the dispute. The debt collector must cease collection from the date verification is requested until the verification is provided, but may continue collection within the first 30 days of the notice.

(4) A statement that upon the consumer's written request within the thirty day period, the debt collector will provide the consumer the name and address of the original creditor if different from the current creditor

b) "When a notice contains language that 'overshadows or contradicts' other language informing a consumer of her rights, it violates the Act.' . . .'[T]he juxtaposition of two inconsistent statements renders the notice invalid under § 1692g.' . . . A debt collection notice is overshadowing or contradictory if it fails to convey the validation information clearly and effectively and thereby makes the least sophisticated consumer uncertain as to her rights." *Savino v. Computer Credit, Inc.*, 164 F.3d 81 (2d Cir. 1998).

(1) When an independent debt collector solicits payment from a consumer, it must -- within five days of the initial communication -- provide the consumer with a detailed validation notice . . .

(2) When determining whether Section 1962g has been violated, courts use "an objective standard, measured by how the 'least sophisticated consumer' would interpret the notice received from the debt collector."

c) Requires that a debt collector's letter disclose that any information provided by recipient will be used to collect debts. See *Emanuel v. American Credit Exchange*, 870 F.2d 805 (2nd Cir. 1989) (disclosure required even when letter did not request information from debtor).

(1) Debt collectors must inform the consumer in the first contact with that consumer (oral or written) that they are a debt collector AND that any information gained will be used in the process of collecting a debt.

(2) Any subsequent communications must disclose only that the communication is from a debt collector.

(3) Formal pleadings made in connection with legal proceedings need not contain the disclosure.

d) The act provides a means by which a consumer can stop the attempts of a debt collector to communicate with the consumer.

(1) Consumer notifies the debt collector in writing

(a) Refuse to pay, or

(b) Wish no further contact

(c) Represented by an attorney with respect to such debt and has knowledge of, or can readily ascertain such attorney's name and address unless the attorney fails to communicate within a reasonable period of time to a communication from the debt collector or unless the attorney consents to direct communication with the

consumer. (Best to tell the debt collector you are the attorney for all debts concerning your client).

(2) Debt collector must cease contact, unless to notify debtor that the debt collector intends to invoke specific remedies.

e) Other consumer protections provided by the FDCPA.

(1) Restricts contact with the debtor unusual or inconvenient times or places.

(a) Know or should have known as inconvenient to consumer.

(b) Absent knowledge, debt collector should assume can only communicate between 0800 and 2100 hours.

(c) Inconvenient places include funeral homes, a neighbor's house, a hospital, or the work place.

(2) Restricts contacts by debt collectors with third parties. Without prior consent of the consumer given directly to the debt collector or a court order, a debt collector may not communicate with a third party (this includes consumer's spouse, parent if consumer is a minor, guardian, executor, or administrator) (15 U.S.C. § 1692c) unless:

(a) Debt collectors may contact third parties seeking debt collection assistance only if:

(i) The debtor has given prior consent directly to the debt collector, or

(ii) The debt collector has obtained a court order permitting such contact, or

(iii) Contact is reasonably necessary to effectuate a post-judgment judicial remedy.

(b) Debt collectors may contact third parties to acquire information about consumer's location, but must

(i) Identify self, state he/she is trying to confirm or correct location information about consumer, and only if expressly asked, identify his/her employer,

(ii) Refrain from referring to the debt,

(iii) Usually make only a single contact with each third party,

(iv) Not communicate by postcard,

(v) Not indicate the collection nature of his/her business purpose in any written communication.

(vi) Check state law. Some states prohibit any contact with the employer. In these states the Army will not assist either the debt collector or the creditor.

(c) They may contact a credit reporting agency if otherwise permitted by law.

(3) Limit communications to the consumer's attorney, where collector knows of the attorney, unless the attorney fails to respond.

(a) If the debt collector knows the consumer is represented by an attorney and knows or can readily ascertain the attorney's name and address. The attorney MUST notify the debt collector that they represent the individual for the subject debt and any future debts that come into collection. See *Graziano v. Harrison*, 763 F.Supp. 1269 (D.N.J. 1991) (Collector did not violate Act by continuing communication with debtor once notified debtor represented by counsel where subsequent notices pertained to

different debts and collector not informed attorney represented debtor on all subsequent debts.)

(4) Prohibits communications at the consumer's place of employment if the debt collector knows or has reason to know that the consumer's employer prohibits consumer from receiving such communication. Include language regarding this prohibition in your letter to the debt collector.

(5) After the consumer notifies the debt collector in writing that the consumer refuses to pay the debt or that the consumer wishes the debt collector to cease further communication with the consumer, except that the debt collector may notify the consumer that the debt collector intends to invoke a specific remedy.

(6) A debt collector may not engage in any conduct the natural consequence of which is to harass, oppress, or abuse any person in connection with a debt. 15 U.S.C. § 1692d.

(7) A debt collector may not use any false, deceptive, or misleading representations in connection with the collection of any debt. 15 U.S.C. § 1692e.

(a) *See Crossley v. Lieberman*, 868 F.2d 566 (3rd Cir. 1989) (debt collector who falsely implied that a mortgage foreclosure case against debtor was in litigation violated the FDCPA).

(b) 15 U.S.C. § 1692e(8) defines the failure of a debt collector to disclose the disputed status of a debt as a "false, deceptive, or misleading representation." Debt collectors must report debts as disputed, whether or not the consumer disputes the debt in writing. *Brady v. The Credit Recovery Company*, 160 F.3d 64 (1st Cir. 1998).

(c) Falsely implying government affiliation.

(8) A debt collector may not use unfair or unconscionable means to collect any debt. 15 U.S.C. § 1692f.

(9) A debt collector may not solicit post-dated checks in lieu of pursing a lawsuit and may not deposit any post-dated checks accepted prior to the date written on the check.

6. Legal Action Prohibitions for Debt Collectors.

a) Debt collector must sue consumer only in the judicial district where the consumer resides or signed the contract sued upon, (*See Shapiro & Meinhold v. Zartman*, 823 P.2d 120 (Colo. 1992) (Attorney collector who brought foreclosure action in county other than that where real estate was situated violated FDCPA, even though state statute allowed such venue); s*ee also, Action Professional Service v. Kiggins*, 458 N.W.2d 365 (S.D. 1990) (interprets "judicial district" as meaning in the appropriate state (vice federal) court "judicial district.")).

b) Except that an action to enforce a security interest in real property must be brought where the property is located.

c) Contradictory notices as to the timing of a lawsuit were misleading, even when one of the options was the statutorily mandated notices. *Bartlett v. Heibl*, 128 F.3d 497 (7th Cir. 1997).

d) The Act prohibits explicit and veiled threats of unintended legal actions. Legal actions are unlikely if:

(1) The proper court is far away from the collector or creditor.

(2) The debt is relatively small (less than $150).

(3) The debt is disputed.

(4) The creditor in the past has shown a policy or tendency not to take legal action.

(5) Collector lacks authority to sue under law or under collector's agreement with creditor.

D. Remedies.

1. Violation of FDCPA is deemed an unfair and deceptive act or practice in violation of the Federal Trade Commission Act. Consequently, the FTC could pursue action.

2. The Act also creates a private cause of action for the consumer. Consumer could also assert violations of the FDCPA as a counter-claim in a suit to collect the debt.

3. Standing to sue.

    a) "Any debt collector who fails to comply with any provision ... with respect to any person is liable to such person..." The Act does not define terms "with respect to any person."

    b) *Wright v. Finance Service of Norwalk, Inc.*, 22 F.3d 647 (6th Cir., 1994) ("the phrase 'with respect to any person' [in 15 U.S.C. § 1692e] includes more than just the addressee of the offending letters. We conclude that the phrase, at a minimum, includes those persons, such as Wright, who 'stand in the shoes' of the debtor or have the same authority as the debtor to open and read the letters of the debtor." Plaintiff Wright, was the executrix of the debtor.).

4. Civil liability for failure to comply with FDCPA includes (15 U.S.C. § 1692k):

    a) Actual damages (FTC Commentary: includes damages for personal humiliation, embarrassment, mental anguish, or emotional distress).

    b) Additional statutory damages allowed by the court up to $1,000 (no actual damages required). Divided 6th Circuit holds $1,000 for each violation of statute rather than $1,000 per suit. (*Wright v. Finance Service of Norwalk, Inc.* discussed above - executrix sued for FDCPA violations in collection notices sent to her deceased mother).

        (1) To collect statutory damages, a consumer need only prove the statute was violated. They do not have to prove they suffered any actual impact. *Bartlett v. Heibl*, 128 F.3d 497 (7th Cir. 1997).

(2) In determining the amount of damages, the court shall consider, among other factors:

(a) frequency and persistence of noncompliance by the debt collector;

(b) nature of the noncompliance; and

(c) the extent to which the noncompliance was intentional.

c) Attorney's fees and court costs if the consumer prevails. "Where a plaintiff prevails, whether or not he is entitled to an award of actual or statutory damages, he should be awarded costs and reasonable attorney's fees in amounts to be fixed in the discretion of the court." *Bartlett v. Heibl*, 128 F.3d 497 (7th Cir. 1997).

5. Generally, this is a strict liability statute; however, a debt collector may not be held liable if the debt collector can show by a preponderance of evidence that the violation was unintentional and resulted from a bona fide error notwithstanding the maintenance of procedures reasonably adapted to avoid any such error.

6. Action to enforce FDCPA may be brought in any appropriate U.S. District Court without regard to amount in controversy, or in any other court of competent jurisdiction, within one year from date on which the violation occurs. (FTC Commentary: 1 year limitations period applies only to private lawsuits, not those initiated by government).

E. Processing Requests for Debt Collection Assistance by the Military.

1. Additional References.

a) 32 C.F.R. Parts 112-113, Indebtedness of Military Personnel.

b) DOD Directive 1344.9, Indebtedness of Military Personnel (Oct. 27, 1994) (certified current as of Dec. 1, 2003).

c) AR 600-15, Indebtedness of Military Personnel (14 March 1986), available at *www.usapa.army.mil*.

d) AFI 36-2906, Personal Financial Responsibility (1 January 1998).

e) MILPERSMAN 7000020 available at *www.bupers.navy.mil*.

f) MCO P5800.16A, Marine Corps Manual for Legal Administration, (31 Aug 1999).

g) United States Coast Guard Personnel Manual, COMDTINST M1000.6A, Ch. 8, Sect. F (8 January 1988).

2. **STEP 1:** Determine whether the requester can contact third parties directly. Is this person a "debt collector" subject to the FDCPA or a "creditor" who may be limited by state law?

a) Requests from debt collectors. Debt collectors may contact third parties seeking debt collection assistance only if:

(1) The debtor has consented to such contact,

(2) The debt collector has obtained a court order permitting such contact, or

(3) Communication necessary to effectuate post-judgment judicial remedy.

b) Requests from creditors.

(1) A "creditor" is a person or organization to whom or to which a debt is owed.

(2) Creditors <u>are</u> entitled to contact third parties for assistance <u>unless</u> state law precludes such contact. If the state forbids contact, the creditor will not be assisted.

(3) Credit Unions and Banks:

(a) **Marine Corps**: Commanders will provide debt processing assistance to credit unions serving DOD personnel even if the host state prohibits third party contact by creditors. Credit unions

may bring delinquent loans or dishonored checks to the attention of the commander.

(b) **Army**: Those serving DOD must conform to Standards of Fairness. Commanders will answer all check complaints. No mention that they are exempt from state law prohibiting third party contact.

(c) **Navy**: Those serving DOD must conform to Standards of Fairness. No mention that they are exempt from state law regarding third party contact.

(d) **Air Force**: Comply with state law prohibiting creditor third party contact.

3. **STEP 2**: Know Service Policy on Debts.

a) Department of Defense Directive 1344.9.

(1) DOD Definitions.

(a) Just Financial Obligations. A legal debt acknowledged by the military member in which there is no reasonable dispute as to the facts or the law; or one reduced to judgment which conforms to 50 U.S.C. App. § 501 (SCRA), if applicable. (32 C.F.R. § 112.3).

(b) A Proper and Timely Manner. A manner which under the circumstances does not reflect discredit on the military service. (32 C.F.R. § 112.3).

(c) Debt Collector. An agency or agent regularly engaged in the collection of debts described under Pub. L. 95-109 (FDCPA). (32 C.F.R. § 112.3).

(2) General Policies.

(a) Members are expected to pay just financial obligations in proper and timely manner.

(b) Services have no legal authority, except in the case of court ordered alimony or child support, to require members to pay a private debt or to divert any part of their pay for its satisfaction.

(c) Enforcement of private obligations of a military member is a matter for civil authorities.

(3) Processing debt complaints will NOT be extended to those:

(a) Who have not made a bona fide effort to collect the debt directly from the military member;

(b) Whose claims are patently false and misleading;

(c) Whose claims are obviously exorbitant.

b) Service regulations implement DOD Directive 1344.9.

4. **STEP 3:** Follow Processing Procedures.

a) Requirements for Creditors.

(1) Creditors subject to Regulation Z (12 C.F.R. 226; Truth in Lending Act) must submit with their requests for assistance:

(a) Certificate of Compliance, and

(b) Copy of disclosures provided the military member as required by Truth in Lending Act 15 U.S.C. § 1601.

(c) Copy of any signed contract or judgment.

(2) Creditors not subject to Regulation Z, such as public utility companies, must submit with their requests for assistance - Certification that no interest, finance

charge, or other fee is in excess of that permitted by law of state where obligation was incurred.

(3) Foreign owned companies must submit with their requests for assistance:

(a) Copy of terms of the debt (English translation), and

(b) Certification it has subscribed to DOD Standards of Fairness.

b) Indebtedness Complaints Meeting DOD Requirements will be Processed.

(1) Commanders shall:

(a) Review facts surrounding transaction forming basis of complaint, to include:

(i) Member's legal rights and obligations,

(ii) Member's defenses or counterclaims.

(b) Advise member that:

(i) Just financial obligations are expected to be paid in proper and timely manner, and

(ii) Financial and legal counseling services are available.

(c) Notify claimant that soldier told of complaint, summarizing soldier's intentions if soldier gave permission to release that information.

(d) Consider administrative or punitive action, if proper.

(2) Commanders will not:

(a) arbitrate disputed debts, or

(b) admit or deny the validity of the claim.

(3) All services: Do not try to judge or settle disputed claims or admit or deny validity. If soldier denies debt, notify creditor that civil authorities must handle disputed debts.

(4) Commanders' responses will not indicate whether any action has been taken against a member as a result of the complaint.

c) Indebtedness Complaints Not Meeting Service Requirements - All services: Return complaint, explaining no action until comply with regulation.

d) Services May Deny Assistance to Creditors.

(1) When the claimant, having been notified of the DOD requirements, refuses or repeatedly fails to comply;

(2) When the claimant, regardless of the merits of the claim, clearly shows an attempt to unreasonably use the processing privilege.

5. **STEP 4:** Discipline, if appropriate. - **All services**: Commanders may take administrative or disciplinary action against members who fail to meet their just financial obligations in a proper and timely manner.

a) **Army**:

(1) Put in permanent record,

(2) Deny reenlistment,

(3) Administrative separation,

(4) Punitive action under UCMJ, articles 92, 123, 133, or 134.

b) **Marine Corps**:

(1) Put in fitness reports and pro/cons,

(2) Take appropriate administrative, non-punitive, or punitive action.

c) **Navy**:

(1) For officers, action should be governed by MILPERSMAN 1611-010, Officer Performance. For enlisted, take appropriate administrative, non-punitive, or punitive action.

(2) Require member to submit a statement of monthly finance to DOD, Central Adjudication Facility.

(3) Counseling,

(4) Administrative discharge for misconduct,

(5) Report all bankruptcies to Chief of Naval Personnel.

d) **Air Force:** Unit commanders will consider and, if appropriate, initiate administrative or disciplinary action against members who continue to demonstrate financial irresponsibility.

e) **Coast Guard**:

(1) Put in officer fitness reports and take other corrective action,

(2) Submit adverse special fitness report,

(3) Counseling,

(4) Put in enlisted records

(5) Administrative separation,

(6) Recommend against reenlistment,

(7) Adverse security clearance,

(8) Punitive action.

II. FAIR CREDIT REPORTING ACT (FCRA)

A. References.

1. Fair Credit Reporting Act, 15 U.S.C. §§ 1681-1681u. (Apr. 25 1971).

2. Consumer Credit Reporting Reform Act of 1996, contained in the Omnibus Consolidated Appropriations Bill, 110 Stat. 3009; 104 Pub. Law 208 (Sept. 30, 1996).

3. NATIONAL CONSUMER LAW CENTER, FAIR CREDIT REPORTING ACT (5th ed. 2002 and Supp. 2005).

4. The Federal Fair and Accurate Credit Transactions Act of 2003, Pub. L. No. 108-159 (Dec. 4 2003).

5. Analysis of the Fair Credit Transactions Act of 2003, National Consumer Law center, available online at: http://www.nclc.org/initiatives/facta/contents/nclc_analysis_content.html

B. Introduction.

1. The Federal Fair Credit Transactions Act of 2003 made significant changes and additions to the FCRA. The Act provides for free annual credit reports, increases standards of accuracy of information, strengthens adverse action notices and creates the right to get credit score from the credit reporting agencies for a fee, adds rights for identity theft victims and for active duty service members. Further, consumers can prevent sharing of information by affiliates for marketing purposes. The act significantly limits States abilities to regulate much of the FCRA's subject matter and conduct requirements except in the area of Identity Theft. Further the Act requires numerous implementing actions by the FTC which have not been completed as of the date of the outline. Once the actions are taken the outline will once again be update.

2. The Omnibus Appropriations Act referenced above contained, among other consumer protection legislation, the Consumer Credit Reporting Act of 1996, which made changes to the Fair Credit Reporting Act

C. Purpose and Scope of FCRA.

1. FCRA applies to Credit Reporting Agencies (CRAs) those furnishing information to the agencies (furnishers) and Users of Credit Reports (Users).

2. The act applies to situations in which a person collects information on a consumer's credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, and mode of living.

3. Purpose of FCRA: Requires CRAs to adopt reasonable procedures for meeting the needs of commerce for consumer credit, personnel, insurance, and other information. The information must be:

   a) Accurate, relevant, up-to-date, and

   b) Furnished only for certain permissible purposes.

4. CRAs must use procedures that:

   a) Are fair and equitable to the consumer, with regard to confidentiality, accuracy, relevancy, and proper use of the information, and,

   b) Place various obligations on persons who use or disseminate credit information about consumers.

D. Definitions.

1. Consumer Reporting Agencies are:

   a) Those "who for monetary fees, dues, or on a cooperative nonprofit basis, regularly engage in ... the practice of assembling or evaluating consumer credit information on consumers for the purpose of furnishing consumer reports to third parties**,** and [who use] any means or facility of interstate commerce for the purpose of preparing or furnishing consumer reports." 15 U.S.C. § 1681a(f). (e.g., Experian, Trans Union Credit Corporation, Equifax).

b) Agencies or persons may become consumer reporting agencies if they regularly furnish information beyond their own transactions to others for use in consumer transactions. (FTC Commentary, 16 C.F.R. Part 600, May 4, 1991).

c) **NOTE:** Creditors that report information about their own experiences with consumers are not credit reporting agencies, nor are they issuing a "consumer report." **BUT**, if the creditor reports any information other than that obtained in its own dealings with consumer, then it may meet definition of "consumer reporting agency."

d) **CRA "that compiles and maintains files on consumers on a nationwide basis."** That term includes any CRA that regularly engages in the practice of assembling, evaluating, and maintaining, for the purpose of issuing consumer reports, EACH of the following things regarding consumers nationwide:

(1) Public record information

(2) Credit account information from persons who furnish that info regularly and in the ordinary course of business.

2. **Users**: Not defined separately in the statute, but means those receiving the "consumer report" information and applying it to a consumer. (Refer to definition of consumer report).

3. **Consumer Credit Reports** are:

a) Any written, oral or other communication of information

b) Collected by a CRA bearing on:

(1) The consumer's credit worthiness,

(2) Credit standing, or,

(3) General reputation, personal characteristics, or mode of living,

(a) Virtually any information about a consumer satisfies the definition of a consumer report.

(b) The report must bear on the consumer's characteristic, not a business or corporation.

c) Which is used or expected to be used in establishing the consumer's eligibility for:

(1) Credit or insurance to be used primarily for personal, family, or household purposes,

(2) Employment purposes other than those listed below, or

(3) Other purposes authorized by the Act. *See* § E below.

d) The Term does NOT include:

(1) The reporting of information based solely on the experiences between the consumer and the person making the report.

(2) Communication of the information above between persons related by common ownership or corporate control.

(3) Communication of any other information between persons related by common ownership or corporate control, PROVIDED that the consumer is given clear and conspicuous notice that this may happen and given the opportunity before it does happen to direct that the information not be shared.

e) Any authorization or approval of a specific extension of credit by the issuer of a credit card or similar device.

f) Courts have also limited the applicability in the way they apply the definition to products issued by CRAs.

(1) *Arcidiacono v. American Express*, 1993 WL 94327 (D.N.J. 1993) - Lists sold by American Express were not consumer reports even though they categorized

consumers with descriptive labels such as "low-end, value-oriented, fashion conscious, Fifth Avenue sophisticated, Rodeo Drive chic."

(2) *Trans Union Corp. v. FTC*, 81 F.3d 228 (D.C. Cir. 1996). Mailing lists were not consumer reports even though placement on the list required having two credit accounts. This "implicit" credit info did not have anything to do with PERFORMANCE and therefore did not satisfy the definition.

(3) An Inquiry Activity Report is a consumer report for purposes of the FCRA. *Yang v. Government Employees Insurance Company (GEICO)*, 146 F.3d 1320 (11th Cir. 1998).

(4) Consumers "file under review" is a consumer report. Thompson v. Equifax Credit Inf. Servs., 2001 U.S. Dist LEXIS 22666 (M.D. Ala. Nov. 14, 2001)

(5) A Check Cashing list is a consumer report for purposes of the FCRA. *Greenway v. Information Dynamics, Ltd.*, 524 F.2d. 1145 (9th Cir. 1975). List including previous issuance of an unpayable check bears directly on a consumer's credit worthiness and credit standing.

4. **Investigative Consumer Reports**:

a) Sometimes a user, usually an insurance company or a prospective employer wants more detail on a consumer so they request an investigative consumer report.

b) Consumer report or portion thereof which contains information on consumer's character, living style, and reputation obtained through personal interviews (subjective evaluations).

c) An investigator will question neighbors, co-workers, and others concerning their knowledge and opinion on the consumer. The report contains more detailed information than a regular consumer report, may include information on individual's marital or sex life, drinking habits, friends and behavior.

d) Some consumer reporting agencies specialize in investigative reports (Equifax) which are a subcategory of consumer reports.

e) Because a report like this could damage a person's reputation in the community there are extra added protections.

(1) CRAs must verify information, and reverify information over 3 months old.

(2) Users of investigative reports must:

(a) Within 3 days, give notice to consumer that investigative report was requested,

(b) That the report will concern the consumer's character, reputation, mode of living, and personal characteristics, or whichever are applicable and may include interviews with acquaintances, and

(c) That consumer has the right to request within a reasonable time, a complete and accurate description of the nature and scope of investigation being conducted.

5. Furnishers

a) Persons who regularly and in the ordinary course of business furnish information to the CRA.

6. **Adverse Action**[1] means:

a) The same as the term means under the Equal Credit Opportunity Act, 15 U.S.C. § 1691(d)(6). That section provides that:

(1) For purposes of this subsection, the term "adverse action" means a denial or revocation of credit, a change in the terms of an existing credit arrangement, or a

[1] Note that the term "adverse action" was not defined in the original version of the statute. However, there were requirements imposed by the statute for taking "adverse action." Having the definition should put consumers in a better position to assert their statutory rights when a User takes "adverse action."

refusal to grant credit in substantially the amount or on substantially the terms requested. Such term does not include a refusal to extend additional credit under an existing credit arrangement where the applicant is delinquent or otherwise in default, or where such additional credit would exceed a previously established credit limit.

(2) The term is also given specific additional meaning within the definition section of the FCRA. an action taken or determination that is--

(a) made in connection with an application that was made by, or a transaction that was initiated by, any consumer, and

(b) adverse to the interests of the consumer.

(3) Credit Adverse actions:

(a) Refusal to grant credit in substantially the amount or terms as requested

(b) Termination of an account or an unfavorable change in its terms

(c) Refusal to increase line of credit

(4) Employment Adverse Actions

(a) Employment is denied

(b) Any employment decision adversely affects a current or prospective employee

(5) Insurance Adverse Actions

(a) Denial or cancellation of insurance coverage

(b) An increase in any charge for insurance

(c) Any reduction or other adverse or unfavorable change in the terms of coverage or amount of, any insurance, existing or applied for.

(6) Government License and Benefits Adverse actions

(a) Denial or cancellation of Government Benefits or Licenses

(b) An increase in any charge of Government benefits or Licenses

(c) Any other unfavorable or adverse change in terms of Government benefits or licenses

7. **Pre-screening Services**:

a) Mailing lists compiled by consumer reporting agencies using criteria specified by the user. (Example: The credit card solicitations received in the mail)

b) User must certify it is considering and will offer to enter into a credit relationship with each consumer on the pre-screened list, if not the release of the report is impermissible.

c) Consumers can elect to be excluded from prescreening lists, CRAs must maintain a system by which consumers can elect to have names omitted from lists. (1 888-5-OPT–OUT). Consumer calls number and is excluded off lists **for five years** (change from 2-5 years under FACTA). Can request a form from CRA to be excluded permanently.

d) Consumers can now opt out of affiliate marketing notices. The opt-out is for five years and consumers may extend for additional 5 years.

E. Permissible Uses of a Consumer Report. (15 U.S.C. § 1681b).

1. In response to a **court order or subpoena** issued in connection with proceedings before federal grand jury, - law enforcement can not request

2. With the consent of the consumer to whom the report relates, - written instructions to the reporting agency or permission to provide a report to the user, just need a dated written authorization that designates who is to send and who is to receive the credit report, don't need a Power of Attorney.

3. Identifying information furnished to the Government, only name, address, former addresses, places of employment, or former places of employment.

4. To a person who the CRA "has reason to believe" intends to use the report:

    a) in connection with **a credit transaction involving** the consumer,

        (1) Collection of Credit accounts

        (2) Credit extension for personal family, or household purpose (not for business extension of credit)

    b) for **employment** purposes

        (1) evaluating a person for employment, promotion, reassignment or retention as an employee

        (2) The business must give special employment related disclosures

        (3) Employers' investigations of their employees now excluded from the FCRA under FACTA. Can not be for investigating consumer's creditworthiness. Must concern investigation of the following:

            (a) Suspected misconduct

            (b) Compliance with federal state or local laws

            (c) Compliance with rules of a self-regulatory organization, or

(d) Compliance with the preexisting written polices of the employer

c) in connection with the **consumer's insurance**, or

d) in connection with the consumer's eligibility for a license or other benefit conferred by the government, or

e) as a potential investor or servicer, or current insurer, in connection with a valuation of, or an assessment of the credit or prepayment risks associated with, an existing credit obligation; or

f) Otherwise has a **legitimate business need** for the information--

(1) The legitimate business need must be in connection with a business transaction that is initiated by the consumer; or

(2) To review an account to determine whether the consumer continues to meet the terms of the account.

(3) *Houghton v. New Jersey Manufacturers Ins. Co.*, 795 F.2d 1144 (3rd Cir. 1986) - The business transaction must relate back to one of the other specifically enumerated transactions, i.e., credit insurance eligibility, employment, or licensing.

(4) What constitutes a "legitimate business need" has gotten more restrictive, both in the statute and the courts.

(a) Litigation is NOT a "legitimate business need" under the FCRA. *Duncan v. Handmaker*, 149 F.3d 424 (6th Cir. 1998); *Bakker v. McKinnon*, 152 F3d 1007 (8th Cir. 1998).

(b) The mere existence of the landlord-tenant relationship does NOT justify accessing a tenant's credit report. *Ali v. Vikar Management Ltd.*, 994 F.Supp. 492 (S.D.N.Y. 1998).

(c) The FTC's interpretation of the new restrictions on legitimate business need releases is very strict. *See* Consumer Law Note, *Federal Trade Commission Staff Issues Informal Interpretation of FCRA Changes*, ARMY LAW., June 1998, at 9.

5. Preconditions of Release. Must be met before a Consumer Credit Report may be issued for the following permissible purposes:

a) Employment purposes (except the areas noted above):

(1) The User must certify to the CRA that they have:

(a) Given a clear and conspicuous written disclosure to the consumer, in a document that consisted solely of the disclosure, that a consumer report may be obtained for employment purposes and the consumer has given the User written authorization to procure the report; AND

(b) That they will comply with the obligations of a User who takes adverse action based upon a consumer credit report; AND

(c) Information from the consumer report will not be used in violation of any applicable Federal or State equal employment opportunity law or regulation.

(2) The CRA must provide with the report a summary of the consumer's rights under the FCRA.

b) Credit or insurance transactions not initiated by the consumer. The CRA may issue the report only if:

(1) The consumer authorizes the agency to provide the report to such person; OR

(2) The transaction consists of a "firm offer of credit or insurance" (defined in the statute) and

(a) The CRA has complied with any election made by the consumer regarding exclusion from lists, and

(b) The information consists solely of

(i) The name and address of a consumer;

(ii) An identifier that is not unique to the consumer and that is used by the person solely for the purpose of verifying the identity of the consumer; and

(iii) Other information pertaining to a consumer that does not identify the relationship or experience of the consumer with respect to a particular creditor or other entity.

c) Reports containing medical information. A consumer reporting agency shall not furnish for employment purposes, or in connection with a credit or insurance transaction or a direct marketing transaction, a consumer report that contains medical information about a consumer, unless the consumer consents to the furnishing of the report.

(1) Consumers consent must be in writing, specific and must describe the use for which the agency will furnish the information.

(2) Users may not re-disclose the reports.

(3) Agencies may not identify the medical information furnishers in reports.

(4) Creditors may not obtain or use medical information in connection with any determination of the consumer's eligibility for credit.

F. Obligations of Consumer Reporting Agencies.

1. Duties when the consumer disputes the accuracy of the report.

a) If the consumer disputes the completeness or accuracy of the report, the CRA must investigate (within a reasonable time) and record the current status of the disputed information **unless the CRA has reason to believe that the dispute is frivolous or irrelevant**. 15 U.S.C. § 1681i.

(1) When a consumer reporting agency prepares a consumer report it shall follow reasonable procedures to assure maximum possible accuracy. *Wilson v. Rental Research Services, Inc.*, 165 F.3d 642 (8th Cir, 1999).

(a) West Headnote: "Technical accuracy of consumer report may be insufficient to satisfy requirement of Fair Credit Reporting Act (FCRA) that report be maximally accurate with respect to individual who is subject of report." 15 U.S.C. § 1681e(b).

(b) "[I]n determining the meaning of 'maximum possible accuracy' under § 1681e(b), the statutory language requires that reports be 'accurate' specifically with respect to the individual who is the subject of the report. . . . [R]eports containing factually correct information that nonetheless mislead their readers are neither maximally accurate nor fair to the consumer who is the subject of the report and thus may violate § 1681."

(2) An entry on a credit report that is incomplete, but not misleading satisfies the "maximally accurate" requirement. *Sepulvado v. CSC Credit Services, Inc.*, 158 F.3d 890 (5th Cir. 1998).

b) If the investigation does not resolve the dispute,

(1) The consumer may file a statement of not more than 100 words, and

(2) In future reports, the CRA must note that the consumer disputes the entry and provide the consumer's statement.

c) If the investigation reveals that the disputed entry is inaccurate or can no longer be verified, the CRA must delete the information.

d) Following either correction of the report or receipt of a consumer's statement in rebuttal, the CRA must furnish a copy of the annotated report (and consumer's statement, where appropriate) to "any person specifically designated by the consumer" who has received the report:

(1) Within the past 2 years for employment purposes.

(2) Within the past 6 months for other purposes.

2. Procedures for handling disputed information.

a) REINVESTIGATION: If the completeness or accuracy of any item of information contained in a consumer's file at a CRA is disputed by the consumer and the consumer notifies the agency directly of such dispute, the CRA SHALL

(1) Reinvestigate free of charge and record the current status of the disputed information, OR

(2) Delete the item from the file within 30-days of the CRA receiving notice of the dispute from the consumer. (This period may be extended not more than 15 additional days if the consumer reporting agency receives information from the consumer during that 30-day period that is relevant to the reinvestigation. However, NO extension may be used if the CRA finds during the 30 days that the information is inaccurate, incomplete, or cannot be verified.

(3) The Agency’s reinvestigation must be reasonable

b) Determination that dispute is frivolous or irrelevant.

(1) A CRA may terminate a reinvestigation of information disputed by a consumer if it reasonably determines that the dispute by the consumer is frivolous or irrelevant. This includes a failure by the consumer to provide

sufficient information to investigate the disputed information.

(2) Upon making this determination, the CRA shall notify the consumer of their determination not later than 5 **business** days after making the determination, by mail or, if authorized by the consumer for that purpose, by any other means.

(3) The notice shall include:

(a) The reasons for the determination; AND

(b) Identification of any information required to investigate the disputed information.

c) Notice to provider of information.

(1) Within 5 **business** days of receipt of the consumer's notice, the CRA SHALL

(a) Provide notification of the dispute to any person who provided any item of information that is disputed.

(b) The notice shall include all relevant information regarding the dispute that the agency has received from the consumer.

(2) Promptly after the initial 5 business day notice, but before the end of the 30 day period for investigation, the CRA must provide to the person who provided the information in dispute all relevant information regarding the dispute that is received by the agency from the consumer.

d) Results of the reinvestigation.

(1) Inaccurate or unverifiable information. Any item of the information found to be inaccurate or incomplete or which cannot be verified SHALL be promptly deleted from the consumer's file or modified, as appropriate, based on the results of the reinvestigation.

(2) Notice of results.

(a) The CRA must provide written notice to a consumer of the results of a reinvestigation under this subsection not later than 5 business days after the completion of the reinvestigation, by mail or, if authorized by the consumer for that purpose, by other means available to the agency.

(b) The notice must contain:

(i) A statement that the reinvestigation is completed;

(ii) A consumer report that is based upon the information in the consumer's file reflecting any changes made as a result of the reinvestigation;

(iii) If requested by the consumer, a description of the procedure used to determine the accuracy and completeness of the information, including the business name and address of any furnisher of information contacted and the telephone number if reasonably available;

(iv) A notice that the consumer has the right to add a statement to the consumer's file disputing the accuracy or completeness of the information; and

(v) A notice that the consumer has the right to request that the CRA notify the following persons of any notation regarding disputed information provided that the consumer specifically designate this person to receive notice.

(a) A user who received a consumer report for employment purposes within the prior two years.

(b) A user who received a consumer report for any other purpose within the last six months.

e) Automated reinvestigation system. Any **CRA that compiles and maintains files on consumers on a nationwide basis** (See definitions above.) shall implement an automated system through which furnishers of information to that consumer reporting agency may report the results of a reinvestigation that finds incomplete or inaccurate information in a consumer's file to other such consumer reporting agencies.

3. Reinsertion of previously deleted material. Before reinserting material, the following must occur:

a) The person who furnishes the information must certify that the information is complete and accurate.

b) The CRA must notify the consumer of the reinsertion in writing not later than 5 **business** days after the reinsertion or, if authorized by the consumer for that purpose, by any other means available to the agency.

c) The CRA must provide with the notice above (in writing not later than 5 business days after the date of the reinsertion) the following:

(1) A statement that the disputed information has been reinserted;

(2) The business name and address of:

(a) Any furnisher of information contacted and the telephone number of such furnisher, if reasonably available, or

(b) Any furnisher of information that contacted the consumer reporting agency, in connection with the reinsertion of such information; and

(c) A notice that the consumer has the right to add a statement to the consumer's file disputing the

accuracy or completeness of the disputed information.

4. Procedures to prevent reappearance.--A CRA shall maintain reasonable procedures designed to prevent the reappearance in a consumer's file, and in consumer reports on the consumer, of information that is deleted pursuant to the dispute procedure (other than information that is reinserted in accordance with the above rules).

5. Expedited dispute resolution. If a dispute regarding an item of information in a consumer's file at a consumer reporting agency is resolved by the deletion of the disputed information by not later than 3 **business** days after the date on which the agency receives notice of the dispute from the consumer, then the CRA does not have to:

   a) Notify the furnisher of the information;

   b) Formally notify the consumer of the results; or

   c) Provide a description of the reinvestigation procedure.

   d) However, it MUST still provide:

      (1) Prompt notice of the deletion to the consumer by telephone;

      (2) In the notice a statement of the consumer's right to request that the CRA notify the following persons of any notation regarding disputed information provided that the consumer specifically designate this person to receive notice.

         (a) A user who received a consumer report for employment purposes within the prior two years.

         (b) A user who received a consumer report for any other purpose within the last six months.

      (3) Written confirmation of the deletion and a copy of a consumer report on the consumer that is based on the consumer's file after the deletion, not later than 5 **business** days after making the deletion.

6. Duties regarding obsolete information.

a) Reporting of obsolete adverse action is prohibited under FCRA

b) Unless otherwise specified, the following information is considered "obsolete" and cannot be included in a CRAs consumer report (Note: this is adverse information; favorable information that is old may be included in the report):

(1) Bankruptcy adjudications more than 10 years old.

(2) Other categories for 7 years. Included are:

(a) Paid tax liens,

(b) Accounts placed for collection or charged to profit and loss,

(c) Suits and judgments which, from date of entry, antedate the consumer report by more than 7 years or until the governing statute of limitations has expired, whichever is the longer period,

(d) Any other adverse item of information that antedates the consumer report by more than 7 years.

(3) Records of criminal arrest, indictment, which, from the date of disposition, release, or parole, antedate the consumer report by more than 7 years, or the expiration of the statute of limitations, whichever is longer (note criminal convictions are NEVER obsolete)

(4) The 10 year time period for bankruptcies begins to run on the date of filing. On other transactions it is the date of the occurrence of the event, not the date acquired by the credit reporting agency.

(5) The 7-year period shall begin, with respect to any delinquent account that is placed for collection (internally or by referral to a third party, whichever is earlier), charged to profit and loss, or subjected to any

similar action, upon the expiration of the 180-day period beginning on the date of the commencement of the delinquency.

c) Inclusion of "adverse" obsolete information. "Obsolete" information **CAN** be included in the consumer report IF the report is intended for use involving (15 U.S.C. § 1681c):

(1) The consumer's participation in a credit transaction of $150,000 or more. (e.g. home mortgage)

(2) Issuance of life insurance coverage on the consumer of $150,000 or more.

(3) Employment of the consumer at an annual salary of $75,000 or more.

d) In order to insure that the obsolete information is provided only for the three above circumstances the CRA must maintain procedures which require that prospective users of information, identify themselves, certify the purposes for which the information is sought and certify that the information will be used for no other purposes

G. Obligations of users.

1. Adverse actions. If the user takes “adverse action” based upon a consumer credit report, the following requirements apply.

2. The user MUST:

a) Provide oral, written, or electronic notice of the adverse action to the consumer; AND

b) Provide to the consumer orally, in writing, or electronically--

(1) The name, address, and telephone number of the CRA (including a toll-free telephone number established by the agency if the agency compiles and maintains files on consumers on a nationwide basis) that furnished the report to the person; AND

(2) A statement that the consumer reporting agency did not make the decision to take the adverse action and is unable to provide the consumer the specific reasons why the adverse action was taken; AND

(3) Provide to the consumer an oral, written, or electronic notice of the consumer's right--

(a) To obtain a FREE copy of a consumer report from the CRA, including notice that the request must be made with 60 days; AND

(b) To dispute the accuracy or completeness of any information in the consumer report.

3. Special Rule for Adverse Action in Employment Situations. **Before taking any adverse action** based in whole or in part on the report, the person intending to take such adverse action shall provide to the consumer to whom the report relates--

a) A copy of the report; AND

b) A description in writing of the rights of the consumer under the FCRA.

4. Users must provide consumers with a Risk-based pricing notice.

a) Whenever creditor extends terms “materially less favorable than the most favorable terms available to substantial proportion of the consumers" It requires creditor to notify consumer when the offered terms are not as good as those offered to other consumers.

(1) Thus a car dealer who only discusses with the consumer a high interest loan, and the consumer may just be happy with getting a loan, now must be told that other consumers get 0% rate loans.

(2) Also a car dealer which takes a 4% yield spread must provide the risk-based pricing notice to the consumer.

b) Must be given at time of application or at the time of communication of approval.

c) May be given orally, in writing, or electronically

H. Obligations of Furnishers of Information to CRAs

1. Consumers may dispute furnished information directly with the furnisher. (change under FACTA)

a) The furnisher must investigate the dispute and report the results back to the consumer in the same time period as the CRA.

b) If the furnisher finds the information to be inaccurate they must correct the information with each agency to which they furnished the information.

c) Reinvestigation responsibility can not be initiated by notice from a credit repair organization

d) Consumers should send own disputes to furnishers instead of directly from lawyers.

2. Requirements to provide accurate information.

a) Prohibitions

(1) Furnishers shall not report information if they ***know or have reasonable cause to believe is inaccurate*** the standard until 2004 was *know or consciously avoid knowing that the information is inaccurate*.

(a) However, they can avoid this requirement by providing an address for consumers to notify them of errors.

(b) They are NOT required to provide such address, but if they do, they fall under paragraph 2 below.

(2) The furnisher must take action to block unverifiable information to prevent it from re-reporting the inaccurate information.

(3) A person shall not report information if

(a) the consumer has notified him (at the address the person has specified for this purpose) that specific information is not accurate; AND

(b) The information is *in fact* not accurate.

(c) May not make adverse reports relating to creditworthiness resulting from a consumer's application to reduce financial obligations as permitted by the SSCRA (e.g. reduce interests rate or delay repossessions, foreclosures, or lawsuits).

b) Duties to correct and update information

(1) Applies ONLY to persons who "regularly and in the ordinary course of business" furnish information to CRAs AND who have reported information that they determine is not complete or accurate.

(2) Such persons MUST

(a) Notify the CRA.

(b) Provide the CRA with necessary corrections or additional information.

(c) NOT provide the inaccurate information thereafter.

c) Duties to provide CRAs with certain notices.

(1) Any person who provided information to CRAs must provide notice that the accuracy of the information is disputed if the person providing the information is notified of the dispute.

(2) Any person who regularly and in the ordinary course of business notifies CRAs of information regarding a consumer who has a credit account with that person SHALL notify the CRA if the consumer voluntarily closes the account.

(3) Any person who notifies a CRA that a delinquent account is being placed in collection MUST, with 90 days, notify the CRA of the month and year of the delinquency that immediately preceded the action.

3. Duties When Notified of a Dispute. After receiving proper notice of a dispute, the person providing the information SHALL:

a) Conduct an investigation with respect to the disputed information;

b) Review all relevant information provided by the CRA pursuant to the dispute procedure in the FCRA;

c) Report the results of the investigation to the CRA; and

d) If the investigation finds that the information is incomplete or inaccurate, report those results to all other consumer reporting agencies to which the person furnished the information and that compile and maintain files on consumers on a nationwide basis.

e) The person MUST complete all investigations, reviews, and reports required within 30 days from the receipt of notice of the dispute.

I. Consumer Rights.

1. FTC must actively publicize and post on internet site "Summary of Rights" to obtain and dispute information in consumer reports and to obtain credit scores.

a) The right of the consumer to obtain a copy of a consumer report.

b) The frequency and circumstances under which the consumer can receive a free consumer report.

c) The right of the consumer to dispute information in their file.

d) The right of the consumer to obtain a credit score, and how to obtain a credit score.

e) The methods to contact and obtain the consumer reports.

2. Consumer reporting agency must provide consumers with the above "Summary of Rights" and the below additional "Summary of Rights**"** every time a consumer receives a written report from a CRA. The FTC requirement includes:

a) A brief description of the FCRA

b) A summary of all the consumer rights under the act including right to dispute information and obtain credit scores

c) An explanation on how the consumer can exercise those rights

d) A toll free number, which is staffed 24 hours a day

e) A statement that the agency is not required to remove accurate information that is not obsolete

f) A list of all Federal enforcement agencies

g) A reminder that the consumer may have additional rights under State law.

3. Access to Credit File

a) Upon request, consumers can obtain (15 U.S.C. § 1681g):

(1) ALL information in their file.

(2) Credit scores – the scores generally fall from low of 300 to high of 850, a borrower with a score of 660 or greater is generally considered to be less of a risk to a lender.

(3) The Source of the information.

(4) The identities of those who have received the report:

(a) Within the past 2 years for employment purposes.

(b) Within the past 6 months for other purposes.

(5) Websites and phone numbers to order reports from big three

(a) www.experian.com 1-(888) 397-3742

(b) www.transunion.com 1-(800) 916-8800

(c) www.equifax.com 1-(800) 997-2493

b) Consumer Copy of the Credit Report

(1) Each of the Nationwide Agencies must provide consumers a free annual credit report starting December 04. The request must be made through a FTC established centralized source and the agency has 15 days to send the report. Free annual reports may be obtained online at www.annualcreditreport.com or by calling (877) 322-8228.

(2) If the consumer wants additional reports other than for adverse actions the CRA may charge a reasonable fee for the disclosures to the consumer.

(3) The reasonable fee is adjusted by the FTC each January 1 based upon the CPI. The fee shall be disclosed to the consumer prior to issuing the information.

(4) If an adverse action has been taken or the consumer is a victim of fraud they are is entitled to a free copy of the credit report

(a) Free reports will also be given during any 12 month period to anyone:

(i) Who is unemployed and intends to apply for employment within the next 60 day period (certified by consumer)

(ii) Is receiving welfare;

(5) Credit Scores

(a) The FCRA requires that agencies disclose to the consumer:

(i) their credit score

(ii) the range of possible scores under the scoring model

(iii) the key factors that adversely affected the score

(iv) the date the credit score was created

(v) the name of the person or entity that created the credit score or credit file upon which the credit score was created.

(b) The agencies can charge a reasonable fee.

(c) Mortgage lenders must disclose credit scores and key factors to the consumer.

4. Dispute/Correct the Information

5. Statement of dispute (100-WORD STATEMENT.) If the reinvestigation does not resolve the dispute, the consumer may file a brief statement setting forth the nature of the dispute. The consumer reporting agency may limit such statements to not more than one hundred words if it provides the consumer with assistance in writing a clear summary of the dispute. The CRA must include the statement in every report that contains the disputed entry.

J. Fraud Alerts

1. Types of Fraud Alerts

a) Initial fraud alerts good for 90 days. The consumer only needs to contact one consumer reporting agency. The agency then must alert the other nationwide agencies and all must include a fraud alert in the consumer's file and provide the alert each

time they generate the consumer's credit score. Agency must provide file to consumer within 3 days.

b) Extended Fraud alerts. The consumer can add an extended fraud alert that lasts for as long as 7 years. The agency must exclude the consumer from any lists generated to sell to users for 5 years and must notify consumer of right to 2 free credit reports within 12 months of request.

c) Active Military Duty Alerts. Consumers on active duty including reservists (other than their normal place of duty) can add an alert of status to their files. The alert is in effect for 12 months; however the military consumer is excluded from any list generated to sell to users for 2 years.

2. Substance of alerts and users' responsibilities to verify identity

a) The alerts must state that the consumer does not authorize new credit, an additional card on existing account, or increase in credit limit.

b) Users may not proceed with a credit transaction unless the user "utilizes reasonable policies and procedures to form a reasonable belief that the user knows the identity of the person making the request.

c) Consumers can provides a phone number for the User to call, however it is an initial fraud report or an active duty alert that user can "take reasonable steps" other than calling.

K. Remedies.

1. Civil liability for <u>willful</u> noncompliance (15 U.S.C. § 1681n) - actual damages, not less than $100, not more than $1,000, punitive damages, and court costs and reasonable attorney's fees if the consumer prevails.

2. Civil liability for <u>negligent</u> noncompliance (15 U.S.C. § 1681o) -actual damages plus court costs and reasonable attorney's fees if the consumer prevails.

3. So if the consumer disputed the information and the agency did not properly respond to the consumer's dispute the agency can be held liable.

a) No strict liability for all inaccuracies.

b) Defenses:

(1) Agencies escape liability by proving the reinvestigation was reasonable to determine whether the disputed information is accurate.

4. Statute of Limitations (15 U.S.C. § 1681p). 2 years from date that consumer discovers violation. Consumer must bring action within 5 years of the date of the violation regardless of discovery.

5. Consumer has burden to prove inaccurate credit report has causal connection to denial of credit or employment or other consumer benefit. *Cahlin v. General Motors Acceptance Corp.*, 936 F.2d 1151 (11th Cir. 1991).

6. Criminal penalties - obtaining information under false pretenses (15 U.S.C. § 1681q) – or if an agent for a consumer reporting agency who knowingly and willfully provides information concerning an individual from the agency's files to a person not authorized to receive the information. Fine pursuant to title 18, United States Code, or imprisonment for not more than 2 years, or both.

7. Administrative enforcement by FTC

8. State enforcement limited

L. Child Support Enforcement.

1. CRAs will include in consumer reports furnished by the agency any information on the failure of consumer to pay overdue support which is provided:

a) To the CRA by a state or local child support enforcement agency, or

b) To the CRA and verified by any local, state, or federal government agency, and

c) Antedates the report by 7 years or less.

III. IDENTITY THEFT

A. Resources

1. Identity Theft and Assumption Deterrence Act, 18 U.S.C. §§ 928(b)(1), 1028.

2. NATIONAL CONSUMER LAW CENTER, FAIR CREDIT REPORTING ACT §13.5.5 and § 16.6 (5th ed. 2002 and Supp. 2005).

3. www.consumer.gov/idtheft

4. The Federal Fair and Accurate Credit Transactions Act of 2003, Pub. L. No. 108-159 (Dec. 4, 2003).

B. Nature

1. Impostor's use of key items of another person's identity, such as name, social security number, credit card number, or PIN to obtain funds, credit, goods, services, or benefits.

2. Thief finds social security number in stolen wallet, stolen documents, stolen mail and over the internet and uses the social security number it to apply for credit cards, checking accounts, loans, utility service, obtain employment and government benefits.

3. One of the fastest growing financial crimes, the FTC has reported to congress in 2002 that they get 3000 calls a week to their toll free identity theft hotline. (1-877-ID-THEFT (438-4338), resulting in over two billion dollars of credit fraud loss each year.

4. The fraud does not come to light until victim is denied a loan or some other kind of credit or in the worse case scenario is arrested for writing bad checks. The average time according to the FTC to discover the fraud is a little over 12 months. 87% had no connection with the thief and 80% of the victims were unaware of what might explain the theft such as loss of their wallet.

C. Identity Theft and Assumption Deterrence Act

1. Under the act one who transfers or uses another's identification with the intent to commit, or aid or abet a violation of federal law or a felony under state law commits a federal crime.

2. Act requires FTC to set up a centralized complaint department to receive reports from identity theft victims, provide informational materials to the victims, and refer the complaints to appropriate entities.

3. Forces law enforcement to see the ones whom the Identify was stolen from as the victims of the crime, instead of the banks or credit card companies who are out the money.

4. The act does not regulate the crediting reporting agencies and a consumer has to rely on the FCRA to try to clean up credit record.

5. The act also does not require creditors to exercise care in extending credit.

6. There are individual state statutes on identity theft and many of them give more protections than the Federal statute, so try that route.

D. Coping actions for victims of identity theft:

1. Contact fraud units of one of the Credit Reporting Agencies (Experian, Equifax, Trans Union) and ask that a fraud alert be added to their file and that the agency delete the fraudulent information. The consumer must provide the CRA with proof of identity, a copy of an identity theft report either to law enforcement or another government agency, and a statement that the disputed information is a result of the identity theft and not the actions of the consumer.

2. Within four days, the CRA must block the disputed information and notify the creditor, who must conduct a reinvestigation. Once the creditor receives notice of the fraud, the creditor is prohibited from selling or transferring the debt to a collection agency.

3. The agency then must alert the other nationwide agencies and all must include a fraud alert in the consumer's file and provide the alert each time they generate the consumer's credit score. Agency must provide file to consumer within 3 days.

4. The fraud alert is only good for 90 days unless the consumer adds an extended fraud alert that lasts for as long as 7 years. The agency must exclude the consumer from any lists generated to sell to users for 5 years and must notify consumer of right to 2 free credit reports within 12 months of request.

    a) Fraud numbers (only need to contact one)

        (1) Equifax: (800) 525-6285

        (2) TransUnion: (800) 680-7289

        (3) Experian: (888) 397-3742

    b) To determine if the identity thief has been writing bad checks in the consumer's name, call SCAN at (800) 262-7771.

    c) To inform retail businesses to stop accepting checks drawn on a fraudulent account in the consumer's name contact Telecheck ((800) 710-9898 or (800) 927-0188)) and Certegy ((800) 437-5120).

5. File report with each law enforcement agency with jurisdiction and get copy of the report. If additional accounts are discovered, file a new police report. A police report can help tremendously in dealing with credit card companies and other businesses.

6. Ask CRA for names/numbers of fraudulent accounts.

7. Ask CRA to remove inquiries generated due to fraudulent access.

8. Contact all creditors who have granted credit of fraudulent accounts by telephone and in writing and notify of fraud and close those accounts. The victim should get new account numbers and cards for misused accounts and ask that all others be processed as "account closed at consumer's request." Also ask them for copies of the fraudulent credit application, and bills on the accounts and copies of information they sent to credit reporting agency.

9. Victim should contact all creditors for which a credit report has been released but no accounts have been opened yet and tell them not to open accounts.

10. If social security has been used, notify the Social Security Administration and if Driver's license number has been used contact their state department of registry of motor vehicles.

11. Fill out a ID theft affidavit at www.consumer.gov/idtheft/affadavit

12. Go to the FTC website listed in the resource paragraph above for more detailed information on how to combat Identity theft.

13. Continue to monitor credit report by requesting new credit reports form the big three reporting agencies every three months

E. Agencies, Furnishers and Creditors Actions

1. Must block identity theft information under FACTA within 4 days of receiving:

   a) proof of the consumer's identity

   b) copy of ID theft report

   c) consumer's identification of fraudulent information

   d) consumer's statement that the information does relate to any transaction by them

2. The agencies must notify furnishes of the block.

3. The furnishers must implement procedures to keep from re-furnishing the information.

   a) The consumer can notify the furnisher directly

   b) Furnishers may not sell or place for collection the identity theft related information

4. If agency rescinds block, must notify consumer within 5 business days with specific reason for recession.

5. Financial institutions and creditors must establish reasonable policies and procedures for implementing to be issued "red flag" guidelines regarding identity theft.

6. FTC – has to develop new summary of rights for identity theft and fraud victims

IV. CONCLUSION.

APPENDIX A

THE FAIR DEBT COLLECTION PRACTICES ACT

§ 1692. Congressional findings and declaration of purpose

(a) Abusive practices. There is abundant evidence of the use of abusive, deceptive, and unfair debt collection practices by many debt collectors. Abusive debt collection practices contribute to the number of personal bankruptcies, to marital instability, to the loss of jobs, and to invasions of individual privacy.

(b) Inadequacy of laws. Existing laws and procedures for redressing these injuries are inadequate to protect consumers.

(c) Available non-abusive collection methods. Means other than misrepresentation or other abusive debt collection practices are available for the effective collection of debts.

(d) Interstate commerce. Abusive debt collection practices are carried on to a substantial extent in interstate commerce and through means and instrumentalities of such commerce. Even where abusive debt collection practices are purely intrastate in character, they nevertheless directly affect interstate commerce.

(e) Purposes. It is the purpose of this *title [15 USCS § § 1692* et seq.] to eliminate abusive debt collection practices by debt collectors, to insure that those debt collectors who refrain from using abusive debt collection practices are not competitively disadvantaged, and to promote consistent State action to protect consumers against debt collection abuses.

§ 1692a. Definitions

As used in this *title [15 USCS § § 1692* et seq.]--

(1) The term "Commission" means the Federal Trade Commission.

(2) The term "communication" means the conveying of information regarding a debt directly or indirectly to any person through any medium.

(3) The term "consumer" means any natural person obligated or allegedly obligated to pay any debt.

(4) The term "creditor" means any person who offers or extends credit creating a debt or to whom a debt is owed, but such term does not include any person to the extent that he receives an assignment or transfer of a debt in default solely for the purpose of facilitating collection of such debt for another.

(5) The term "debt" means any obligation or alleged obligation of a consumer to pay money arising out of a transaction in which the money, property, insurance, or services which are the subject of the transaction are primarily for personal, family, or household purposes, whether or not such obligation has been reduced to judgment.

(6) The term "debt collector" means any person who uses any instrumentality of interstate commerce or the mails in any business the principal purpose of which is the collection of any

debts, or who regularly collects or attempts to collect, directly or indirectly, debts owed or due or asserted to be owed or due another. Notwithstanding the exclusion provided by clause (F) of the last sentence of this paragraph, the term includes any creditor who, in the process of collecting his own debts, uses any name other than his own which would indicate that a third person is collecting or attempting to collect such debts. For the purpose of section 808(6) [*15 USCS § 1692f(6)*], such term also includes any person who uses any instrumentality of interstate commerce or the mails in any business the principal purpose of which is the enforcement of security interests. The term does not include--

(A) any officer or employee of a creditor while, in the name of the creditor, collecting debts for such creditor;

(B) any person while acting as a debt collector for another person, both of whom are related by common ownership or affiliated by corporate control, if the person acting as a debt collector does so only for persons to whom it is so related or affiliated and if the principal business of such person is not the collection of debts;

(C) any officer or employee of the United States or any State to the extent that collecting or attempting to collect any debt is in the performance of his official duties;

(D) any person while serving or attempting to serve legal process on any other person in connection with the judicial enforcement of any debt;

(E) any nonprofit organization which, at the request of consumers, performs bona fide consumer credit counseling and assists consumers in the liquidation of their debts by receiving payments from such consumers and distributing such amounts to creditors; and

(F) any person collecting or attempting to collect any debt owed or due or asserted to be owed or due another to the extent such activity (i) is incidental to a bona fide fiduciary obligation or a bona fide escrow arrangement; (ii) concerns a debt which was originated by such person; (iii) concerns a debt which was not in default at the time it was obtained by such person; or (iv) concerns a debt obtained by such person as a secured party in a commercial credit transaction involving the creditor.

(7) The term "location information" means a consumer's place of abode and his telephone number at such place, or his place of employment.

(8) The term "State" means any State, territory, or possession of the United States, the District of Columbia, the Commonwealth of Puerto Rico, or any political subdivision of any of the foregoing.

§ 1692b. Acquisition of location information

Any debt collector communicating with any person other than the consumer for the purpose of acquiring location information about the consumer shall--

(1) identify himself, state that he is confirming or correcting location information concerning the consumer, and, only if expressly requested, identify his employer;

(2) not state that such consumer owes any debt;

(3) not communicate with any such person more than once unless requested to do so by such person or unless the debt collector reasonably believes that the earlier response of such person is erroneous or incomplete and that such person now has correct or complete location information;

(4) not communicate by post card;

(5) not use any language or symbol on any envelope or in the contents of any communication effected by the mails or telegram that indicates that the debt collector is in the debt collection business or that the communication relates to the collection of a debt; and

(6) after the debt collector knows the consumer is represented by an attorney with regard to the subject debt and has knowledge of, or can readily ascertain, such attorney's name and address, not communicate with any person other than that attorney, unless the attorney fails to respond within a reasonable period of time to communication from the debt collector.

§ 1692c. Communication in connection with debt collection

(a) Communication with the consumer generally. Without the prior consent of the consumer given directly to the debt collector or the express permission of a court of competent jurisdiction, a debt collector may not communicate with a consumer in connection with the collection of any debt--

(1) at any unusual time or place or a time or place known or which should be known to be inconvenient to the consumer. In the absence of knowledge of circumstances to the contrary, a debt collector shall assume that the convenient time for communicating with a consumer is after 8 o'clock antimeridian and before 9 o'clock postmeridian, local time at the consumer's location;

(2) if the debt collector knows the consumer is represented by an attorney with respect to such debt and has knowledge of, or can readily ascertain, such attorney's name and address, unless the attorney fails to respond within a reasonable period of time to a communication from the debt collector or unless the attorney consents to direct communication with the consumer; or

(3) at the consumer's place of employment if the debt collector knows or has reason to know that the consumer's employer prohibits the consumer from receiving such communication.

(b) Communication with third parties. Except as provided in section 804 [*15 USCS § 1692b*], without the prior consent of the consumer given directly to the debt collector, or the express permission of a court of competent jurisdiction, or as reasonably necessary to effectuate a post-judgment judicial remedy, a debt collector may not communicate, in connection with the collection of any debt, with any person other than the consumer, his attorney, a consumer reporting agency if otherwise permitted by law, the creditor, the attorney of the creditor, or the attorney of the debt collector.

(c) Ceasing communication. If a consumer notifies a debt collector in writing that the consumer refuses to pay a debt or that the consumer wishes the debt collector to cease further communication with the consumer, the debt collector shall not communicate further with the consumer with respect to such debt, except--

(1) to advise the consumer that the debt collector's further efforts are being terminated;

(2) to notify the consumer that the debt collector or creditor may invoke specified remedies which are ordinarily invoked by such debt collector or creditor; or

(3) where applicable, to notify the consumer that the debt collector or creditor intends to invoke a specified remedy. If such notice from the consumer is made by mail, notification shall be complete upon receipt.

(d) "Consumer" defined. For the purpose of this section, the term "consumer" includes the consumer's spouse, parent (if the consumer is a minor), guardian, executor, or administrator.

§ 1692d. Harassment or abuse

A debt collector may not engage in any conduct the natural consequence of which is to harass, oppress, or abuse any person in connection with the collection of a debt. Without limiting the general application of the foregoing, the following conduct is a violation of this section:

(1) The use or threat of use of violence or other criminal means to harm the physical person, reputation, or property of any person.

(2) The use of obscene or profane language or language the natural consequence of which is to abuse the hearer or reader.

(3) The publication of a list of consumers who allegedly refuse to pay debts, except to a consumer reporting agency or to persons meeting the requirements of section 603(f) or 604(3) of this Act [*15 USCS § § 1681a(f)* or *1681b(3)*].

(4) The advertisement for sale of any debt to coerce payment of the debt.

(5) Causing a telephone to ring or engaging any person in telephone conversation repeatedly or continuously with intent to annoy, abuse, or harass any person at the called number.

(6) Except as provided in section 804 [*15 USCS § 1692b*], the placement of telephone calls without meaningful disclosure of the caller's identity.

§ 1692e. False or misleading representations

A debt collector may not use any false, deceptive, or misleading representation or means in connection with the collection of any debt. Without limiting the general application of the foregoing, the following conduct is a violation of this section:

(1) The false representation or implication that the debt collector is vouched for, bonded by, or affiliated with the United States or any State, including the use of any badge, uniform, or facsimile thereof.

(2) The false representation of--

(A) the character, amount, or legal status of any debt; or

(B) any services rendered or compensation which may be lawfully received by any debt collector for the collection of a debt.

(3) The false representation or implication that any individual is an attorney or that any communication is from an attorney.

(4) The representation or implication that nonpayment of any debt will result in the arrest or imprisonment of any person or the seizure, garnishment, attachment, or sale of any property or wages of any person unless such action is lawful and the debt collector or creditor intends to take such action.

(5) The threat to take any action that cannot legally be taken or that is not intended to be taken.

(6) The false representation or implication that a sale, referral, or other transfer of any interest in a debt shall cause the consumer to--

(A) lose any claim or defense to payment of the debt; or

(B) become subject to any practice prohibited by this *title [15 USCS § § 1692* et seq.].

(7) The false representation or implication that the consumer committed any crime or other conduct in order to disgrace the consumer.

(8) Communicating or threatening to communicate to any person credit information which is known or which should be known to be false, including the failure to communicate that a disputed debt is disputed.

(9) The use or distribution of any written communication which simulates or is falsely represented to be a document authorized, issued, or approved by any court, official, or agency of the United States or any State, or which creates a false impression as to its source, authorization, or approval.

(10) The use of any false representation or deceptive means to collect or attempt to collect any debt or to obtain information concerning a consumer.

(11) The failure to disclose in the initial written communication with the consumer and, in addition, if the initial communication with the consumer is oral, in that initial oral communication, that the debt collector is attempting to collect a debt and that any information obtained will be used for that purpose, and the failure to disclose in subsequent communications that the communication is from a debt collector, except that this paragraph shall not apply to a formal pleading made in connection with a legal action.

(12) The false representation or implication that accounts have been turned over to innocent purchasers for value.

(13) The false representation or implication that documents are legal process.

(14) The use of any business, company, or organization name other than the true name of the debt collector's business, company, or organization.

(15) The false representation or implication that documents are not legal process forms or do not require action by the consumer.

(16) The false representation or implication that a debt collector operates or is employed by a consumer reporting agency as defined by section 603(f) of this Act [*15 USCS § 1681a(f)*].

§ 1692f. Unfair practices

A debt collector may not use unfair or unconscionable means to collect or attempt to collect any debt. Without limiting the general application of the foregoing, the following conduct is a violation of this section:

(1) The collection of any amount (including any interest, fee, charge, or expense incidental to the principal obligation) unless such amount is expressly authorized by the agreement creating the debt or permitted by law.

(2) The acceptance by a debt collector from any person of a check or other payment instrument postdated by more than five days unless such person is notified in writing of the debt collector's intent to deposit such check or instrument not more than ten nor less than three business days prior to such deposit.

(3) The solicitation by a debt collector of any postdated check or other postdated payment instrument for the purpose of threatening or instituting criminal prosecution.

(4) Depositing or threatening to deposit any postdated check or other postdated payment instrument prior to the date on such check or instrument.

(5) Causing charges to be made to any person for communications by concealment of the true purpose of the communication. Such charges include, but are not limited to, collect telephone calls and telegram fees.

(6) Taking or threatening to take any nonjudicial action to effect dispossession or disablement of property if--

(A) there is no present right to possession of the property claimed as collateral through an enforceable security interest;

(B) there is no present intention to take possession of the property; or

(C) the property is exempt by law from such dispossession or disablement.

(7) Communicating with a consumer regarding a debt by post card.

(8) Using any language or symbol, other than the debt collector's address, on any envelope when communicating with a consumer by use of the mails or by telegram, except that a debt collector may use his business name if such name does not indicate that he is in the debt collection business.

§ 1692g. Validation of debts

(a) Notice of debt; contents. Within five days after the initial communication with a consumer in connection with the collection of any debt, a debt collector shall, unless the following information is contained in the initial communication or the consumer has paid the debt, send the consumer a written notice containing--

(1) the amount of the debt;

(2) the name of the creditor to whom the debt is owed;

(3) a statement that unless the consumer, within thirty days after receipt of the notice, disputes the validity of the debt, or any portion thereof, the debt will be assumed to be valid by the debt collector;

(4) a statement that if the consumer notifies the debt collector in writing within the thirty-day period that the debt, or any portion thereof, is disputed, the debt collector will obtain verification of the debt or a copy of a judgment against the consumer and a copy of such verification or judgment will be mailed to the consumer by the debt collector; and

(5) a statement that, upon the consumer's written request within the thirty-day period, the debt collector will provide the consumer with the name and address of the original creditor, if different from the current creditor.

(b) Disputed debts. If the consumer notifies the debt collector in writing within the thirty-day period described in subsection (a) that the debt, or any portion thereof, is disputed, or that the consumer requests the name and address of the original creditor, the debt collector shall cease collection of the debt, or any disputed portion thereof, until the debt collector obtains verification of the debt or a copy of a judgment, or the name and address of the original creditor, and a copy of such verification or judgment, or name and address of the original creditor, is mailed to the consumer by the debt collector. Collection activities and communications that do not otherwise violate this title may continue during the 30-day period referred to in subsection (a) unless the consumer has notified the debt collector in writing that the debt, or any portion of the debt, is disputed or that the consumer requests the name and address of the original creditor. Any collection activities and communication

during the 30-day period may not overshadow or be inconsistent with the disclosure of the consumer's right to dispute the debt or request the name and address of the original creditor.

(c) Admission of liability. The failure of a consumer to dispute the validity of a debt under this section may not be construed by any court as an admission of liability by the consumer.

(d) Legal pleadings. A communication in the form of a formal pleading in a civil action shall not be treated as an initial communication for purposes of subsection (a).

(e) Notice provisions. The sending or delivery of any form or notice which does not relate to the collection of a debt and is expressly required by the Internal Revenue Code of 1986 [*26 USCS § § 1* et seq.], title V of Gramm-Leach-Bliley Act [*15 USCS § § 6801* et seq.], or any provision of Federal or State law relating to notice of data security breach or privacy, or any regulation prescribed under any such provision of law, shall not be treated as an initial communication in connection with debt collection for purposes of this section.

§ 1692h. Multiple debts

If any consumer owes multiple debts and makes any single payment to any debt collector with respect to such debts, such debt collector may not apply such payment to any debt which is disputed by the consumer and, where applicable, shall apply such payment in accordance with the consumer's directions.

§ 1692i. Legal actions by debt collectors

(a) Venue. Any debt collector who brings any legal action on a debt against any consumer shall--

(1) in the case of an action to enforce an interest in real property securing the consumer's obligation, bring such action only in a judicial district or similar legal entity in which such real property is located; or

(2) in the case of an action not described in paragraph (1), bring such action only in the judicial district or similar legal entity--

(A) in which such consumer signed the contract sued upon; or

(B) in which such consumer resides at the commencement of the action.

(b) Authorization of actions. Nothing in this *title [15 USCS § § 1692* et seq.] shall be construed to authorize the bringing of legal actions by debt collectors.

§ 1692j. Furnishing certain deceptive forms

(a) It is unlawful to design, compile, and furnish any form knowing that such form would be used to create the false belief in a consumer that a person other than the creditor of such consumer is participating in the collection of or in an attempt to collect a debt such consumer allegedly owes such creditor, when in fact such person is not so participating.

(b) Any person who violates this section shall be liable to the same extent and in the same manner as a debt collector is liable under section 813 [*15 USCS § 1692k*] for failure to comply with a provision of this *title [15 USCS § § 1692* et seq.].

§ 1692k. Civil liability

(a) Amount of damages. Except as otherwise provided by this section, any debt collector who fails to comply with any provision of this *title [15 USCS § § 1692* et seq.] with respect to any person is liable to such person in an amount equal to the sum of--

(1) any actual damage sustained by such person as a result of such failure;

(2) (A) in the case of any action by an individual, such additional damages as the court may allow, but not exceeding $ 1,000; or

(B) in the case of a class action, (i) such amount for each named plaintiff as could be recovered under subparagraph (A), and (ii) such amount as the court may allow for all other class members, without regard to a minimum individual recovery, not to exceed the lesser of $ 500,000 or 1 per centum of the net worth of the debt collector; and

(3) in the case of any successful action to enforce the foregoing liability, the costs of the action, together with a reasonable attorney's fee as determined by the court. On a finding by the court that an action under this section was brought in bad faith and for the purpose of harassment, the court may award to the defendant attorney's fees reasonable in relation to the work expended and costs.

(b) Factors considered by court. In determining the amount of liability in any action under subsection (a), the court shall consider, among other relevant factors--

(1) in any individual action under subsection (a)(2)(A), the frequency and persistence of noncompliance by the debt collector, the nature of such noncompliance, and the extent to which such noncompliance was intentional; or

(2) in any class action under subsection (a)(2)(B), the frequency and persistence of noncompliance by the debt collector, the nature of such noncompliance, the resources of the debt collector, the number of persons adversely affected, and the extent to which the debt collector's noncompliance was intentional.

(c) Intent. A debt collector may not be held liable in any action brought under this *title [15 USCS § § 1692* et seq.] if the debt collector shows by a preponderance of evidence that the violation was not intentional and resulted from a bona fide error notwithstanding the maintenance of procedures reasonably adapted to avoid any such error.

(d) Jurisdiction. An action to enforce any liability created by this *title [15 USCS § § 1692* et seq.] may be brought in any appropriate United States district court without regard to the amount in controversy, or in any other court of competent jurisdiction, within one year from the date on which the violation occurs.

(e) Advisory opinions of Commission. No provision of this section imposing any liability shall apply to any act done or omitted in good faith in conformity with any advisory opinion of the Commission, notwithstanding that after such act or omission has occurred, such

opinion is amended, rescinded, or determined by judicial or other authority to be invalid for any reason.

§ 1692l. Administrative enforcement

(a) Federal Trade Commission. Compliance with this *title [15 USCS § § 1692* et seq.] shall be enforced by the Commission, except to the extent that enforcement of the requirements imposed under this *title [15 USCS § § 1692* et seq.] is specifically committed to another agency under subsection (b). For purpose of the exercise by the Commission of its functions and powers under the Federal Trade Commission Act [*15 USCS § § 41* et seq.], a violation of this *title [15 USCS § § 1692* et seq.] shall be deemed an unfair or deceptive act or practice in violation of that Act [*15 USCS § § 41* et seq.]. All of the functions and powers of the Commission under the Federal Trade Commission Act [*15 USCS § § 41* et seq.] are available to the Commission to enforce compliance by any person with this *title [15 USCS § § 1692* et seq.], irrespective of whether that person is engaged in commerce or meets any other jurisdictional tests in the Federal Trade Commission Act [*15 USCS § § 41* et seq.], including the power to enforce the provisions of this *title [15 USCS § § 1692* et seq.] in the same manner as if the violation had been a violation of a Federal Trade Commission trade regulation rule.

(b) Applicable provisions of law. Compliance with any requirements imposed under this *title [15 USCS § § 1692* et seq.] shall be enforced under--

(1) section 8 of the Federal Deposit Insurance Act [*12 USCS § 1818*], in the case of--

(A) national banks, and Federal branches and Federal agencies of foreign banks, by the Office of the Comptroller of the Currency;

(B) member banks of the Federal Reserve System (other than national banks), branches and agencies of foreign banks (other than Federal branches, Federal agencies, and insured State branches of foreign banks), commercial lending companies owned or controlled by foreign banks, and organizations operating under section 25 or 25(a) [25A] of the Federal Reserve Act [*12 USCS § § 601* et seq. or *§ § 611* et seq.], by the Board of Governors of the Federal Reserve System; and

(C) banks insured by the Federal Deposit Insurance Corporation (other than members of the Federal Reserve System) and insured State branches of foreign banks, by the Board of Directors of the Federal Deposit Insurance Corporation;

(2) section 8 of the Federal Deposit Insurance Act [*12 USCS § 1818*], by the Director of the Office of Thrift Supervision, in the case of a savings association the deposits of which are insured by the Federal Deposit Insurance Corporation;

(3) the Federal Credit Union Act [*12 USCS § § 1751* et seq.], by the Administrator of the National Credit Union Administration [National Credit Union Administration Board] with respect to any Federal credit union;

(4) the Acts to regulate commerce [*49 USCS § § 10101* et seq.], by the Secretary of Transportation, with respect to all carriers subject to the jurisdiction of the Surface Transportation Board;

(5) the Federal Aviation Act of 1958 [*49 USCS § § 40101* et seq.], by the Secretary of Transportation with respect to any air carrier or any foreign air carrier subject to that Act [*49 USCS § § 40101* et seq.]; and

(6) the Packers and Stockyards Act, 1921 [*7 USCS § § 181* et seq.] (except as provided in section 406 of that Act [*7 USCS § § 226* and *227*]), by the Secretary of Agriculture with respect to any activities subject to that Act [*7 USCS § § 181* et seq.].

The terms used in paragraph (1) that are not defined in this *title [15 USCS § § 1692* et seq.] or otherwise defined in section 3(s) of the Federal Deposit Insurance Act (*12 U.S.C. 1813(s)*) shall have the meaning given to them in section 1(b) of the International Banking Act of 1978 (*12 U.S.C. 3101*).

(c) Agency powers. For the purpose of the exercise by any agency referred to in subsection (b) of its powers under any Act referred to in that subsection, a violation of any requirement imposed under this *title [15 USCS § § 1692* et seq.] shall be deemed to be a violation of a requirement imposed under that Act. In addition to its powers under any provision of law specifically referred to in subsection (b), each of the agencies referred to in that subsection may exercise, for the purpose of enforcing compliance with any requirement imposed under this *title [15 USCS § § 1692* et seq.] any other authority conferred on it by law, except as provided in subsection (d).

(d) Rules and regulations. Neither the Commission nor any other agency referred to in subsection (b) may promulgate trade regulation rules or other regulations with respect to the collection of debts by debt collectors as defined in this *title [15 USCS § § 1692* et seq.].

§ 1692m. Reports to Congress by the Commission; views of other Federal agencies

(a) Not later than one year after the effective date of this title and at one-year intervals thereafter, the Commission shall make reports to the Congress concerning the administration of its functions under this *title [15 USCS § § 1692* et seq.], including such recommendations as the Commission deems necessary or appropriate. In addition, each report of the Commission shall include its assessment of the extent to which compliance with this *title [15 USCS § § 1692* et seq.] is being achieved and a summary of the enforcement actions taken by the Commission under section 814 of this *title [15 USCS § 1692l*]

(b) In the exercise of its functions under this *title [15 USCS § § 1692* et seq.], the Commission may obtain upon request the views of any other Federal agency which exercises enforcement functions under section 814 of this *title [15 USCS § 1692l*].

§ 1692n. Relation to State laws

This *title [15 USCS § § 1692* et seq.] does not annul, alter, or affect, or exempt any person subject to the provisions of this *title [15 USCS § § 1692* et seq.] from complying with the laws of any State with respect to debt collection practices, except to the extent that those laws are inconsistent with any provision of this *title [15 USCS § § 1692* et seq.], and then only to the extent of the inconsistency. For purposes of this section, a State law is not inconsistent with this *title [15 USCS § § 1692* et seq.] if the protection such law affords any consumer is greater than the protection provided by this *title [15 USCS § § 1692* et seq.].

§ 1692o. Exemption for State regulation

The Commission shall by regulation exempt from the requirements of this *title [15 USCS § § 1692* et seq.] any class of debt collection practices within any State if the Commission determines that under the law of that State that class of debt collection practices is subject to requirements substantially similar to those imposed by this *title [15 USCS § § 1692* et seq.], and that there is adequate provision for enforcement.

§ 1692p. Exception for certain bad check enforcement programs operated by private entities

(a) In general.

(1) Treatment of certain private entities. Subject to paragraph (2), a private entity shall be excluded from the definition of a debt collector, pursuant to the exception provided in section 803(6) [*15 USCS § 1692a(6)*], with respect to the operation by the entity of a program described in paragraph (2)(A) under a contract described in paragraph (2)(B).

(2) Conditions of applicability. Paragraph (1) shall apply if--

(A) a State or district attorney establishes, within the jurisdiction of such State or district attorney and with respect to alleged bad check violations that do not involve a check described in subsection (b), a pretrial diversion program for alleged bad check offenders who agree to participate voluntarily in such program to avoid criminal prosecution;

(B) a private entity, that is subject to an administrative support services contract with a State or district attorney and operates under the direction, supervision, and control of such State or district attorney, operates the pretrial diversion program described in subparagraph (A); and

(C) in the course of performing duties delegated to it by a State or district attorney under the contract, the private entity referred to in subparagraph (B)--

(i) complies with the penal laws of the State;

(ii) conforms with the terms of the contract and directives of the State or district attorney;

(iii) does not exercise independent prosecutorial discretion;

(iv) contacts any alleged offender referred to in subparagraph (A) for purposes of participating in a program referred to in such paragraph--

(I) only as a result of any determination by the State or district attorney that probable cause of a bad check violation under State penal law exists, and that contact with the alleged offender for purposes of participation in the program is appropriate; and

(II) the alleged offender has failed to pay the bad check after demand for payment, pursuant to State law, is made for payment of the check amount;

(v) includes as part of an initial written communication with an alleged offender a clear and conspicuous statement that--

(I) the alleged offender may dispute the validity of any alleged bad check violation;

(II) where the alleged offender knows, or has reasonable cause to believe, that the alleged bad check violation is the result of theft or forgery of the check, identity theft, or other fraud that is not the result of the conduct of the alleged offender, the alleged offender may file a crime report with the appropriate law enforcement agency; and

(III) if the alleged offender notifies the private entity or the district attorney in writing, not later than 30 days after being contacted for the first time pursuant to clause (iv), that there is a dispute pursuant to this subsection, before further restitution efforts are pursued, the district attorney or an employee of the district attorney authorized to make such a determination makes a determination that there is probable cause to believe that a crime has been committed; and

(vi) charges only fees in connection with services under the contract that have been authorized by the contract with the State or district attorney.

(b) Certain checks excluded. A check is described in this subsection if the check involves, or is subsequently found to involve--

(1) a postdated check presented in connection with a payday loan, or other similar transaction, where the payee of the check knew that the issuer had insufficient funds at the time the check was made, drawn, or delivered;

(2) a stop payment order where the issuer acted in good faith and with reasonable cause in stopping payment on the check;

(3) a check dishonored because of an adjustment to the issuer's account by the financial institution holding such account without providing notice to the person at the time the check was made, drawn, or delivered;

(4) a check for partial payment of a debt where the payee had previously accepted partial payment for such debt;

(5) a check issued by a person who was not competent, or was not of legal age, to enter into a legal contractual obligation at the time the check was made, drawn, or delivered; or

(6) a check issued to pay an obligation arising from a transaction that was illegal in the jurisdiction of the State or district attorney at the time the check was made, drawn, or delivered.

(c) Definitions. For purposes of this section, the following definitions shall apply:

(1) State or district attorney. The term "State or district attorney" means the chief elected or appointed prosecuting attorney in a district, county (as defined in *section 2 of title 1, United States Code*), municipality, or comparable jurisdiction, including State attorneys general who act as chief elected or appointed prosecuting attorneys in a district, county (as so defined), municipality or comparable jurisdiction, who may be referred to by a variety of titles such as district attorneys, prosecuting attorneys, commonwealth's attorneys, solicitors, county attorneys, and state's attorneys, and who are responsible for the prosecution of State crimes and violations of jurisdiction-specific local ordinances.

(2) Check. The term "check" has the same meaning as in section 3(6) of the Check Clearing for the 21st Century Act [*12 USCS § 5002(6)*].

(3) Bad check violation. The term "bad check violation" means a violation of the applicable State criminal law relating to the writing of dishonored checks.

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CHAPTER 7

CREDIT REPAIR

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CHAPTER 7

CREDIT REPAIR

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B. The Credit Repair Organizations Act (CROA), 15 U.S.C. §§ 1679 – 1679j (2000).

C. Telemarketing Sales Rule, 16 C.F.R. § 310.

D. NATIONAL CONSUMER LAW CENTER, FAIR CREDIT REPORTING (5^{th} ed. 2002 and Supp. 2005).

II. INTRODUCTION.

Credit has taken on increasing importance in the daily lives of U.S. citizens. As a result, credit reporting is also increasingly important. Many consumers worry about problems in their credit history that may affect their access to credit in the future. This worry leaves them open to businesses that prey on these insecurities and offer credit repair services. Congress, concerned about unscrupulous businesses in this field passed the Credit Repair Organizations Act in 1996.

III. PURPOSE OF CREDIT REPAIR ORGANIZATION ACT (15 U.S.C. § 1679).

A. Congress found that:

1. **"**Consumers have a vital interest in establishing and maintaining their credit worthiness and credit standing in order to obtain and use credit. As a result, consumers who have experienced credit problems may seek assistance from credit repair organizations which offer to improve the credit standing of such consumers."

2. "Certain advertising and business practices of some companies engaged in the business of credit repair services have worked a financial hardship upon consumers, particularly those of limited economic means and who are inexperienced in credit matters."

B. Purpose of the Act.

1. To ensure that prospective buyers of the services of credit repair organizations are provided with the information necessary to make an informed decision regarding the purchase of such services; and

2. To protect the public from unfair or deceptive advertising and business practices by credit repair organizations.

IV. SCOPE – WHO IS A "CREDIT REPAIR ORGANIZATION?" (15 U.S.C. § 1679a)

A. The term "credit repair organization"--

1. Means any person who uses any instrumentality of interstate commerce or the mails to sell, provide, or perform (or represent that such person can or will sell, provide, or perform) any service, in return for the payment of money or other valuable consideration, for the express or implied purpose of--

a) improving any consumer's credit record, credit history, or credit rating; or

b) providing advice or assistance to any consumer with regard to any activity or service described above.

2. The term does not does not include the following:

a) Any nonprofit organization which is exempt from taxation under 26 U.S.C. § 501(c)(3);

b) Any creditor (as defined in section 103 of the Truth in Lending Act) with respect to any consumer, to the extent the creditor is assisting the consumer to restructure any debt owed by the consumer to the creditor; or

c) Any depository institution (as that term is defined in section 3 of the Federal Deposit Insurance Act [12 USCS § 1813]) or any Federal or State credit union (as those terms are defined in section 101 of the Federal Credit Union Act [12 USCS § 1752]), or any affiliate or subsidiary of such a depository institution or credit union.

3. Automobile dealers have been found to be credit repair organizations when targeting individuals with bad credit and promising to find financing or offering to help them reestablish credit or improve their credit records even if no separate fee is charged for credit repair. *See Hall v. Jack Walker Pontiac, Toyota, Inc.*, CCH 52,143, Ohio C.P. Mar. 15, 1999. *But see Sannes v. Jeff Wyler Chevrolet Inc*., 1999 U.S. Dist. LEXIS 21748 (S.D. Ohio Mar. 31, 1999) (credit repair services advertised by dealer were considered ancillary to main business so act did not apply.)

4. Simply advertising or claiming to provide credit repair services is sufficient for coverage. *See Parker v. 1-800 Bar None*, 2002 WL 215530 (N.D. Ill. Feb. 12, 2002) (Company that provided no credit repair services itself but just referred the consumer to another organization, is covered).

V. REQUIREMENTS OF THE ACT.

A. Specific Disclosures (15 U.S.C. § 1679c).

1. Mandatory Disclosure Statement. Any credit repair organization shall provide any consumer with the written disclosures at Appendix A to this Chapter before any contract or agreement between the consumer and the credit repair organization is executed: Consumer must sign to acknowledge receipt.

2. The credit repair company must provide the required written statement as a separate document from any written contract or other agreement between the credit repair organization and the consumer or any other written material provided to the consumer.

3. Retention of compliance records.

a) The credit repair organization must maintain a copy of the statement signed by the consumer acknowledging receipt of the statement.

b) The copy of any consumer's statement shall be maintained in the organization's files for 2 years after the date on which the statement is signed by the consumer.

B. Protections in the Act.

1. Required Terms of Credit Repair Contract (15 U.S.C. § 1679d).

a) Written contracts required. No services may be provided by any credit repair organization for any consumer unless there is a written and dated contract (for the purchase of such services) which meets the requirements below.

b) The contract must contain the following terms and conditions.

(1) The terms and conditions of payment, including the total amount of all payments to be made by the consumer to the credit repair organization or to any other person;

(2) A full and detailed description of the services to be performed by the credit repair organization for the consumer, including--

(a) all guarantees of performance; and

(b) an estimate of the date by which the performance of the services (to be performed by the credit repair organization or any other person) will be complete; or the length of the period necessary to perform such services;

(3) The credit repair organization's name and principal business address; and

(4) A conspicuous statement in bold face type, in immediate proximity to the space reserved for the consumer's signature on the contract, which reads as follows: "You may cancel this contract without penalty or obligation at any time before midnight of the 3rd business day after the date on which you signed the contract. See the attached notice of cancellation form for an explanation of this right."

c) Three Day Waiting Period. Once the written contract is signed, the services cannot be performed before the end of the 3-business-day period beginning on the date the contract is signed.

2. Right to cancel contract (15 U.S.C. § 1679e).

a) Any consumer may cancel any contract with any credit repair organization –

(1) Without penalty or obligation

(2) By notifying the credit repair organization of the consumer's intention to do so at any time before midnight of the 3rd business day after the date the contract is signed.

b) The consumer may cancel by providing oral or written notice, although written notice by certified or registered mail is encouraged.

c) Cancellation form. Each contract shall be accompanied by a form, in duplicate, titled "Notice of Cancellation." The form must contain the following statement in bold face type.

"You may cancel this contract, without any penalty or obligation, at any time before midnight of the 3rd day which begins after the date the contract is signed by you.

"To cancel this contract, mail or deliver a signed, dated copy of this cancellation notice, or any other written notice to [name of credit repair organization] at [address of credit repair organization] before midnight on [date]

"I hereby cancel this transaction,

[date]
[purchaser's signature].

d) At the time the contract or other documents are signed, the credit repair organization must provide the consumer a copy of the completed contract, the disclosure statement required under section 1679c, and a copy of any other document the credit repair organization requires the consumer to sign.

C. Prohibited Practices (15 U.S.C. § 1679b).

1. Untrue and misleading statements.

a) No person may make any statement, or counsel or advise any consumer to make any statement, which is untrue or misleading

b) **OR** which, upon the exercise of reasonable care, should be known by the credit repair organization, officer, employee, agent, or other person to be untrue or misleading

c) **WITH RESPECT TO** any consumer's credit worthiness, credit standing, or credit capacity to--

(1) any consumer reporting agency; or

(2) any person--

(a) who has extended credit to the consumer; or

(b) to whom the consumer has applied or is applying for an extension of credit;

2. Hiding the Consumer's Accurate Credit History.

a) No person may make any statement, or counsel or advise any consumer to make any statement, the intended effect of which is to alter the consumer's identification to prevent the display of the consumer's credit record, history, or rating for the purpose of concealing adverse information that is accurate and not obsolete. Credit repair services have told clients to use Employee identification numbers instead of their social security numbers to repair their credit.

b) The information may not be hidden from:

(1) any consumer reporting agency;

(2) any person--

(a) who has extended credit to the consumer; or

(b) to whom the consumer has applied or is applying for an extension of credit;

3. Other Misconduct in the Provision of Credit Repair Services.

a) No person may make or use any untrue or misleading representation of the services of the credit repair organization; **OR**

b) No person may engage, directly or indirectly, in any act, practice, or course of business that constitutes or results in the commission of, or an attempt to commit, a fraud or deception on any person in connection with the offer or sale of the services of the credit repair organization.

c) No payment in advance! No credit repair organization may charge or receive any money or other valuable consideration for the performance of any service which the credit repair organization has agreed to perform for any consumer before such service is fully performed.

d) If the credit repair services are provided by a telemarketer, then no payment may be requested or received until after the seller has provided the consumer with a consumer credit report demonstrating that the promised results have been achieved, such report having been issued more than six months after the results were achieved. Telemarketing Sales Rule, 16 C.F.R. § 310.4(a)(2).

e) Effect of Noncompliance (15 U.S.C. § 1679F)

D. Waiver of Protections.

1. Consumer waivers are invalid. Any waiver by any consumer of any protection provided by or any right of the consumer under this subchapter--

a) shall be treated as void; and

b) may not be enforced by any Federal or State court or any other person.

2. Attempts to obtain waivers. Any attempt by any person to obtain a waiver from any consumer of any protection provided by the Act is treated as a violation of the Act.

E. Contracts not in compliance. Any contract for services which does not comply with the Act--

1. Shall be treated as void; and

2. May not be enforced by any Federal or State court or any other person.

VI. REMEDIES.

A. Civil liability (§ 1679g). Any person who fails to comply with any provision of this Act with respect to any other person shall be liable to such person in an amount equal to the sum of the amounts determined under each of the following paragraphs:

1. Actual damages. The greater of--

a) the amount of any actual damage sustained by such person as a result of such failure; or

b) any amount paid by the person to the credit repair organization.

2. Punitive damages.

a) Individual actions. Any additional amount the court may allow.

b) Class actions. The sum of--

(1) the aggregate of the amount which the court may allow for each named plaintiff; and

(2) the aggregate of the amount which the court may allow for each other class member, without regard to any minimum individual recovery.

c) Factors to be considered in awarding punitive damages.

(1) The frequency and persistence of noncompliance by the credit repair organization.

(2) The nature of the noncompliance.

(3) The extent to which such noncompliance was intentional.

(4) In the case of any class action, the number of consumers adversely affected.

3. Attorneys' fees. In any successful action to enforce any liability, the person may recover the costs of the action, together with reasonable attorneys' fees.

B. Administrative enforcement (15 U.S.C. § 1679h).

1. Federal Trade Commission.

a) Enforced under the Federal Trade Commission Act [15 U.S.C. § 41 et seq.] by the Federal Trade Commission.

b) Violation of any requirement or prohibition imposed under the Act with respect to credit repair organizations shall constitute an unfair or deceptive act or practice in commerce.

c) All functions and powers of the Federal Trade Commission shall be available to the Commission to enforce compliance with the Act without regard to whether the credit repair organization is engaged in commerce, or meets any other jurisdictional tests in the Federal Trade Commission Act.

2. State action for violations.

a) In addition to such other remedies as are provided under State law, whenever the chief law enforcement officer of a State, or an official or agency designated by a State, has reason to believe that any person has violated or is violating the Act, the State--

(1) may bring an action to enjoin such violation;

(2) may bring an action on behalf of its residents to recover damages for which the person is liable to such residents; and

(3) in the case of any successful action shall be awarded the costs of the action and reasonable attorney fees as determined by the court.

b) The State shall serve prior written notice of any civil action upon the Federal Trade Commission and provide the Commission with a copy of its complaint, except in any case where such prior notice is not feasible, in which case the State shall serve such notice immediately upon instituting such action.

c) The Commission shall have the right--

(1) to intervene in any action referred to in subparagraph (A);

(2) upon so intervening, to be heard on all matters arising in the action; and

(3) to file petitions for appeal.

d) Whenever the Federal Trade Commission has instituted a civil action for violation of this subchapter, no State may, during the pendency of such action, bring an action under this section against any defendant named in the complaint of the Commission for any violation of this subchapter that is alleged in that complaint.

C. Statute of limitations. (15 U.S.C. § 1679i)

1. 5 years beginning on:

a) the date of the occurrence of the violation involved; or

b) the date of the discovery by the consumer of the misrepresentation in any case in which any credit repair organization has materially and willfully misrepresented any information which--

(1) the credit repair organization is required, by any provision of the Act, to disclose to any consumer; and

(2) is material to the establishment of the credit repair organization's liability to the consumer under this subchapter.

D. Relationship to other protections.

1. FTC Telemarketing Sales Rule. There is no private cause of action unless damages exceed $50,000, but a violation of the rule may be a *per se* violation of State UDAP statutes.

2. State UDAP Statutes. These statutes typically provide a private cause of action against the merchant (credit repair organization) authorizing the court to award actual damages, statutory damages, costs, and attorney's fees.

APPENDIX A TO CHAPTER 7
MANDATORY DISCLOSURE LANGUAGE
15 U.S.C. § 1679c

Consumer Credit File Rights Under State and Federal Law

You have a right to dispute inaccurate information in your credit report by contacting the credit bureau directly. However, neither you nor any 'credit repair' company or credit repair organization has the right to have accurate, current, and verifiable information removed from your credit report. The credit bureau must remove accurate, negative information from your report only if it is over 7 years old. Bankruptcy information can be reported for 10 years.

You have a right to obtain a copy of your credit report from a credit bureau. You may be charged a reasonable fee. There is no fee, however, if you have been turned down for credit, employment, insurance, or a rental dwelling because of information in your credit report within the preceding 60 days. The credit bureau must provide someone to help you interpret the information in your credit file. You are entitled to receive a free copy of your credit report if you are unemployed and intend to apply for employment in the next 60 days, if you are a recipient of public welfare assistance, or if you have reason to believe that there is inaccurate information in your credit report due to fraud.

You have a right to sue a credit repair organization that violates the Credit Repair Organization Act. This law prohibits deceptive practices by credit repair organizations.

You have the right to cancel your contract with any credit repair organization for any reason within 3 business days from the date you signed it.

Credit bureaus are required to follow reasonable procedures to ensure that the information they report is accurate. However, mistakes may occur.

You may, on your own, notify a credit bureau in writing that you dispute the accuracy of information in your credit file. The credit bureau must then reinvestigate and modify or remove inaccurate or incomplete information. The credit bureau may not charge any fee for this service. Any pertinent information and copies of all documents you have concerning an error should be given to the credit bureau.

If the credit bureau's reinvestigation does not resolve the dispute to your satisfaction, you may send a brief statement to the credit bureau, to be kept in your file, explaining why you think the record is inaccurate. The credit bureau must include a summary of your statement about disputed information with any report it issues about you.

The Federal Trade Commission regulates credit bureaus and credit repair organizations. For more information contact:

The Public Reference Branch, Federal Trade Commission
Washington, D.C. 20580.

CHAPTER 8

CREDIT DISCRIMINATION

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CHAPTER 8

CREDIT DISCRIMINATION

I. REFERENCES.

A. Equal Credit Opportunity Act, 15 U.S.C. §§ 1691 – 1691f (2000).

B. Federal Reserve Board Regulation B (Equal Credit Opportunity), 12 C.F.R. pt. 202.

C. NATIONAL CONSUMER LAW CENTER, CREDIT DISCRIMINATION (4th ed. 2005 and Supp. 2006) [hereinafter "NCLC Discrimination"].

II. INTRODUCTION.

A. The approach to discrimination can take a number of tacks using a variety of civil rights statutes at the state and federal level. This outline deals only with the Equal Credit Opportunity Act (ECOA) – a critical consumer protection statute regulating access to credit. Unfortunately, credit discrimination is a widespread problem throughout America. Credit discrimination is usually based on race, national origin, sex, marital status, familial status, sexual orientation, disability, age, religion, or receipt of public assistance. A direct consequence of credit discrimination is lost opportunity, such as for home owner ship or college education. Situations in which the ECOA may be useful include:

1. Creditors excluding, or "redlining," the inhabitants of certain neighborhoods because of poor payment experience.

2. Banks discouraging minority applications by not having branches in minority communities.

3. Car dealers or brokers steering minorities to different creditors or charging them higher prices and fees.

4. Reverse "redlining" by charging higher interest rates in certain minority neighborhoods.

5. Merchants using differing standards when cash up front is required.

6. Merchants using differing standards when collateral, cosigners or down payments are required.

B. The purpose of the ECOA is "to require that financial institutions and otherfirms engaged in the extension of credit make that credit equally available to all creditworthy customers without regard to sex or marital status."

C. Congress has directed that the Federal Reserve Board promulgate rules and regulations for the implementation and enforcement of the ECOA. The Federal Reserve Board has done so in Regulation B, codified at 12 C.F.R. pt. 202.

III. APPLICABILITY.

A. In general, the ECOA prohibits creditors from discriminating against applicants based on race, color, religion, national origin, sex, marital status, age, public assistance income, and exercise of rights under the Consumer Protection Act regarding any aspect of a credit transaction. 12 C.F.R. § 202.4. Whether or not the ECOA applies to a transaction may be determined by answering the threshold questions below.

B. Has there been an extension of "credit" covered by the ECOA?

1. 15 U.S.C. § 1691a(d). The term "credit" means "the right granted by a creditor to a debtor to defer payment of debt or to incur debts and defer its payment or to purchase property or services and defer payment thereof."

2. The ECOA definition is intentionally broader than the definition under the Truth in Lending Act (TILA) because TILA requires a finance charge or at least 5 installment payments. See 15 U.S.C. § 1602; Official Staff Commentary to 12 C.F.R. § 202.1(a)-1. The ECOA applies whenever a payment is deferred.

3. Specific types of transactions. See NCLC DISCRIMINATION § 2.2.2. Does the ECOA apply to:

a) Leases?

(1) Residential – Probably not, but the Fair Housing Act might apply.

(2) Personal property leases covered by the Consumer Leasing Act – Probably Yes. *See Brothers v. First Leasing*, 724 F.2d 789 (9th Cir. 1984).

(3) Rent-To-Own & Terminable Leases – No, if they are terminable at will without penalty. If you can argue it is really a disguised credit sale then the ECOA applies.

b) Utility Service? Yes. Official Staff Commentary § 202.3(a)-2.

c) Check Cashing or ATM Cards? – No, because there is no extension of credit.

C. Is the client an "Applicant" under the ECOA?

1. 15 U.S.C. § 1691a(b). "Applicant" means "any person who applies to a creditor directly for an extension, renewal, or continuation of credit, or applies to a creditor indirectly by use of an existing credit plan for an amount exceeding a previously established credit limit."

2. 12 C.F.R. § 202.2(e). Applicant means "any person who requests or who has received an extension of credit from a creditor, and includes any person who is or may become contractually liable regarding an extension of credit."

3. To be an applicant, a person does NOT have to submit an application. Be aware, however, that certain protections under the ECOA only apply to someone who has submitted an application.

D. Is the party who allegedly violated the Act a "creditor?"

1. 15 U.S.C. 1691a(e). The term "creditor" means:

a) any person who "regularly" extends, renews, or continues credit;

b) any person who regularly arranges for the extension, renewal, or continuation of credit;

c) or any assignee of an original creditor who *participates* in the decision to extend, renew, or continue credit.

d) "Regularly" is NOT defined under the ECOA or the CFR provisions based upon it. NCLC suggests looking to the old Regulation Z (Truth in Lending Act) that existed at the time the ECOA was originally passed. Cases interpreting this provision said that "regularly" means more than "isolated" or "incidental" occurrences. *See* NCLC DISCRIMINATION § 2.2.5.2.

2. Exclusions from the definition of creditor.

a) The term does not include a person whose only participation in a credit transaction involves honoring a credit card. 12 C.F.R. § 202.2(l).

b) A person is not a creditor regarding any violation of the act or Regulation B committed by another creditor unless the person knew or had reasonable notice of the act, policy, or practice that constituted the violation before becoming involved in the credit transaction. *Id.*

3. The Government as a creditor. The ECOA applies to the government, except that governmental creditors are not subject to punitive damages. *See* 15 U.S.C. § 1691e(b).

E. Exempt transaction. Some transactions are partially exempted by the Federl Reserve Board. However, the rule against discrimination against applicants on a prohibited basis still applies. *See* NCLC DISCRIMINATION § 2.2.6; 12 C.F.R. § 202.3(a).

1. Public utilities credit.

a) Public utilities credit refers to extensions of credit that involve public utility services provided through pipe, wire, or other connected facilities, or radio or similar transmission, if the charges for service, delayed payment, and any discount for prompt payment are filed with or regulated by a government unit. Utilities are not exempt if the extension of credit is for something other than the utility.

b) Rural electric cooperatives and other unregulated utilities are NOT included in this exception.

c) The credit must relate to the delivery of utility services as well. If the credit relates to another transaction (such as for equipment), the exemption would not apply.

d) Public utilities must comply with the majority of ECOA provisions. There are, however, the following exceptions:

(1) Public utilities may ask the marital status of applicants.

(2) Public utilities may report credit reporting information in the names of both spouses.

(3) Public utilities are not required to maintain copies of credit applications.

2. Incidental consumer credit.

a) Incidental credit refers to extensions of credit.

(1) Primarily for personal, family, and household use;

(2) That are NOT Public Utilities or Securities Credit;

(3) That are not made pursuant to the terms of a credit card account;

(4) That are not subject to a finance charge or interest; and

(5) That are not payable by agreement in more than four installments.

b) Exceptions. The following provisions of Regulation B do not apply to incidental credit transactions:

(1) Section 202.5(c) concerning information about a spouse or former spouse;

(2) Section 202.5(d)(1) concerning information about marital status;

(3) Section 202.5(d)(2) concerning information about income derived from alimony, child support, or separate maintenance payments;

(4) Section 202.5(d)(3) concerning information about the sex of an applicant, but only to the extent necessary for medical records or similar purposes;

(5) Section 202.7(d) relating to the signature of a spouse or other person;

(6) Section 202.9 relating to notifications;

(7) Section 202.10 relating to furnishing of credit information; and

(8) Section 202.12(b) relating to record retention.

3. Securities credit.

a) Securities credit refers to extensions of credit subject to regulation under section 7 of the Securities Exchange Act of 1934 (15 U.S.C. §§ 78a – 78eee) or extensions of credit by a broker or dealer subject to regulation as a broker or dealer under the Securities Exchange Act of 1934. 15 U.S.C. § 78c contains definitions and applicability information for this Act.

b) Exceptions. The following provisions of Regulation B do not apply to securities credit:

(1) Section 202.5(c) concerning information about a spouse or former spouse;

(2) Section 202.5(d)(1) concerning information about marital status;

(3) Section 202.5(d)(3) concerning information about the sex of an applicant;

(4) Section 202.7(b) relating to designation of name, but only to the extent necessary to prevent violation of rules regarding an account in which a broker or dealer has an

interest, or rules necessitating the aggregation of accounts of spouses for the purpose of determining controlling interests, beneficial interests, beneficial ownership, or purchase limitations and restrictions;

(5) Section 202.7(c) relating to action concerning open-end accounts, but only to the extent the action taken is on the basis of a change of name or marital status;

(6) Section 202.7(d) relating to the signature of a spouse or other person;

(7) Section 202.10 relating to furnishing of credit information; and

(8) Section 202.12(b) relating to record retention.

4. Credit extended to the Government.

a) Government credit refers to extensions of credit made to governments or governmental subdivisions, agencies, or instrumentalities.

b) Except for section 202.4, the general rule prohibiting discrimination on a prohibited basis, the requirements of this regulation **DO NOT** apply to government credit.

IV. PROHIBITED ACTIVITIES (15 U.S.C. § 1691).

A. Discrimination by a creditor is unlawful when the creditor's actions in relation to an applicant are made because of a prohibited basis, or when the creditor's decision-making process results in individuals being treated differently because of a prohibited basis (disparate treatment). For example:

1. Requiring a minority applicant to produce more documentation than a white applicant.

2. Relaxing the credit standards for a non-minority applicant.

B. Activities constituting discrimination. It is unlawful for any creditor to discriminate against any applicant, with respect to any aspect of a credit transaction—

1. on the basis of race, color, religion, national origin, sex or marital status, or age (provided the applicant has the capacity to contract);

2. because all or part of the applicant's income derives from any public assistance program; or

3. because the applicant has in good faith exercised any right under the Consumer Credit Protection Act.

C. Activities not constituting discrimination. It shall not constitute discrimination for purposes of this subchapter for a creditor—

1. to make an inquiry of marital status if such inquiry is for the purpose of ascertaining the creditor's rights and remedies applicable to the particular extension of credit and not to discriminate in a determination of creditworthiness;

2. to make an inquiry of the applicant's age or of whether the applicant's income derives from any public assistance program if such inquiry is for the purpose of determining the amount and probable continuance of income levels, credit history, or other pertinent element of credit-worthiness as provided in regulations of the Board;

3. to use any empirically derived credit system which considers age if such system is demonstrably and statistically sound in accordance with regulations of the Board, except that in the operation of such system the age of an elderly applicant may not be assigned a negative factor or value; or

4. to make an inquiry or to consider the age of an elderly applicant when the age of such applicant is to be used by the creditor in the extension of credit in favor of such applicant.

D. Refusals of Credit that are **NOT** considered discriminatory. It is not a violation of the ECOA for a creditor to refuse to extend credit offered pursuant to—

1. any credit assistance program expressly authorized by law for an economically disadvantaged class of persons;

2. any credit assistance program administered by a nonprofit organization for its members or an economically disadvantaged class of persons; or

3. any special purpose credit program offered by a profit-making organization to meet special social needs which meets standards prescribed in regulations by the Board;

4. if such refusal is required by or made pursuant to such program.

E. Non-discriminatory Activities Specifically described in the ECOA (15 U.S.C. § 1691d).

1. Requests for the signature of both parties to a marriage for the purpose of creating a valid lien, passing clear title, waiving inchoate rights to property, or assigning earnings, shall not constitute discrimination. NOTE: This does NOT permit a creditor to take sex or marital status into account in connection with the evaluation of creditworthiness of any applicant.

2. Consideration or application of state property laws directly or indirectly affecting creditworthiness shall not constitute discrimination for purposes of this subchapter.

F. Credit to husband and wife.

1. State laws prohibiting separate extension of consumer credit to husband and wife are specifically preempted by the ECOA. (15 U.S.C. § 1691d)

2. Creditors may NOT combine credit accounts of a husband and wife with the same creditor to determine permissible finance charges or loan ceilings under federal or state laws where each party to a marriage separately and voluntarily applies for and obtains separate credit accounts. (15 U.S.C. § 1691d)

V. NOTIFICATION PROVISIONS.

A. Notification requirements.

1. Creditors must notify applicants of the action taken within 30 days of receiving a completed application, within 30 days of taking adverse action on an incomplete application, within 30 days of taking adverse action on an existing account, or within 90 days after notifying the applicant of a counteroffer if the applicant does not expressly accept or use the credit offer .

2. The required notification of action must contain:

   a) A statement of the action taken;

   b) The creditor's name and address;

   c) Written notification of adverse action which includes:

      (1) The specific reasons for the action taken; or

      (2) The applicant's right to receive a statement of specific reasons within thirty, provided the request is made within sixty days after notification of the adverse action

      (3) The identity and contact information of the person or office from which such statement may be obtained.

      (4) Such statement may be given orally if the written notification advises the applicant of his right to have the statement of reasons confirmed in writing on written request.

B. Definition.

1. "Adverse Action" means a denial or revocation of credit, a change in the terms of an existing credit arrangement, or a refusal to grant credit in substantially the amount or on substantially the terms requested.

2. The term does **NOT** include a refusal to extend additional credit under an existing credit arrangement where the applicant is delinquent or otherwise in default, or where such additional credit would exceed a previously established credit limit.

VI. INCENTIVES FOR SELF-TESTING AND SELF-CORRECTION (15 U.S.C.. § 1691c-1; 12 C.F.R. § 202.15)

A. Creditors may conduct “self-tests” to determine their compliance with the ECOA. A self-test is any program, practice, or study that:

1. Is designed and used specifically to determine the extent or effectiveness of a creditor's compliance with the act or this regulation; and

2. Creates data or factual information that is not available and cannot be derived from loan or application files or other records related to credit transactions.

B. IF a creditor—

1. conducts, or authorizes an independent third party to conduct, a self-test of any aspect of a credit transaction by a creditor, in order to determine the level or effectiveness of compliance with this subchapter by the creditor; and

2. has identified any possible violation of the ECOA by the creditor and has taken, or is taking, appropriate corrective action to address any such possible violation.

C. THEN, any report or results of that self-test is privileged; and may not be obtained or used by any applicant, department, or agency in any proceeding or civil action in which one or more violations of the ECOA are alleged; or examination or investigation relating to compliance with the ECOA.

D. Self-test results MAY be used in any proceeding IF:

1. The creditor or any person with lawful access to the report or results voluntarily releases or discloses all, or any part of, the report or results to the applicant, department, or agency, or to the general public, or b) refers to or describes the report or results as a defense to charges of violations of the ECOA against the creditor to whom the self-test relates; or

2. The report or results are sought in conjunction with an adjudication or admission of a violation of the ECOA for the sole purpose of determining an appropriate penalty or remedy.

VII. ENFORCEMENT.

A. Administrative enforcement. (15 U.S.C. § 1691c)

1. Enforcing agencies. The ECOA is enforced by the agency with specific regulatory authority over the creditor. Depending upon the creditor involved, enforcement authority may be found in any of the following sources:

a) Section 8 of the Federal Deposit Insurance Act [12 U.S.C. § 1818], in the case of--

(1) National banks, and Federal branches and Federal agencies of foreign banks, by the Office of the Comptroller of the Currency;

(2) Member banks of the Federal Reserve System (other than national banks), branches and agencies of foreign banks (other than Federal branches, Federal agencies, and insured State branches of foreign banks), commercial lending companies owned or controlled by foreign banks; and

(3) Banks insured by the Federal Deposit Insurance Corporation (other than members of the Federal Reserve System) and insured State branches of foreign banks, by the Board of Directors of the Federal Deposit Insurance Corporation;

b) Section 8 of the Federal Deposit Insurance Act [12 U.S.C. § 1818], by the Director of the Office of Thrift Supervision, in the case of a savings association the deposits of which are insured by the Federal Deposit Insurance Corporation.

c) The Federal Credit Union Act [12 U.S.C.A. § 1751 et seq.], by the Administrator of the National Credit Union Administration with respect to any Federal Credit Union.

d) Several other agencies including the Secretaries of Transaportation and Agriculture, the Securities and Exchange Commission, and the Small Business Administration.

2. Violations of the ECOA that also violate other statutory requirements. Agencies may enforce both the ECOA provision as well as the other statutory provision.

3. Overall enforcement authority of Federal Trade Commission.

a) Except where enforcement is specifically given to another agency above, the Federal Trade Commission enforces the ECOA.

b) A violation of any requirement imposed under the ECOA is also a violation of the Federal Trade Commission Act.

B. Civil liability (15 U.S.C.A. § 1691e).

1. Individual or class action.

a) Creditor liable for actual damages.

b) Punitive damages.

(1) Any creditor, other than a government or governmental subdivision or agency, is liable to the aggrieved applicant for punitive damages in an amount not greater than $10,000.

(2) In the case of a class action, the total recovery under this subsection shall not exceed the lesser of $500,000 or 1 per centum of the net worth of the creditor.

(3) In determining the amount of punitive damages in any action, the court shall consider, among other relevant factors:

(a) the amount of any actual damages awarded,

(b) the frequency and persistence of failures of compliance by the creditor,

(c) the resources of the creditor, the number of persons adversely affected, and

(d) the extent to which the creditor's failure of compliance was intentional.

c) U.S. District Courts may give equitable and declaratory relief as is necessary to enforce the requirements imposed by the ECOA.

d) If successful, the plaintiff may recover both the costs of the action, and reasonable attorney's fee as determined by the court.

2. Jurisdiction and Statute of Limitations.

   a) ECOA actions may be brought in the appropriate United States district court without regard to the amount in controversy, or in any other court of competent jurisdiction.

   b) Statute of Limitations as a general rule is two years from the date of the violation, except that--

      (1) whenever any agency having responsibility for administrative enforcement commences an enforcement proceeding within two years from the date of the occurrence of the violation, or

      (2) whenever the Attorney General commences a civil action under this section within two years from the date of the occurrence of the violation,

      (3) then any applicant who has been a victim of the discrimination which is the subject of the agency's proceeding or civil action may bring an action not later than one year after the commencement of the Agency's proceeding or action.

3. Discovery. Nothing in the ECOA shall be construed to prohibit the discovery of a creditor's credit granting standards under appropriate discovery procedures.

VIII. CONCLUSION.

CHAPTER 9

MILITARY UNIQUE CONSUMER LAW ISSUES

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CHAPTER 9

MILITARY UNIQUE CONSUMER LAW ISSUES

I. INVOLUNTARY ALLOTMENTS FOR CREDITOR JUDGMENTS.

A. Background to DoD Dir. 1344.9; DoD Instr. 1344.12.

1. Congress required DoD to promulgate these regulations in the Hatch Act.

2. The Act waives sovereign immunity for the collection of creditor judgments from federal employees.

3. The Act directed DOD to promulgate regulations providing for involuntary allotment of military pay to account for "the procedural requirements of the Soldiers and Sailors Civil Relief Act...and in consideration for the absence of a member of the uniformed services from an appearance in a judicial proceeding resulting from the exigencies of military duty."

B. Military Procedure For Involuntary Allotments.

1. Initiation Procedure for Creditors.

a) Final order of court with specific money award, and DD Form 2653. Either no appeal or the time for an appeal has expired.

b) Served on designated agent - DFAS - Cleveland.

c) Certifications [DD Form 2653]:

(1) Judgment not modified, set aside or satisfied. If partially satisfied, the amount unpaid.

(2) Not issued while service member was on active duty. If the service member was on active duty, then either the service member was present or represented by an attorney or the SSCRA was followed fully.

(3) State law allows garnishment of a similarly situated civilian.

(4) Debt has not been discharged in bankruptcy or barred by other legal impediment.

(5) Creditor agrees to repay service member within 30 days if payment to creditor is erroneous.

2. Amounts Available.

a) Pay includes - Disposable (generally taxable) pay (only).

b) Maximum amount of allotment - 25% of disposable pay or lower if state law provides for lower amount. The states of PA and TX do not allow garnishment of wages for commercial debts, thereby precluding involuntary allotment actions from debt actions in those states. The states of NH, NC, FL, SC exempt such a high percentage of earnings that the practical effect precludes involuntary allotment actions for commercial debts.

3. DFAS action.

a) Facial review.

b) Mail notice [DA Form 2653] to service member [90 day clock starts].- No time limit for DFAS to issue notice. Mail two additional copies to the "immediate commander" with DD Form 2654.

4. Command action ("Immediate Commander").

a) Serve service member with copy of notice and DD Form 2654 (Rights Warning Form) [5 day req].

b) Inform service member of right to contest the involuntary allotment [15 days to respond].

c) Grant 30 day extension to respond if necessary.

5. Service member's actions.

a) Consent.

b) Seek legal assistance.

6. Service member defenses per 32 CFR Part 113, § 113.6(b)(2)(iii)(d):

a) SSCRA [now SCRA] was not followed in the underlying judgment.

b) Military exigency caused the absence of the service member from appearance in the judicial proceeding, which forms the basis of the judgment.

c) Application for allotment is false or erroneous in material part.

d) Judgment has been satisfied, set-aside, or modified.

e) Legal impediment (e.g. bankruptcy) prevents processing the allotment.

f) "Other appropriate reasons..." Violation of consumer law-underlying the judgment.

7. Immediate Commander Response.

a) Rule on military exigency defense only.

(1) Standard of review - preponderance.

(2) Definition - "[M]ilitary assignment or mission essential duty that, because of its urgency, importance, duration, location or isolation, necessitates the absence of a member of the military service from appearance at a judicial proceeding. Absence from an appearance in a judicial proceeding is normally to be presumed to be caused by exigencies of military duty during periods of war, national emergency, or when the member is deployed."

b) Forward the debtor response to DFAS. Debtor failure to timely respond results in automatic initiation of involuntary allotment.

8. DFAS decides all other defenses.

9. No appeal of DFAS determinations.

II. PUTTING AREAS OFF-LIMITS – ARMED FORCES DISCIPLINARY CONTROL BOARDS.

A. References.

1. AR 190-24, Armed Forces Disciplinary Control Boards and Off-installation Liaison and Operations (27 July 2006).

2. AR 600-20, Army Command Policy (7 June 2006).

B. Off-Limits Establishments and Areas.

1. Purposes.

a) Maintain good discipline, health, morals, safety, and welfare of service members.

b) Prevent service members from being exposed to or victimized by crime-conducive conditions.

2. Effect of Off-limits Designation.

a) Service members are prohibited from entering establishments or areas declared off-limits according to AR 190-24.

b) Violations subject the service member to discipline under appropriate regulations or the UCMJ.

c) Family members should be made aware of the off-limits areas.

C. Procedure – The Armed Forces Disciplinary Control Board

1. The Role of Commanders

a) Establishment of off-limits areas is a function of command.

b) Commanders retain substantial discretion to declare establishments or areas temporarily off-limits for their commands. These areas are given first priority for review at the AFDCB.

c) Prior to initiating AFDCB action, installation commanders will attempt to correct adverse conditions or situations through the assistance of civic leaders or officials.

2. The Armed Forces Disciplinary Control Board (AFDCB).

a) Composition.

(1) Established at the installation base or station level.

(2) Structured according to the needs of the command, but consider reps from the following functional areas:

(a) Law Enforcement

(b) Legal Counsel

(c) Medical, Health, and Environmental Protections

(d) Public Affairs

(e) Equal Opportunity

(f) Fire and Safety

(g) Chaplain

(h) Alcohol and Drug Abuse

(i) Personnel an Community Activities

(j) Consumer Affairs

(3) Commanders designate a board president and voting members in the written agreement establishing the

board. At most installations, the president is the Provost Marshal.

b) Function

(1) Advise and make recommendations to commanders concerning eliminating conditions which adversely affect the health, safety, morals, welfare, morale, and discipline of the Armed Forces.

(2) The Board is required to meet at least quarterly.

(3) The Board makes recommendations as to the following conditions:

(a) Disorders and Lack of Discipline

(b) Prostitution

(c) Sexually Transmitted Disease

(d) Liquor Violations

(e) Racial and other discriminatory practices

(f) Alcohol and Drug Abuse

(g) Criminal or illegal activities involving cults or hate groups

(h) Illicit Gambling

(i) Areas Susceptible to terrorist activities

(j) Unfair commercial or consumer activities

(k) Other undesirable conditions that may adversely affect members of the military or their families.

(4) The Board coordinates with local and civil authorities regarding these conditions.

c) Procedure.

(1) The Board receives and considers reports of the conditions cited above.

(2) The board may investigate or visit an establishment, but if they do so, the President must submit a report of the findings and recommendations from the visit at the next meeting.

(3) DUE PROCESS: When the board concludes that conditions adverse to Armed Forces personnel exist, they must do the following before placing the establishment off-limits:

(a) Notify the individual responsible (owner or manager) for the conditions of the problem. This notification letter must be sent by certified mail.

(b) The proprietor should be afforded an opportunity to appear before the board.

(c) Conduct further investigation to determine whether improvements have been made.

(4) Make a recommendation to the sponsoring commander. The commander will approve or disapprove and notify the president.

(5) The president will notify the proprietor of the outcome.

(6) Commanders will publish a list of off-limits establishments

d) Limitations.

(1) Commanders may not post signs on private property (saying “off-limits.”)

(2) OCONUS procedures must be consistent with the SOFA for that country.

(3) Off-limits should only be imposed where there is substantive information supporting the action. The board must not act arbitrarily.

e) Removal.

(1) The proprietor may petition for removal at any time. Removal action must be taken by the AFDCB.

(2) A change in ownership, management, or name does NOT in and of itself revoke the off-limits order.

(3) Additionally, the Board should inspect off-limits establishments at least quarterly to ensure that continued limitations are justified.

(4) Once the board is convinced that adequate corrective measures have been taken, they should forward a recommendation for removal to the commander.

III. REPOSSESSION

A. References.

1. AR 27-40, *Litigation* (19 Sep 1994).

2. NATO SOFA Supplementary Agreement available at http://www.aeaim.hqusareur.army.mil/library/MIS/F-PUB-MIS.htm.

3. NATIONAL CONSUMER LAW CENTER, REPOSSESSIONS (6^{th} ed. 2005).

4. Uniform Commercial Code, Article 9, *Secured Transactions*.

B. Repossession on the Installation.

1. Seizure of personal property. (AR 27-40, para. 2-3f.) State and federal courts issue orders (for example, writ of attachment) authorizing a levy (seizure) of property to secure satisfaction of a judgment. DA personnel will comply with valid state or federal court orders commanding or authorizing the seizure of private property to the same extent that state or federal process is served.

2. Service of Civil Process.

a) Policy. (AR 27-40, para. 2-3a.)

(1) DA officials will not prevent or evade the service of process in legal actions brought against the United States or against themselves in their official capacities.

(2) If acceptance of service of process would interfere with the performance of military duties, Army officials may designate a representative to accept service.

b) Service on Soldiers in their individual capacity.

(1) DA personnel sued in their individual capacity should seek legal counsel concerning voluntary acceptance of process.

(2) Process of federal courts. Subject to reasonable restrictions imposed by the commander, civil officials will be permitted to serve federal process. (See Federal Rules of Civil Procedure 4, 45). (AR 27-40, para. 2-3c.)

(3) Process of state courts. (AR 27-40, para. 2-3d.)

(a) In areas of exclusive federal jurisdiction that are not subject to the right to serve state process, the commander or supervisor will determine whether the individual to be served wishes to accept service voluntarily. A JA or other DA attorney will inform the individual of the legal effect of voluntary acceptance. If the individual does not desire to accept service, the party requesting service will be notified that the nature of the exclusive Federal jurisdiction precludes service by State authorities on the military installation.

(b) On Federal property where the right to serve process is reserved by or granted to the State, in areas of concurrent jurisdiction, or where the United States has only a proprietary interest,

Army officials asked to facilitate service of process will proceed initially as provided in the preceding subparagraph. If the individual declines to accept service, the requesting party will be allowed to serve the process per applicable State law, subject to reasonable restrictions imposed by the commander.

(4) Process in Germany.[1]

(a) German process servers generally have access to our installations. Art. 32, SA NATO SOFA.

(b) The service is either accomplished through a liaison agency designated by the U.S. or with notice to that agency.

(c) The liaison agency for process is normally within OJA USAREUR.

(d) You will likely have a German civilian who acts as the liaison in your SJA office or Law Center.

(e) Repossession in Germany.

(i) The German Civil Code generally allows self-help repossession. Court orders are only required if there will be resistance or the agent that is doing the repossessing has to enter private property.

(ii) The "bailiff" (similar to a sheriff or deputy) does both service of process and execution of judgments in Germany. Thus, we will grant access to our installations in accordance with the SA to the NATO SOFA. (Through liaison or notice to liaison.)

[1] TJAGLCS would like to thank Mr. P.J. Conderman, International Law Division, OJA, USAREUR for providing invaluable support in the preparation of this section.

(iii) Art. 34, SA NATO SOFA, however, places additional restrictions on execution of judgments. The enforcement must be "effected . . . in the presence of a representative of the force." Thus, an U.S. representative would have to be present during the repossession.

(iv) Note that U.S. creditors seeking to enforce their judgments must obtain a domestic (German) basis for the repossession prior to proceeding. OJA, USAREUR is unaware of any recent cases where U.S. concerns have had to enforce their security interest in this way. Without a valid German order, however, the German authorities may view the action as theft.

3. Practical Advice.

a) Know your state law.

(1) Is self-help allowed or is a court order required?

(2) Most states do not allow a "breach of the peace" during the repossession.

(a) Physical force is a breach of the peace. Examples of breach of peace:

(i) A repossessor grabs keys from debtor and twists wrist.

(ii) A repossessor pushes door open and strikes debtor in the stomach.

(iii) A debtor's car is towed away with her in it and the car is put in fenced lot with loose guard dog.

(b) If the debtor objects at the time of the taking, that may be a "breach of the peace." *See*, *e.g.*, Hester *v. Bandy*, 627 So.2d 833 (Miss. 1993); *State v. Trackwell*, 458 N.W.2d 181 (Neb. 1990); *but see Chrysler Credit Corp. v. Kootnz*, 661 N.E.2d 1171 (Ill. App. 1996) *Giles v. First Va. Credit Services*, 563 S.E.2d 568, 46 U.C.C. Rep. Serv. 2d 913 (N.C. Ct. App. 2002)

(c) If there is a breach of peace, the repossessor must try again another day or get a court order.

(d) The repo man may have a defense to breach of the peace if he gains possession of the collateral prior to the breach. *See Clark v. Auto Recovery Bureau, Inc.*, 889 F.Supp. 543 (D.Conn. 1994).

b) Know Your Installation. Where are the spots of exclusive jurisdiction? Did the state reserve the right to serve process?

c) Have a written policy!

(1) Person reports to MP station or SJA office with court order or documentation (contract, evidence of default, evidence of ownership, authorization from creditor if agent, etc.).

(2) JA Review of court order/documents for validity.

(3) MP escorts the repossession agent to unit area to prevent breaches of the peace.

(4) Beware of conflicts – LAOs should not be reviewing documents – they will have to advise the soldier!

C. Assisting the soldier.

1. Repossession Threatened, But Not Accomplished.

a) Is the security interest valid?

b) Voluntary Surrender?

(1) May save expenses and result in a larger value at the collateral sale (avoiding or minimizing the deficiency judgment).

(2) Know your state law – about half of the states have anti-deficiency statutes that prohibit or limit the seeking of a deficiency. In this case, voluntary surrender is almost never a good idea. For example, in Georgia the creditor must send notice of intention to seek a deficiency judgment within 10 days of the repossession. Failure to comply with the notice provision precludes a deficiency judgment.

(3) Negotiate favorable concessions in return for voluntary repossession. For example, they may waive the right to a deficiency.

c) Resisting the Repossession.

(1) Notify the creditor in writing that:

(a) The client objects to the repossession.

(b) The creditor may not trespass on the consumer's property.

(c) The creditor may not use force, threats, or intimidation.

(d) The debt is disputed and any information provided to a credit reporting agency must reflect the dispute.

(2) Alert family members not to consent to the repossession agent entering onto the property.

(3) Alert neighbors so they can watch for and witness violations by repossession agent.

(4) DO NOT resort to violence to resist the repossession agent – call the police.

(5) DO NOT resist sheriff/government official. Simply verify identification.

(6) Advise client of the possible adverse credit consequences of resisting repossession.

d) SCRA Interface. The SCRA prohibits the self-help repossession of collateral where the debt arose prior to entry into military service even if the debtor's military status in no way affects the default. 50 U.S.C. App. § 532. The creditor is limited to a judicial action to recover the collateral, and the court, even on its own motion, can stay the proceedings or take other equitable action if the debtor's entry into the military service affects the debtor's ability to repay the debt. Remember to check state law as well. Many states have laws extending the coverage of the SCRA to National Guard members on active duty.

2. Repossession has occurred, but collateral not sold.

a) Reinstate the Contract.

(1) Know your state: A number of states statutorily require the creditor to permit the consumer to reinstate the contract after default and repossession.

(2) This may be labeled redemption or right to cure, but it is not the same as the Article 9, UCC redemption.

(3) The consumer only has to pay the amounts in default PRIOR TO acceleration in order to reinstate the K. Thus the consumer would only have to pay:

(a) The amount in default plus

(b) Repossession charges.

(4) Note that this right is normally limited to a very short period of time, like 15 days after repossession.

b) Redemption.

(1) Article 9 gives the consumer an absolute right to redeem prior to disposition of the collateral. The collateral is considered "disposed of" when a contract disposing of the collateral is entered into.

(2) Here, however, the consumer must satisfy all obligations secured by the collateral. Thus, if the contract has been accelerated, the consumer would have to pay the entire remaining amount due, not just the delinquent installments.

(3) Waiver.

(a) May NOT be waived prior to default.

(b) MAY be waived after default by signing a written waiver. Waiver should be knowing and voluntary.

(4) Who may redeem? Only the "debtor." This term is broad and should include:

(a) The collateral owner and primary obligor on the debt.

(b) Sureties like guarantors and cosigners.

(5) Tender.

(a) Debtor should determine from creditor the exact amount due – get it in writing!

(b) Tender must be made physically – Show me the money!

(c) Tender must be unconditional.

c) Minimizing the Potential Deficiency.

(1) Strict Foreclosure.

(a) Creditors may propose that they simply keep the collateral as full satisfaction of the debt.

(b) They also get to keep all prior payments and do NOT have to return any surplus.

(c) Buyer can object within 21 days of creditor's notice.

(d) Where consumer has paid 60% of the debt, strict foreclosure is not allowed.

(2) Object to unreasonable delays in sale (that might impact value of car). Sale must be made in a commercially reasonable manner.

(3) Encourage others to attend sale.

3. Use of Warranty Law to Combat Repossession (See Chapter 5 for more detail).

a) Revocation of acceptance. If the car has not been repossessed and there are substantial nonconformities with provisions of an express or implied warranty, revoke acceptance prior to the repossession.

(1) Protects the consumer from deficiencies.

(2) Requires return of moneys already paid.

b) Deducting Damages from Balance Due. Article 2 (§ 2-717) of the UCC allows the consumer to deduct damages caused by the dealer's breach from the amount owed. This may cure the default.

(1) Warn clients that repossession will probably still occur and they will be fighting this out in court.

(2) A strong letter to creditors, however, may prevent the repossession and bring them to the bargaining table.

CHAPTER 10

LANDLORD-TENANT LAW

TABLE OF CONTENTS

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CHAPTER 10

LANDLORD-TENANT LAW

I. REFERENCES.

A. Schoshinski, Robert S., AMERICAN LAW OF LANDLORD AND TENANT, 1980 with 1993 Supplement.

B. AR 27-3, The Army Legal Assistance Program (21 February 1996).

C. Uniform Residential Landlord and Tenant Act (URLTA).

D. NATIONAL CONSUMER LAW CENTER, ACCESS TO UTILITY SERVICE (3d ed. 2004 and Supp. 2006). [Hereinafter, "NCLC ACCESS"]

E. Attached is a German Landlord Tennant Information Paper authored by the Schweinfurt Law Center, part of the Great 1st Infantry Division OSJA.

F. HierosGamos, Landlord & Tenant Law: www.hg.org/landlord.html

G. Nolo, Landlords & Tenants: www.nolo.com/lawcenter

II. ELIGIBLE CLIENTS.

A. Army.

1. Legal Assistance Attorneys (LAA) will provide legal assistance and advice on consumer affairs and landlord-tenant matters. (AR 27-3, Paras. 3-6c., d., and e.).

2. LAA may draft leases, but may not help clients with issues involved in income producing business activities. (AR 27-3, Para. 3-6c., 3-8a.(2)).

3. Tenants - military members who rent from either civilian or individual military landlords. (AR 27-3, Para. 3-6c.).

a) Assistance WILL be provided on:

(1) Leases, issues, and disputes involving the military member's principal residence.

(2) Termination of pre-service leases under the SCRA.

b) Legal Assistance MAY be provided:

(1) On matters relating to the purchase, sale, or rental of a client's principal residence or other real property.

(2) This assistance, if provided, is not prohibited by the limitation on private business activities. (AR 27-3, Para. 3-8a(2)).

c) LAA should not review a lease on behalf of a tenant when another attorney in the office drafted it on behalf of the landlord.

4. Landlords - military members renting out property in the hope of returning to the home, as an investment, or renting out property due to an inability to sell the property in conjunction with transfer. (*See* definition of "Private business activities in AR 27-3, Glossary.)

B. Air Force.

1. The Air Force considers Landlord-Tenant issues mission-related legal assistance.

2. Assistance must be provided to "active duty members, including reservists and guardsmen on federal active duty under Title 10 U.S.C., and their family members entitled to an identification card, and for civilian employees stationed overseas and their family members entitled to an identification card, and for civilian employees stationed overseas and their family members residing with them who are entitled to an identification card, . . ." Para. 1.3.1, AFI 51-504 (1 May 1996).

C. Navy.

1. Tenant Services.

a) Review leases, provide language and suggested modifications, and advise clients on rights and remedies.

b) Attorneys may contact landlords on behalf of clients and negotiate or participate in ADR.

2. Landlord Services.

a) May advise landlords on the renting of a former principal residence including lease preparation.

b) LAAs may assist the landlord in negotiating with prospective tenants and use of ADR.

c) Properties held primarily for investment or production of income are considered businesses and landlords of these properties are not eligible for legal assistance services.

III. CONSUMER LAW CAN HELP IN LANDLORD TENANT CASES.

A. Ultimatums about rent may fall within the Fair Debt Collections Practices Act. *Romea v. Heiberger & Associates*, 988 F.Supp. 712 (S.D.N.Y. 1997).

B. Absent consent, landlord access to credit reports when making rental decisions is limited. *Ali v. Vikar Management Ltd.*, 994 F.Supp. 715 (S.D.N.Y. 1998).

IV. LANDLORD'S OBLIGATIONS.

A. Covenant of Quiet Enjoyment. Generally ensures that the tenant's enjoyment and use of the premises is protected against the landlord or some other taking through the landlord.

1. Eviction

a) Is a BREACH of the lease if:

(1) The tenant is physically evicted from the property; AND

(2) That action was wrongful.

b) Can be caused by actions of the landlord or by third persons for whom the landlord is responsible.

c) Relieves the tenant of any further obligation to pay rent, even in jurisdictions that view the tenant's rent obligation as separate and distinct from the landlord's breach generally!

d) May be partial! *See, e.g., Washburn v. 166th East 96th Street Owners Corp.*, 166 A.D.2d 272, 564 N.Y.S.2d 115 (1990) (Transfer of roof

area adjacent to penthouse from exclusive tenant use to common use was a partial actual eviction.)

(1) The expulsion of the tenant is from a significant part of the premises.

(2) Tenant may remain in possession of the part she is not expelled from.

(3) Tenant does NOT have to pay ANY of the RENT!!!

2. Constructive Eviction. *See, e.g., Home Rentals Corporation c. Curtis*, 236 Ill.App.3d 994, 602 N.E.2d 859 (1992); *Manhattan Mansions v. Moe's Pizza*, 149 Misc.2d 43, 561 N.Y.S.2d 331 (1990).

a) Covers actions of the landlord that fall short of actual physical expulsion.

b) To be actionable the landlords action must.

(1) Be injurious to the tenant's use and enjoyment of the premises.

(2) Be so severe that they justify abandonment by the tenant. Tenant must:

(a) Establish that the interference is substantial and not just incidental.

(b) Show that the landlord intended to evict tenant. NOTE: The landlord is PRESUMED to intend the natural consequences of his actions.

(c) Abandon the premises within a reasonable time after the landlord's interference begins.

(d) Give the landlord an opportunity to correct the situation.

c) Constructive eviction is a question of fact for the trier of fact.

d) Some states allow a PARTIAL constructive eviction. *See Moe's Pizza* above.

e) Examples.

(1) Successful

(a) Interference with access to the leased premises (e.g. obstructions in walkways or hallways).

(b) Lost use of rights or an easement.

(c) Loss of light, air, or ventilation.

(d) Persistent, harmful, and offensive odor.

(e) Water Leaks.

(2) Not Successful

(a) Actions of neighbors

(i) But may be responsible if he allows extensive remodeling.

(ii) May be responsible if he fails to take sufficient action to abate a nuisance.

3. Remedies for Actual & Construction Eviction.

a) Treat the tenancy & rent obligation as terminated.

b) Action for recovery of possession (Actual Eviction).

c) Seek Injunctive Relief (Constructive Eviction)

d) Action for Damages. (There is a split about whether you can get these without vacating the premises).

(1) Usually measured by the difference between the reserved rent and the fair rental value for the remainder of the term.

(2) May be able to get special damages (such as relocation expenses) for wrongful evictions.

B. Responsibility for Condition of the Premises.

1. Traditional Rule - *Caveat Emptor*

2. Latent Defects

a) Defects which tenant could not reasonably have made herself aware.

b) Landlord must disclose.

c) If not, Tenant may:

(1) Vacate the premises.

(2) Sue for Damages

(3) If he vacates, avoid any further obligation for rent.

(4) Recover special damages, such as damage to his property.

3. Duties to Repair

a) Common Law

(1) No obligation EXCEPT

(2) Areas he still controls (like common areas).

(3) Relief limited.

(a) Obligation to pay rent continues.

(b) Tenant may NOT abandon the premises.

b) Express Covenants may modify this.

c) Many states have modified this with statute.

C. Implied Warranty Of Habitability.

1. Formerly, provisions like the following were indicative of the doctrine of *caveat emptor* in leasing:

   "Tenant has inspected the premises and finds them to be in good and habitable condition. At all times and at the Tenant's own expense, Tenant shall maintain the premises in a good and habitable condition, including all appliances and equipment. Tenant shall make all repairs required for exposed plumbing and electrical wiring."

2. Implied warranty of habitability is result of judicial frustration with the impotence of the tenant.

   a) *See Javins v. First National Realty Corp*, 428 F.2d 1071 (D Cir.), *cert. denied*, 400 U.S. 925 (1970). The warranty, which is normally implied with respect to residential (v. commercial), multiple-family dwellings, constitutes an obligation by the landlord to:

      (1) Deliver and ,

      (2) Maintain a habitable dwelling.

   b) States adopting implied warranty of habitability differ regarding remedies, measure of damages, precise standards of habitability. Some states consider the following in addition to compliance with housing code:

      (1) Nature of defect.

      (2) Effect on safety or sanitation.

      (3) Length of time it persisted.

      (4) Age of structure.

      (5) Amount of rent.

      (6) Tenant's intelligent waiver of defect.

      (7) Attribution of defect to tenant's own abuse.

3. Some states have codified implied warranty of habitability(Hawaii, Maine, Michigan, Minnesota, Washington, and West Virginia), imposing a wide

range of contractual duties on the landlord and affording the tenant a broad range of remedies unknown at common law.

a) *See Aspon v. Loomis*, 816 P.2d 751 (Wash. App. 1991). Court disapproved standard jury instruction that "a landlord has a duty to use ordinary care to keep the premises fit for human habitation at all times during a tenancy." A landlord's duty to tenant is restricted to those duties enumerated by statute.

b) Application of the implied warranty is contingent on tenant's notice to landlord of defective conditions plus reasonable time to repair.

c) Courts generally find breach only when premises rendered truly unsafe, unsanitary, or uninhabitable.

4. Waiver of Implied Warranty.

a) Tenant's continued occupancy of uninhabitable premises generally not a waiver.

b) "No waiver rule."

(1) Private agreements to shift duties fixed by warranty illegal and unenforceable.

(2) Rule has been adopted in some states (i.e. Wash.; D.C.; Mass.; Pa.).

(3) Uniform Residential Landlord and Tenant Act prohibits lease provisions waiving warranty.

(4) Restatement (Second) of Property allows waivers if not unconscionable.

5. Remedies.

(1) Common Law/Contractual.

(2) Rescission.

(3) Withhold part or all of rent.

(4) Pay rent and sue for damages.

(a) *Wade v. Jobe*, 818 P.2d 1006 (UT. 1991). Once landlord breaches duty to provide habitable conditions, tenant may withhold rent or continue to pay rent to landlord and then bring action for reimbursement for excess rent paid. Special damages also recoverable.

(b) Action for specific performance.

b) Statutory Remedies.

(1) Rent abatement.

(2) Repair and deduct. The states which have such statutes include AZ, CA, MT, ND, LA, SD, and WA.

(3) Rent escrow until repairs made. The states which have such statutes include: MD, MA, MI, MO, NJ, NY, OH, PA, TN, and VT.

(4) Appoint receiver to apply rent to repairs. The states which have such statutes include: CT, IL, IN, MA, MI, MN, MO, NJ, and NY.

(5) Suits for damages and specific performance.

(a) Example: Idaho § 6-320 - A tenant may file suit for failure to provide reasonable weatherproofing and weather protection of the premises; failure to maintain in good working order electrical, plumbing, heating, ... or sanitary facilities supplied by landlord; maintaining premises in manner hazardous to health or safety of tenant...

(b) King v. Brace, 552 A.2d 398 (Vt. 1989). Punitive damages against lessor of mobile home park rendered uninhabitable when lessor failed to remedy problems despite repeated requests by lessee and notices from health authorities.

V. TENANT'S OBLIGATIONS.

A. Rent.

1. Existence of a Tenancy is a Prerequisite to Paying Rent.

2. Normally contractual - a specific covenant in the lease specifies the amount of the rent.

    a) If no amount is stated, the tenant would be liable for the reasonable value.

    b) May include collateral payments (e.g. tax payments, utility payments, etc.) as part of the rent.

3. Promises to change the rent (up or down) must be supported by fresh consideration.

4. Place & Mode of Rent Payment

    a) Generally, AT the premises unless the parties agree otherwise. Therefore, the landlord is supposed to come and pick up the rent.

    b) Changes to the location can be established by the parties' practice with regard to past rent payments.

    c) Rent is normally payable in money, which may be paid in the form of check.

    d) Can be made by mail if the parties so agree.

5. When is the Rent Due? (Time of Payment).

    a) Generally accrues on the day it is payable, NOT day to day.

    b) Unless the parties agree otherwise, the rent does not accrue until the period which that rent covers is complete. Provisions in the lease regarding this are construed strictly

6. Other charges.

    a) Rent Acceleration.

(1) Makes all rent under the lease due and payable upon the default of the tenant on any installment.

(2) Some states allow these provisions to take effect.

(3) Others view this as an unenforceable penalty.

b) Late Payment Charges.

(1) Specific Dollar or a percentage fee if the rent is late.

(2) Most states allow. There are two approaches:

(a) The charge is considered interest in which case it must comply with usury laws.

(b) The charge is considered liquidated damages. In that instance it must:

(i) be a good faith estimate of the loss likely to incur.

(ii) bear a reasonable relationship to the loss likely to occur.

(c) Look to case law in you jurisdiction. Particularly where the lease is residential, courts have sometimes struck these down if they are excessive.

B. Duty to Repair.

1. Common Law: Absent an express provision, tenant was required to make minor repairs to preserve the premises.

2. Modern Statutory Schemes.

a) Largely relieves tenant of obligations to repair.

b) However, must notify landlord and give landlord opportunity to repair. If not, and damage occurs because of situation of which landlord was not aware, tenant may be liable.

c) Many place obligations on tenants to maintain the dwelling in “clean and sanitary” condition.

3. Express covenants to repair may be enforceable, but this is unclear in jurisdictions with statutory schemes.

C. Landlord's Remedies For Tenant's Breach.

1. Self-help repossession.

2. Many states limit or disallow self-help.

3. Trend - make legal process the landlord's exclusive remedy. In many jurisdictions, landlord liable for punitive damages if uses self help.

4. The Restatement (Second) of Property takes the position that the availability of summary eviction bars the use of self-help by the landlord "unless the controlling law preserves the right of self-help."

5. Summary eviction.

a) Statutory summary eviction procedures in all states.

(1) Avoids protracted process required for writs of ejectment.

(2) Avoids potential for violence and physical injury inherent in a landlord's attempt to recover possession personally.

b) Available when the tenancy term expires and tenant refuses to leave the premises or upon certain statutorily enumerated conditions, such as the tenant's failure to pay the rent.

6. Service Members' Civil Relief Act.

a) Prevents eviction of service member or dependent for nonpayment of rent without court order.

b) Military service affects ability to pay.

c) Rent does not exceed $2465.00 for 2004 and the act has a calculation for rent ceiling for subsequent years based on the housing price inflations adjustment.

d) Court shall upon application or *sua sponte* stay the proceeding for a period of 90 days unless in the opinion of the court, justice and equity require a longer or shorter period.

e) Criminal sanctions are possible for self-help repossessions.

f) The court can order and allotment from the pay of the servicemember.

7. Landlord's liens.

a) Statutory liens.

b) Contractual liens.

c) Retention of security deposit.

8. Landlord's Duty To Mitigate.

a) Common Law - No duty to mitigate.

b) Contract based doctrine.

(1) Recoverable losses limited to damages unavoidable through reasonable effort.

(2) Not all states require mitigation.

c) Uniform Residential Landlord Tenant Act, 78 U.L.A. 427 (1974).

(1) Contains statutory language imposing obligation to mitigate damages on landlord.

(2) Under the Act, if landlord fails to use reasonable efforts to relet at fair market rental, lease is deemed terminated as of date landlord has notice of abandonment.

(3) Adopted by at least 15 states.

VI. SELECTED MILITARY TENANT ISSUES.

A. Early Lease Termination Due To Military Exigencies.

1. Termination of Leases of Premises. Servicemembers Civil Relief Act Pub. L. No. 108-189, § 305).

   a) A lease of premises occupied, or intended to be occupied, by a servicemember or a servicemembers dependents for a residential, professional, business, agricultural, or similar purpose if

      (1) The servicemember, while in military service, executes the lease and thereafter receives military orders for a permanent change of station or to deploy with a military unit for not less than 90 days.

      (2) The lease is executed by or on behalf of a person who thereafter and during the term of the lease enters military service. The termination may be made by a service member entering active duty [or by his or her dependent in their own right (see § 536/§305)].

   b) Question: If a pre-service lease was signed only by non-military spouse, could he or she terminate the lease?

      (1) Yes. Dependents have protection in their own right even though § 534 says the lease must be executed by or on behalf of the service member.... (use § 536 to insert "by or on behalf of the dependent."

   c) Question: What if the non-military person signed the lease before marrying a person who enters military service..... could the non-military spouse terminate the lease?

      (1) Arguably, yes. *See Tuscon Telco Federal Credit Union v. Bowser*, 451 P.2d 322 (Ariz. Ct. App. 1969) (single woman entered chattel mortgage on car, was subsequently married to civilian who was later drafted; car registered solely in her name and she alone made payments before repossession; court held that repossession without court order violated § 532, SSCRA. SSCRA applied because her ability to pay was impaired by husband's subsequent induction.

   d) Manner of Termination - Deliver written notice of termination and copy of military orders

      (1) By hand

(2) By private business carrier

(3) By U.S. mail

e) Effective Date of Termination- the lessee may at their option terminate the lease any time after entry into military service of the date on their orders.

(1) If lease provides for monthly payment – the lease terminates 30 days after the first date on which the next rental payment is due after notice is delivered.

(2) If no monthly payment, effective on the last day of the month following the month in which notice is delivered.

f) Relief to Lessor

(1) Can go to court before termination date and make application for relief which can be granted as justice and equity require.'

g) Penalties

(1) If the person knowingly holds, security deposit, or personal effects or other property of the service member or his dependents protected under this provision, or tries to prevent removal of property can be fined as provide in title 18, United States Code, or imprisoned for not more than one year.

h) Practice point

(1) The Texas Landlord Association has taken the position in 2004 that in order for dependents to terminate their property interest in a lease (both servicemember and spouse on lease) under §305 that they are required to make application to a court under §308 which states:

(a) Upon application to a court, a dependent of a servicemember is entitled to the protections of this title if the dependent's ability to comply with the lease, contract, bailment, and other obligation is materially affected by reason of the servicemembers military service.

(2) Try to argue that if the servicemember's name is jointly on the actual lease than the lease can be terminated once the requirements under §305 are met and that §308 only pertains to the situation where the dependent is the only name on the lease and then the dependent could be required to show how the servicemembers military service materially affected the defendant in court.

2. Other Termination of Leases.

a) State Statutory or contractual provisions for early residential lease termination are designed to meet the exigencies of military service - when a service member (either as a tenant or a landlord) must move unexpectedly due to military orders.

(1) The soldier landlord who receives orders back into the area may wish to terminate his/her tenant's lease to allow him/her to reoccupy the residence.

(2) Question: If a soldier simply wanted to break an apartment lease to move into a house in the same location, would a "typical" military clause allow lease termination? No. (Of course, other contract terms could be negotiated).

(3) Some states allow termination when the service member is released from active duty (see VA Code Ann. § 55-248.21:1), others are silent on that issue - leaving it unclear whether receipt of "PCS orders" is synonymous with orders to leave active duty. For example, the Maryland early lease termination statute failed to address this point. On September 15, 1992, the Md. Attorney General issued an opinion that allows military personnel who are released from active duty and ordered to report to their home of record to terminate their residential leases.

3. Military clauses may be part of a contract or statutory.

a) Attorneys should be careful not to "contract away" Federal or State statutory protections by drafting inconsistent "military clause" language into a lease.

b) States having military clause protection by statute:

State	***Cite***	***Limitations***
Arizona	ARIZ. REV. STAT. ANN. § 33-1413 (1995)	Mobile Homes Only
Connecticut	CONN. GEN. STAT. § 21-82(11) (1994)	Mobile Homes Only
Delaware	DEL. CODE ANN. tit. 25, §§ 5314(b), 7007, 7012 (1996)	
Florida	FL STAT §83.828	
Georgia	GA. CODE ANN. § 44-7-37 (1996)	
Idaho	IDAHO CODE § 55-2010 (1996)	
Kansas	KAN. STAT. ANN. §§ 58-2504, 58-2570 (1995)	
Maryland	MD. CODE ANN., REAL PROP. § 8-212.1 (1995)	
Missouri	MO. REV. STAT. § 41.944 (1995)	
North Carolina	N.C. GEN. STAT. § 42-45 (1995)	
Oregon	ORS CHAPTER 90 (1999)	
Pennsylvania	PA CON. STAT. TITLE 51§ 7315 (1991)	
Rhode Island	R.I. GEN. LAWS § 31-44-7 (1995)	Mobile Homes Only
Virginia	VA. CODE ANN. § 55-248.21:1 (2002)	Liquidated damages authorized. – see Statute
Washington	WASH. REV. CODE § 59.20.090 (1995) §59.18.200, §59.18.220 (2003)	

4. Sample Contractual Military Clause.

a) Although the SCRA now allows post service termination of leases, the act does not cover all possible situations and thus the servicemember may still need a military clause included in the actual lease.

(1) **MILITARY LANDLORD**: In the event LANDLORD is or hereafter becomes a member of the United States Armed Forces, then LANDLORD may terminate this lease on thirty days written notice to TENANT in any of the following events:

If LANDLORD receives permanent change-of-station orders to return to the area in which the premises are located.
If LANDLORD is released from active duty.
Other: _____

(2) **MILITARY TENANT**: In the event TENANT is or hereafter becomes a member of the United States Armed Forces, TENANT may terminate the lease on thirty days written notice in any of the following events:

If TENANT receives permanent change-of-station orders to depart from the area in which the premises are located.
If TENANT is released from active duty.
If TENANT has leased the property prior to arrival in the area and TENANT is ordered to a different area before occupying the property.
If TENANT has been ordered to on-post housing.
Other: _____

(3) **MILITARY NOTICE AND RENT ADJUSTMENT**: Notice furnished under the provisions of this paragraph shall include a copy of official orders or a letter signed by the party's commander reflecting the circumstances warranting termination under this paragraph. If LANDLORD terminates the lease under this paragraph, a credit shall be allowed toward the rental otherwise due, and if TENANT terminates the lease under this paragraph, TENANT shall pay an amount in addition to the rental otherwise due. Such adjustment (credit or addition) shall constitute a liquidation of the damages caused by such termination, but shall be in addition to a proration of the rental to the actual termination date and shall not reflect any actual physical damages to the property for which TENANT is otherwise liable under this lease. Said adjustment amounts shall be computed as follows:

If termination occurs before expiration of one-half of the original term, without extension, _____ percent of one month's rent.
If termination occurs on or after the period stated above but before the end of the original term, without extension, _____ percent of one month's rent.
If termination occurs on or after the end of the original term of the lease, without extension, there shall be no adjustment of rent under this paragraph.

5. SAMPLE STATUTORY MILITARY CLAUSE

a) Va. Code Ann. § 55-248.21:1 (1996) (excerpt):

Any member of the armed forces of the United States or a member of the Virginia National Guard serving on full-time duty or ... may... terminate his rental agreement with the landlord if the member

has received permanent change of station orders to depart thirty-five miles or more (radius) from the location of the dwelling unit;

has received temporary duty orders in excess of three months' duration to depart thirty-five miles or more (radius) from the location of the dwelling unit;

is discharged or released from active duty with the armed forces of the United States or from his full-time duty ... with the Virginia National Guard; or

is ordered to report to government-supplied quarters resulting in the forfeiture of basic allowance for quarters.

B. Security Deposits

1. Common Law. (Now modified by statute)

a) No ceiling on the size of the tenant's security deposit.

b) Landlord not obliged to pay interest on the deposit or to avoid commingling deposit with the landlord's own funds.

c) Ordinarily, tenant cannot compel landlord to return deposit or to apply deposit to rent or damages while the tenancy or tenant's obligations continue.

d) See also, *Burgess v. Stroud*, 17 Kan. App. 2d 560, 840 P.2d 1206 (1992). A Kansas statute stating that a tenant forfeits the security deposit if the tenant applies or deducts any portion of the deposit from the last month's rent requires affirmative action on the part of the tenant, and not simply an action or silence such as delivering notice to vacate without any payment for rent.

e) If the landlord's deductions are challenged, burden of proving the absence of damages sustained was on the tenant.

2. State Statutes.

a) Limit the size of the deposit that a landlord can demand (usually limiting this to 1 to 2 months' rent).

(1) Regulate the landlord's use of the deposit during the tenancy.

(a) Require that interest be paid on the deposit.

(b) Require that the deposit be refunded within a specified period of termination, often 30 to 60 days.

(2) Require that landlords furnish tenants an itemized list of deductions from the deposit. *See, e.g., Duchon v. Ross*, 599 N.E, 2d 621 (Ind. App. 1992). Even if cost of repair is in dispute, landlord must comply with statute requiring accounting within 45 days of itemized costs to repair and refund of difference between repair costs and security deposit.

(3) Provide for return of the entire deposit, punitive damages, and attorneys' fees for the tenant if the landlord fails to comply with the statute.

(a) Burden on the landlord to prove damages caused by the tenant in order to retain deposit. *See, e.g., Battis v. Hofman*, 832 S 2d 937 (Mo. App. 1992). If landlord fails to return security deposit within 30 days and it is later discovered tenant is entitled to it, then landlord has wrongfully withheld under the Missouri statute providing for penalty, regardless of landlord's intent. Court may consider reasons money withheld in determining penalty to impose.

(b) *See, Love v. Monarch Apartments*, 771 P.2d 79 (Kan. App. 1989). Statutory damages mandatory under Kansas law for wrongfully withholding security deposit , even if landlord acted in good faith and tenant suffered no damages.

C. Discrimination.

1. Additional References

a) Fair Housing Act, Title VIII of the Civil Rights Act of 1968, as amended. 42 U.S.C. §§ 3601-3631.

b) DoD Instruction 1100.16, Equal Opportunity in Off-Base Housing (14 August 1989).

c) Chapter 2, DoD 4165.63-M, DoD Housing Management (September 1993).

d) AR 210-50, Housing Management (3 Oct 2005).

e) AR 190-24, Armed Forces Disciplinary Control Boards and Off Installation Liaison and Operations (27 July 2006).

f) AR 600-20, Army Command Policy para. 6-10 (7 June 2006).

2. Fair Housing Act, Title VIII of the Civil Rights Act of 1968, as amended. 42 U.S.C. §§ 3601-3631.

a) Equal opportunity for all citizens in obtaining housing regardless of race, color, religion, sex, national origin, age, handicap or familial status. (See Fair Housing Amendments Act of 1988; see also, state statutes).

b) Applicable within the U.S.

c) OCONUS, intent carried out to extent possible within laws and customs of foreign country.

3. DOD Instruction 1100.16, Equal Opportunity in Off-Base Housing (14 August 1989) - eliminate discrimination in off-base housing to include familial status discrimination.

a) Army Implementation: AR 210-50, Housing Management (1 Sept 1997), Chapter 6, Community Homefinding, Relocation, and Referral Office (CHRRO).

b) Navy/Marine Corps: SECNAVINST 5350.14 (2 February 1993).

c) Air Force: Section 1.30, AF HB 32-6009, Housing Handbook (1 June 1996).

4. Provisions of DoD Program.

a) Intent of Program: To eliminate discrimination in housing against DoD Personnel on the basis of race, color, religion, gender, national origin, age, physical disability, or familial status.

b) An agent's refusal to show, rent, lease, or sell otherwise suitable housing may be basis for housing discrimination complaint, as well as agent's words or statements.

c) Legal assistance must be provided to complainants to the extent that they are eligible under the program. DoD Inst. 1100.16, pg. 4-2.

d) Housing Referral Services (HRS) or CHRRO.

(1) Maintains listings of adequate off-post rental and sales units reflecting full range of prices, sizes, and locations. Also lists property and agents against whom restrictive sanctions have been imposed for founded discrimination complaints.

(2) Processes Off-post housing discrimination complaints concerning DoD personnel.

e) Processing complaints.

(1) Refer complaint to HRS or CHRRO which makes a preliminary inquiry.

(2) Time limits:

(a) All complaints must begin within 3 working days of receiving the complaint. DoD Inst. 1100.16, pg. 4-2.

(b) ARMY: Each allegation processed within 30 days of complaint with provision for 10-day extension. (AR 210-50, para. 6-12c.)

(3) Use of "verifiers" is authorized. (DoD 1100.16, pg. 4-3; AR 210-50, para. 6-14). The purpose of verification is to isolate the attribute of race, color, religion, sex, national origin, age, handicap, or familial status that is the suspected basis for the alleged discrimination against the complainant.

(4) Informal hearing. Conducted when basic facts of the preliminary inquiry appear to confirm the complaint.

(5) Legal review. DoD 1100.16, pg. 4-4 – 4-5; AR 210-50, para. 6-17.

(6) Commander's actions. DoD 1100.16, pg. 4-5 – 4-8; AR 210-50, paras. 6-18 and 6-19.

(a) If complaint not supported by evidence --

(i) Advise complainant of action and rights.

(ii) Advise alleged discriminator.

(iii) Send file to Department of Justice or Department of Housing & Urban Development if complainant requests.

(b) If complaint supported by the evidence --

(i) Impose restrictive sanctions for minimum of 180 days.

(ii) Service members renting BEFORE the imposition of sanctions MAY continue to rent and MAY renew. NEW rentals, however, are prohibited. DoD Inst. 1100.16, pg. 4-8.

(c) Removal of sanctions. DoD Inst. 1100.16, pg. 4-8; AR 210-50, para. 6-22.

(i) Before 180 days:

(a) ARMY: Only HQDA may remove and then only if unusual circumstances are shown.

(b) DoD-Wide: Approved waiver request must go to service department from Senior Installation Commander.

(ii) After 180 days: Local commander may remove upon receipt of written assurance of nondiscrimination in the future.

f) Housing Discrimination Overseas. DoD Inst. 1100.16; AR 210-50, para. 6-23.

(1) Civil Rights Act of 1866 and Fair Housing Act inapplicable.

(2) Process complaint as if in the United States, but do not forward case to HUD or DOJ.

(a) Consider local laws,

(b) Determine if any civil redress can be pursued. Many nations have laws prohibiting discrimination. Your OSJA may have access to, or employ, a local attorney.

(c) Consider Status of Forces Agreement.

D. Protecting Tenants at Foreclosure Act of 2009

1. On 20 May 2009 the President signed S. 896, the "Protecting Tenants at Foreclosure Act of 2009." This Act has now been codified as Public Law 111-22.

2. Section 702 of the Act provides that, for any foreclosed residential property purchased with a "federally related" mortgage loan (defined below), a tenant living in the property under a conventional lease agreement has a right to remain in the property until the end of the lease, subject to specific exceptions.

3. Essentially, "federally related" mortgage loans are either: (1) regulated, insured, or otherwise assisted by the Federal Government; (2) included in a housing or urban development program administered by the Federal Government; or (3) intended to be sold by the lender to the Federal National Mortgage Association or the Government National Mortgage Association. For example, any Veterans Administration (VA) loan or Federal Housing Administration (FHA) loan qualifies as a "federally related" loan. However, a loan from a private company that does not take any federal funds may not qualify as a "federally related" loan. Those seeking additional "light reading" are encouraged to review 12 U.S.C. Section 2602 for a complete definition.

4. Nothing in this act affects the validity of any state or federal law currently in existence that provides additional legal protections for tenants. In particular, legal assistance practitioners should remember Section 301 of the Servicemember's Civil Relief Act (SCRA) (50 U.S.C. App. 531), which precludes the eviction of a servicemember or dependents from a rented property without a court order. This is especially important in cases where

mortgage loans may not be "federally related." For 2009, the maximum monthly rent covered by the SCRA is $2932.21.

E. American Recovery and Reinvestment Act of 2009: Expansion of the Homeowners Assistance Program

1. The American Recovery and Reinvestment Act of 2009 (ARRA) temporarily expands the existing Homeowners Assistance Program (HAP) to cover certain persons affected by BRAC 2005, certain persons on permanent change of station (PCS) orders, and certain wounded persons and surviving spouses.

2. Section 3374 of Title 42, United States Code, as amended by Section 1001 of the ARRA, authorizes the Secretary of Defense, under specified conditions, to acquire title to, hold, manage, and dispose of, or, in lieu thereof, to reimburse for certain losses upon private sale of, or foreclosure against, any property improved with a one- or two-family dwelling owned by designated individuals.

3. The broadest relief is in another part of section 1001 which offers "temporary homeowner assistance for members of the Armed Forces permanently reassigned during specified mortgage crisis." Specific requirements apply including:

   a) the property involved is the current principal residence of the servicemember;

   b) that the property was **purchased** by the servicemember **prior to July 1, 2006**;

   c) that the servicemember was "permanently reassigned" on orders "to a duty station or home port outside a 50-mile radius" of the prior base or installation; and

   d) the qualifying property was sold by the owner between July 1, 2006 and September 30, 2012 (or some earlier date in the regulations).

4. The program is administered by Headquarters, United States Army Corps of Engineers (HQUSACE).

VII. ACCESS TO UTILITY SERVICE.

A. Types of Utilities

1. Regulated - Public Utilities.

   a) Definition: "A business whose services are sufficiently important so as to warrant government regulation; . . . . The public interest is implicated because the commodity which the utility provides -- whether electric, gas, water, or telephone service -- is viewed as being of great economic consequence." NCLC ACCESS at 27.

   b) Characteristics:

      (1) The nature of the industry is such that the market would not produce many competitors.

      (2) Facilities must be constructed with "excess capacity" because the commodity they deliver (e.g. electricity) cannot be stored indefinitely, yet consumers expect the service to be available whenever they need to use it.

      (3) Consumer demand for the services is inelastic. That is, the service is viewed as indispensable so there is little if any fluctuation in demand when prices increase.

      (4) Consumers have little choice in who they buy from.

   c) Duties & Obligations

      (1) Provide service on reasonable terms to all who request it.

         (a) Whether or not it is profitable.

         (b) Can be limited to a particular service area; to persons willing to comply with the utilities rules & regulations; and to the amount that they have the technical capacity to support.

      (2) Must provide safe and adequate service to all of its customers.

      (3) Must serve all members of the public on equal terms.

      (4) Must charge "just and reasonable" prices for their services.

   d) Types of Regulated Utilities

(1) Natural Gas

(2) Electric Power

(3) Water

(4) Telephone

2. Unregulated Utilities

a) Municipal Utilities

(1) Most common in electric & water industries

(2) Key distinction is that these are publicly owned, government run utilities, NOT private.

(3) Will usually meet the duties of a public utility, even though they do not answer to any public utility commission.

b) Rural Electric Cooperatives.

(1) Authorized by Congress in 1936.

(2) Some courts will make them comply with public utility duties.

(3) Many view them for what they are today - large scale public utilities.

c) Deliverable Fuels

(1) Propane, oil, kerosene, & wood.

(2) Almost totally unregulated.

(3) Dangerous because they are usually *de facto* monopolies.

B. Payment Issues

1. Late Charges

a) Authorized since 1915. Generally, 1-2 percent per month.

b) Purposes.

(1) To compensate the utility for expenses incurred as a result of the lateness.

(2) To provide an incentive for consumers to make timely payments.

(3) Prevent subsidization of late payers by timely payers.

c) Some states now regulate late charges

(1) Prohibit All Late Charges: AL, CO, VT.

(2) Prohibit Late Charges (Residential Customers): KY, MA, NJ, RI, TX.

(3) Limit Late Charges: D.C., HI, IL, IN, IA, KS, ME, MD, MI, MN, NY, NC, OK, OR, SC, TN, VA, WA, WI.

d) Courts tend to use the "penalty" v. interest distinction discussed with late charges for rent above.

e) Challenging Late Fees

(1) Regulatory Challenges - Use Public Utility Commission (PUC) procedures for states where late charges are regulated.

(2) Late Receipt of Bill/Late payment by others. If the utility bill is late or some other party (like the Army) doesn't issue pay on time, courts will usually not enforce late fees.

(3) Consumer Protection Statutes

(a) Equal Credit Opportunity Act - If late fees are assessed in a discriminatory fashion.

(b) UDAP Statutes (if utilities are not exempted).

(c) Fair Credit Billing Act (at least for unregulated utilities).

(4) Improper Pyramiding - Applying the utility payments to the late fee first, then to the bill causing the consumer to continually underpay and have continual late charges. FTC Rule Prohibits this. 12 C.F.R. § 226.13.

(5) Challenges Based Upon Regulatory Principles

(a) Late charge should only cover reasonable & legitimate expenses.

(b) Late charges should not begin to accrue until a reasonable time (20-30 days) after mailing of the bill

(c) Late payment charges to induce prompt payment

(i) Does this rationale apply if the consumer cannot pay?

(ii) Is the amount excessive for this purpose?

(iii) Some states have a general "residential hardship category" against whom late charges are banned

2. Budget Billing Plans

a) Allowed everywhere except Hawaii and Nebraska.

b) "Level Payment Plans." Allows customer to pay the same amount each month based on estimate of annual usage.

3. Deferred Payment Plans

a) Required in 36 states as an alternative to utility shut-off.

b) Utility must essentially offer credit to the consumer who has failed to pay their bill prior to turning off the service. If the consumer agrees to make all future payments, plus an amount toward the arrearages in installments, the utility must continue to provide service.

C. Fighting Terminations

1. Grounds for Termination

a) Nonpayment of the bill.

b) Meter Tampering or Fraud

c) Misrepresenting Identity to Evade Payment.

2. Protections from Disconnection

a) Special Protections for Elderly, Low-income, & Disabled Consumers

(1) Winter Moratorium: Prohibition against disconnection during certain periods likely to have extreme weather.

(2) Special Payment Plans: See Above.

b) Disputed Bills

(1) Rule found in both common law and regulatory jurisdictions.

(2) Must be a "bona fide" dispute.

(3) Cannot disconnect until the dispute is resolved.

(4) Cannot threaten to disconnect.

(5) Utility may be subject to claims for damages if they violate this rule.

c) Collateral Matters. A utility cannot disconnect a customer based on collateral matters. It must be based on the current contract.

(1) Unrelated contracts/Debts from another time or place.

(2) Separate Business of Utility. Generally, you cannot disconnect a customer from a service simply because they have not paid on a different service provided by the same utility. There are several exceptions:

(a) Water & Sewer. Since use of water necessarily results in waste water, these are not considered collateral. Thus, water utilities CAN disconnect the water for failure to pay the sewer charges.

(b) Local & Long Distance Telephone. Another set of intertwined services. PUCs have long allowed one to be disconnected for failure to pay the other.

(3) Third Party Debts.

(a) Arrearages of Prior Occupant

(b) Landlord in arrears.

(c) Roommate/Family member in arrears.

d) Mistaken Undercharge. After months or years of undercharging, the consumer is presented with a lump sum payment required by the utility. Several theories may help.

(1) Mistake. Basic K doctrine that places the burden of an error on the party most capable of preventing it and most capable of bearing the risk.

(2) Equitable Estoppel.

(3) Past undercharges as a collateral matter.

(4) Regulatory Rules.

e) Proper Notice Before Disconnection.

(1) Required at Both common law and regulatory jurisdictions.

(2) General Requirements:

(a) Notice of the disconnection & the reason therefore.

(b) Hearing or other procedure to protest the disconnection.

(c) Timing of the notice must be sufficient to allow consumer to prepare for and be present at any procedure for objecting to the disconnection.

(d) Except Meter Tampering

D. Erroneous Billing & Unauthorized Use

1. Reverse Metering

a) Due to improper wiring or connection of meters in multi-family dwellings, Consumer A pays Consumer B's bills and vice versa. When the situation is finally rectified, one's bills will probably go up and the other down. Additionally, the electric company may try to collect arrearages from the person who underpaid before, particularly if they have had to credit the other consumer's account. This can result in a large lump sum payment.

b) Generally, the utility MAY collect for the undercharge! Even if the mistake is simply in reading the meter!

c) May be able to use equitable limitations on COLLECTIONS to prevent disconnection of service as a means to force the consumer to pay. *See* the alternate payment methods above.

d) May be able to argue the undercharge amount is "collateral" to the current service.

2. Non-exclusive Use

a) In multiple unit dwellings, through mistake or intention, more than one tenant's service may run from a particular meter.

b) The general rule is that the tenant is on the hook for all metered service and must go after the third party who is tapped into the meter for relief.

c) Some courts, however, have held that one tenant cannot be denied service because another has not paid.

d) Moreover, some jurisdictions are shifting away from the general rule and placing the burden on others more suited to bear it.

(1) IL prohibits billing of a consumer who is the innocent victim of an *illegal* tap. The utility must go against the third party to collect. *Jones v. Peoples Gas Light & Coke Co.*, 97 P.U.R.4th 178 (Ill. 1988).

(2) MA and MD shift the burden to the landlord to either collect from tenants routinely if there is non-exclusive use and pay the bill themselves (MA) or be held liable after the fact for any tenant who does not pay (MD). *See* 105 Mass. Regs. Code §§ 410.354(A) (electric & gas) & 410.180 (water) (1986); *Legg v. Castruccio*, 100 Md. App. 748 (1994).

3. Alleged Unauthorized Use by the Consumer

a) Meter Tampering & Meter Bypass - changing the meter so that it will record less use than what actually occurs.

(1) Disconnection of service

(a) Ordinarily, the utility must still give the consumer notice and an opportunity to dispute the allegation of tampering before disconnection. (Bona Fide Dispute). *See Memphis Light, Gas and Water Division v. Craft*, 436 U.S. 1 (1978) (Supreme Court found a property interest in continued electrical service and held that this interest could not be taken by a government utility without due process (notice & a pretermination hearing)); *Sowell v. Douglas County Electric Membership Corporation*, 258 S.E.2d 149 (Ga. App. 1979)(While the consumer was liable to pay for the service, the utility must still meet its procedural obligations).

(b) However, some utilities have succeeded in terminating without notice by citing safety concerns. *See Hendrickson v. Philadelphia Gas Works*, 672 F.Supp. 823 (E.D.Pa. 1987)(distinguishing *Myers* based on safety concerns because of the particular tampering done).

(c) Generally, If the consumer obtains service through a meter and that meter has been tampered with, there is a presumption that the consumer did the tampering! This is not a universal presumption so check state law.

b) Reconnection - Use mandamus or injunctive actions to force restoring of service.

c) Liability for Unmetered Use

(1) Generally, the utility MAY estimate the use and charge the person who's meter was tampered with or bypassed!

(2) Utility must show two things:

(a) It is entitled to be paid (i.e. the meter was tampered with); AND

(b) The appropriate amount to bill the consumer.

(i) Some courts allow "billing analysis" to suffice.

(ii) Others require more evidence.

4. High Bills - Claims of the fast meter.

a) Some jurisdictions force testing of the meter by the utility if the consumer complains that it is reading too high. These jurisdictions require that this be done free of charge once in certain period.

b) Normally if the test is within a certain tolerance, the meter is deemed accurate.

c) If the meter is running fast, the utility must refund the overcharge. Commissions differ on how many months back the utility must go with this refund.

d) Burden of proof is generally on the customer. Some jurisdictions will accept evidence of usage patterns, even in the face of a tested meter, to establish a claim of overcharging.

VIII. CONCLUSION

SUPPLEMENTARY MATERIAL

Appendix D

Consumer's Guide To Maintaining Utility Service (Appropriate for Distribution to Clients)

It is essential to maintain utility service, such as water, heat, electricity and telephone. But since consumers generally do not have a choice of utility providers, and utility providers are generally allowed by law the drastic remedy of cutting off service to force payment of back bills, consumers are often feel like they are between a rock and a hard place when faced with a large utility bill—pay an unaffordable bill or lose essential service.

This guide to maintaining utility service summarizes for consumers their basic rights when they are facing termination of utility service. It also provides many self-help steps which a consumer may take to lower utility bills and to reestablish service.

The guide is adapted from Chapter 14 on utility service in National Consumer Law Center, Surviving Debt (2d ed. 1996). Permission is granted to duplicate this Consumer's Guide To Maintaining Utility Service for the purpose of making it available to consumers who are faced with high utility bills and/or terminations.

Consumer's Guide To Maintaining Utility Service

Ways to Reduce Your Utility Bills

Even if your most pressing concern at the moment is getting *present* utility bills paid to maintain service, you should still be interested in reducing your bills in the coming months, to avoid repeating the problems of this moment. Here are ideas on how to reduce your bills.

You May Be Eligible for a Discount Utility Service Plan

Some utilities have special programs which will allow you to reduce the *charges* for the utility service that you receive. It only takes some investigation to see what the different utilities have to offer and whether you are eligible for the program.

Discounted Rates for Financially Distressed Households. Many utilities around the nation have special programs for low-income households to help them pay their utility bills. Some of these programs reduce the bills by a set amount each month; others provide discounts based on the amount of the bill. Check with your utility to see what is available.

PIPS or Energy Assurance Programs. A growing number of utilities have plans by which families pay only a certain percentage of their income instead of the amount called for by their normal utility bills. This results in lower bills. Typically, a low-income family's consistent payment of the lower amount is rewarded by gradual forgiveness of old unpaid bills. So you get two benefits in one.

These plans are sometimes called Percentage of Income Plans (PIPs) or Energy Assurance Plans (EAPs), but each utility seems to have its own unique name for the program. The best way to determine if a utility has such a program is to contact that particular utility or the public utility commission in your state capitol.

Telephone Discounts. In most states, households in financial distress can obtain a significant discount on telephone monthly charges under the "Lifeline" program run by your local phone company. Contact the public utility commission or the local telephone company for details.

Eligibility. Eligibility for each of these programs vary considerably. Some look at household income, others look for receipt of, or eligibility for, governmental benefits such as Social Security. SSI, Aid to Families with Dependent Children (AFDC), Food Stamps, or the Low Income Home Energy Assistance Program (LIHEAP). Check with your utility company to see if you are eligible.

Changing the type of Service Can Reduce Your Bill

You may be receiving some utility services which you can fairly easily do without. While the charges for each of these individual services may not seem a lot, together they can add up to quite a few dollars each month. A careful review of your bills and a discussion with each utility company may yield some real savings.

Local Telephone Service. Examine your telephone bill. Are you paying for call waiting, call forwarding, call answering and other high tech services? Can you do without these services? Are you paying for extended area service (local rates for calls to an area which otherwise would be long distance)? How much is this costing you, and do you really call to the extended area enough to justify the extra cost each month? Another question is whether you are you paying a lot for local measured service—which is when you are billed separately for each local call. Contact the telephone company and see if they have different programs which might save you money.

Long Distance Telephone Calls. How much does your long distance service cost? Shop around with the different long distance carriers. Their various deals are often complicated, but can result in significant savings depending upon your calling patterns. Some programs have less expensive calls during the day, others at night. Look for the long distance service which best fits your actual calling patterns.

Long Distance Telephone Charges For Calls You Did Not Make. If you are billed for calls that you did not make, or do not feel you owe the full long distance bill, you may not have to pay the bill. While some states *prohibit* the local telephone company from terminating your service for nonpayment of long distance service, the majority of states do not yet have these protections. Check with your public utility commission to find out the rules for this.

Also, to prevent bills for unauthorized calls from occurring in the future, you may want to investigate a blocking service. Every local telephone company must provide a service to its customers which will block long distance calls from being made unless a password is used, or some other device. The local telephone company can charge for these blocking services, yet they are not foolproof. A creative and sneaky friend or relative can figure out a way around the long distance blocking, and you will still be charged for the calls. So be careful who you let use your telephone.

Other Telephone Charges. Are you being billed high amounts for 900 calls or other "audio text services" that you didn't make or didn't authorize? Every local telephone company is prohibited from terminating your *local* telephone service for nonpayment of these "pay per call" services. Further, you can put a block on your telephone so that these calls can no longer be billed to your telephone. Unlike the block for long distance service, this block should be free, and should be foolproof.

Cable TV Service. Are there cable TV services that you can drop? Can you return to using an antenna for your television, and save yourself the whole bill?

Electric Service. Sometimes you can save considerably by going to a "time of use" type of service with your electric supplier. Whether you actually save money is entirely dependent on the type of program that your electric supplier has and your household's actual electric use patterns. A "time of use" type of service means that you are charged less for using electricity at some times of the day—generally during the evening and night hours and the weekend, and more for electricity used during the daytime. These programs often work well for households where no one is home during most of the work day. Check with your electric company to see if this program is available and would be of benefit to your family.

Reducing Your Bill by Changing the Billing Patterns

Level Payment Plans. If you are able to pay your *average* utility bill without a problem, but have difficulty meeting the high level months (the coldest months of winter for heating bills and the hottest months of summer for electric bills), try a level payment plan. A level payment plan allows you to average your expected bills so that you pay the same amount each month. Your projected yearly bill is divided into equal monthly installments; monthly bills reflect this amount rather than each month's actual use. For example, a customer whose total gas bill for a year is $1200, would pay $100 each month instead of $200 to $300 a month in the winter, and $30 to $40 a month in the summer. At some point during the year, the average bill and the actual usage are reconciled. Many states require their regulated utilities to provide these plans.

Dealing with Quarterly or Bi-Monthly Bills. If you find it difficult to deal with quarterly or bi-monthly bills, particularly when they represent a significant portion of your monthly income, contact your local utility company. Explain the difficulty and see if they will bill you on a monthly basis. In the alternative, ask them to accept monthly payments from you, even if they won't send you a separate bill each month. If you make this choice, ask about "service charges" or "finance charges." This is the cost of paying over time. If the cost is too high, this type of payment plan is a bad idea.

Avoiding Late Payment Charges by Changing the Date Your Bill Is Due. If you receive your main source of income on the 5th of the month, but your utility bill is due on the 4th, obviously it is difficult to pay your utility bill on time. Thus not only do you have the high utility bill to contend with, but you also have late charges added to your bill. Generally, utility companies will help you deal with this, if you explain the situation. Although they may insist that you pay the late charges that have already been billed to your account, they should agree to change the date your bill is due each month so that late charges don't keep accruing. By avoiding the late charges, you may reduce your bill by $5 to $15 each month.

Reducing Your Bill by Reducing Usage of Utility Service

Utility Sponsored Weatherization or Conservation Programs. Many utilities have programs that provide free, or low cost weatherization or conservation services. The programs have varying eligibility requirements. Some are limited to the elderly, or homes with disabled persons and/or children; some are based on the household's income or eligibility for a government programs such as Energy Assistance or the Weatherization Assistance Program; some are available to all households.

These programs run the gamut. In the best programs, the utility sends someone into your home who conducts a full energy audit and provides extensive weatherization services. Other programs simply provide hints on how you can reduce usage, or they supply conservation products such as special energy efficient light bulbs, insulating hot water tanks, and "low flow" efficient faucets, or other conservation products. Even the less ambitious programs which provide only some conservation advice should be helpful to you. Investigate by calling your local energy and water providers and finding out what programs they have available.

You should be very cautious before investing more than a few dollars in any weatherization or conservation efforts with a contractor, however. While it might make sense in the long run for households with extra cash, it is often not the wisest use of funds for households which are strapped to pay for necessities.

Government Sponsored Weatherization Programs. Several programs are designed to provide weatherization assistance for owner-occupied housing as well as rental units. The primary program

is the Weatherization Assistance Program. Households that qualify generally receive over $1000 in actual weatherization benefits which are provided at no cost to the beneficiaries. Although there may be a long waiting list, it is worthwhile looking into these programs. Additionally, many states have state weatherization programs. Cities also have Community Development Block Grant money which is often used to help low-income households weatherize their homes.

Self-Help Weatherization. If you are unable to find or qualify for any of programs through your utility or the government, there are still a number of practices which you can employ which may help reduce your usage. (Note, these procedures are unlikely to reduce your bills significantly, but even a 3 or 5So reduction means some added dollars for you.) Some examples include:

- Check for leaks of air or water. If you are a tenant, try to get the landlord to fix these leaks. If you own your own home, and it is possible, try a number of homespun fix ups. For example, for air leaks around windows use tape. For leaks around doors, leave a rolled up towel next to the bottom of the door. If necessary to stop leaks around the top and sides of doors, tack up a blanket or large towel. You will be surprised how much warmer a house or apartment can be without the heat loss from cracks between openings and walls. As the home warms up, you can consider turning down the heat.
- Remember that your sewer bill is generally determined by how much water you consume. So that by saving water you are saving twice. Putting a brick in your toilet tank may seem silly, but it will actually cut down on the amount of water consumed each time you flush.
- Turn off lights and heat or cooling when not at home. Also close the door for any rooms you are not using, and don't try to heat or cool them.

Your Rights When Faced with Possible Termination of Utility Service

The threat of immediate termination of utility service, as well as the need to restore service that has already been terminated, are the two most urgent problems faced by utility customers. In most states there are laws which
provide a variety of significant protections when utility companies threaten termination of service. Many of the larger utilities are regulated by commissions called public utility commissions, or public service commissions. The protections provided by these commissions generally include substantial requirements which must be followed before the utility can shut off your service. A **utility company's failure to comply with these requirements will generally make the termination illegal**—which means you should be able to stop the termination for no other reason than the utility has failed to follow the rules. These rules generally have the following basic requirements:

Notice. Prior to termination, a utility customer must be given notice a) that the service is subject to termination, and b) of the various rights that the customer has to prevent termination. Often this requirement includes a repeat written notice. Face-to-face notice may also be required in certain parts of the country.

Limit on Circumstances Warranting Termination. Regulations typically permit disconnection for nonpayment, but often prohibit disconnections for very small amounts, or which have been owed for less than a certain number of months. Further, if you dispute that you owe the bill which the utility says must be paid, the utility is generally prohibited from terminating service over a disputed bill. If you dispute that you owe part of the bill, you must pay the undisputed amount to preserve your rights.

Right To A Hearing. Before or after termination, you have a right to appeal to both the utility and to an independent third party such as the Public Utility Commission. In many states, informal appeals can be made by telephone prior to termination and often utility service will be maintained or reconnected during the appeals process.

A utility commission's consumer division responds to phone calls, letters, and visits by residential customers. Many of these complaints are resolved informally, by consultation between the consumer division and the utility. Consumer divisions also hold hearings on complaints that cannot be resolved informally. In large states, several hundred of these hearings are held each year.

Consumers generally have a legal right to a hearing whenever they have grounds to contest a utility termination. Simply request the utility commission to provide a hearing before service is terminated. (If you dispute only part of a back bill, you will usually have to pay the undisputed part to keep your service on while the dispute is being decided). While city owned utilities are generally not regulated by the utility commission, customers of municipal utilities have a constitutional right to a hearing before termination.

Consumers need not retain the services of a lawyer to represent them at the hearing. However, it may be helpful to have a paralegal or experienced utility counselor assist with the hearing. To support

the claim, it is important for consumers to bring all relevant documentary evidence, such as a physician's affidavit or past bills. It may also be helpful to have witnesses such as friends and neighbors present.

Right to A Deferred Payment Plan. Before utility service is cut off, most states require that a customer must be informed about the option to pay all overdue bills over a period of some months through a reasonable installment plan. Often this payment plan has a six month or a one year limit for bringing the account up-to-date. To make a successful payment plan, the customer must develop a simple budget that the household can reasonably meet, and should be assertive with the utility company employee who negotiates the agreement. Payment plans need not be level. For example, seasonal workers may want to pay less toward arrears in the winter and more in the summer.

The utility company may want a payment plan that requires larger payments than you can afford. However, unrealistic plans harm both you and the utility company in the long run. You may not be able to make the payments, and may lose the service, and the company does not collect its debt. In some states, utilities are not required to enter into a second payment plan with consumers who have defaulted on a first payment plan. It is better to explain your financial circumstances and push for an affordable agreement from the beginning.

Winter Moratorium on Terminations. In most northern states there is a total prohibition on termination of heat related utilities between November 1 and March 31st to residential consumers. In other states, there is usually a limited moratorium to prevent utility terminations for households with elderly or disabled residents, and occasionally for households with infants. Generally, financial hardship must be shown. Some of these rules require that before a household be considered for the moratorium, all efforts to obtain state energy assistance must have been pursued. It is important to note that a moratorium only prevents disconnection of service. Your bill will still be charged and you will be responsible to pay for service used during the moratorium period. For this reason you should pay, if you can, even if your service is not subject to being disconnected.

No Termination If There Is Serious Illness. Similarly, state law or public utility commission regulations often restrict termination of service for households whose members face a serious illness, are threatened with serious illness, or depend upon life support systems. Often, the illness must be certified by a doctor. A family with very young children may also be able to use the health risk to the children as grounds to stop utility termination.

Information about Sources of Assistance. Utility companies often must provide consumers with information about the existence of energy assistance programs, such as LIHEAP or local crisis intervention programs. (Places to go for assistance in paying your utility bills are listed later in this handout.)

Protections for Tenants from Termination of Service By Landlords. If your landlord is responsible for paying utilities and is delinquent, you risk losing your utility service. In some states, tenants must receive a special shut-off notice if the landlord is delinquent. Then, tenants make utility payments directly to the utility, and deduct those payments from their rent.

It is illegal in almost every state for a landlord to cut off your utility service as a way of making you move. Landlords must go through the courts to evict tenants; they cannot make the place uninhabitable by terminating the heat or water service so that the tenant moves. Generally, a tenant not only can stop a "self-help" eviction when the landlord tries this, but also the tenant is entitled to recover damages for the landlord's wrongful actions.

No Termination of Local Telephone Service for Bills for other Services. Some states prohibit the local telephone company from terminating your service for nonpayment of long distance service, but the majority of states do not yet have these protections. Also, every local telephone company is prohibited from terminating your local telephone service for nonpayment of 900 calls or "audio text" services.

A Moratorium Linked to a Plant Closing. A utility or utility commission may impose a temporary prohibition against termination of utility service for customers or neighborhoods particularly hard hit by a recent plant closing. If such a moratorium is not in effect, it may be possible for a counselor for families affected by a plant closing to negotiate one. The moratorium only prevents the utility company from terminating service if bills incurred during the moratorium period are not paid. When the moratorium period expires, the utility can then start the termination process for amounts not paid during the moratorium or owed before the moratorium. Most utilities encourage their customers to pay what they can afford during a moratorium.

The Utility Does Not Follow Required Termination Procedures. The utility's failure to follow the termination rules typically provides grounds to demand that the termination process start all over, and utility service must be maintained throughout the process. Wrongful termination of utility service generally will give the customer a claim for damages. An attorney can often get a

special court order (an injunction) to stop termination or to have service restored when the utility has failed to follow the rules on termination procedures. You should not hesitate to contact a local legal services attorney or the consumer services division of the state public utilities commission to find out whether the utility has complied with the rules on termination.

Public Utility Commissions generally have dispute resolution authority, and a call to the appropriate person can often stall or prevent a termination altogether.

Bankruptcy Protections. The filing of a bankruptcy petition automatically requires the utility to restore service or stop a threatened termination. The bankruptcy filing starts a twenty day period during which you are entitled to service from all applicable utilities. The utility can only terminate service after that twenty day period if you fail to pay bills arising after the bankruptcy is filed, even if you never pay another penny on past due arrears. The utility, though, can also require that you provide adequate assurance that future bills will be paid, such as providing a new security deposit. Bankruptcy can be complicated. Professional advice is a good idea.

Sources of Assistance for Payment of Your Utility Bills

If you have a low income and high utility bills, you are probably eligible for some assistance with your utility bills. All programs have eligibility requirements, but they differ considerably in their specific terms.

Federal Energy Assistance. The Federal Low Income Home Energy Assistance Program (LIHEAP), which is run by the states, helps low-income families pay their utility bills. Most states provide this assistance for winter heating bills; although some states also use LIHEAP funds to assist families with summer cooling expenses. LIHEAP benefits can even go to some renters and public and subsidized housing tenants, with the energy assistance payments going directly to the landlord's fuel supplier and the amount being credited against the family's rent.

Most states require that family income over the past three or twelve months he below 150 % of the federal poverty guidelines. The size of a family's LIHEAP ben**efits generally depends** on the family's income, the number of household members, and may also depend on housing type, fuel type, fuel prices, weather conditions, **or actual** energy consumption.

To apply for LIHEAP benefits, you should contact the **local agency** in the community administering the program. This is usually a nonprofit agency, such as the local community action program (CAP), or a county department of social services office.

- **Emergency Assistance.** If you need immediate assistance paying a utility bill to prevent termination, the following sources should be pursued:
- **LIHEAP Crisis Assistance.** Contact your local CAP agency (community action program) or the county department of social services to find out who provides these funds in your area.
- **AFDC Emergency Assistance.** If you have children and you are about to lose essential utility services (water, heat in the winter months, etc.) contact your county department of social services to see if special emergency funds are available to help you.
- **State Emergency Assistance.** Some states have special funds to help prevent utility terminations. Also many counties have "homeless prevention" funds which can be used to prevent utility terminations. Contact your local CAP agency or the county department of social services.
- **Utility Fuel Funds.** Many utilities collect money from their customers or their shareholders to go into a special fund to help people pay their utility bills. Contact the utility which is threatening to shut off the service to see if they have a fund which might be of some assistance to you. You should not assume that because they haven't told you about it that they don't have such a fund, or that you are not eligible.
- **Salvation Army, Local Churches.** The Salvation Army and other local religious and charitable organizations often have money that is available to help needy people in the community with emergency bills such as utilities. Check around, ask the utility company, the public utility commission, or the department of social services. Some churches that have these funds do not limit them to their own members

Ways to Get Your Utility Service Turned Back On

Everyone has the right to receive utility service from the provider in their area. Establishing new service after a move or after previous service has been terminated can be difficult and expensive. However, there are a number of things you can try to reduce the amount of money you have to come up with to establish new utility service. Utilities are

prohibited against discriminating in service, and are required to establish *reasonable* rules for customers to follow.

Dealing With an Old Bill. If the bill is *very* old, such as more than three or four years, it is possible that the utility can not legally require you to pay it before providing you with new service. Check with a local attorney if you have a very old bill.

The best method to deal with old bills which must be paid may be to request the utility to allow you to pay the old bill off in installments over a period of six to twelve months or longer. So long as you maintain your payments on the new service you will be receiving, there is no reason for the utility to refuse to provide you service under this arrangement. If you are ready and willing to pay for future service as it is provided, and to pay for the old service, over time the utility does not have reasonable grounds to deny you this new service.

Late Charges. Generally a utility will charge late fees for paying a utility bill after it is due. There should be specific rules on how much these late charges are, and state law and regulations generally limit the late charges to reasonable amounts.

If the late charges are so high as to be unreasonable, try contacting the consumer services division of your state public utility commission to challenge the amount. Otherwise, try to negotiate with the local utility about the amount. If you lost your job, went through a separation or divorce, or suffered an illness in the family which caused you to be late on your payments before, you can show that this was a temporary difficulty which has now passed. Bargain with the utility; especially if you had a good reason for missing payments.

Reconnection Fee. This is a fee which may be imposed on a household after it has its service terminated for nonpayment. The purpose of this fee is similar to late charges. Try the same type of arguments and negotiation.

Deposits. Before establishing new or renewed service, many utility companies ask households with poor payment histories to pay a deposit, usually equal to an average monthly bill. Utilities are prohibited from discriminating against certain types of customers in setting the deposit requirements. Customers who believe that a deposit is being requested unreasonably, or that a requested deposit is too large, should not hesitate to complain to the public utility commission's consumer division.

If you cannot afford the deposit, some of the sources of assistance listed earlier may help pay deposits. Later, when you have established a good payment record, or when you decide to terminate service, request that the utility return the deposit, with interest. This should always happen if you did not fall behind again after the deposit was made.

Instead of a deposit, some utilities accept the signature of a cosigner or guarantor, who agrees to be responsible for payments you fail to make.

Failure to Pay Prior Bills as Grounds for Denying Service. Utility companies often require customers to pay outstanding bills from a previous address before connecting service at a new address. Check with a local legal services attorney or the public service commission to see if it is legal in your state for a utility to do this. If you must pay the bill from the previous address to obtain new service, you should be able to pay for the old service under an installment agreement.

It is generally prohibited for a utility to insist upon one customer's payment of another customer's bill. For example, you are not obligated to pay the delinquent bills of the prior tenant of your new residence, or bills that your old landlord was obligated to pay. Similarly, you may not have to pay an old bill where the old service was in someone else's name (for example, an old roommate or former spouse), or where service is now in your name, and one of your current roommates has an old delinquent bill.

When you are obligated to pay an old bill before service will be connected, one option is to file for bankruptcy. The old obligation will likely be discharged in the bankruptcy. The utility will have to provide new service as long as you provide a reasonable assurance, such as a deposit, of the ability to make *future* payment. The filing of the bankruptcy will immediately entitle you to service at the new address.

Failure to Provide Information as Grounds for Denying Service. Sometimes companies refuse to hook up service because you have not provided requested forms of identification or proof of residence. The company will use this information for various reasons, including to make sure that you do not owe money for service received at a previous address. This is generally not an unreasonable request unless the company carries it to extremes, such as demanding a birth certificate, or information about all previous residences.

Avoiding Utility Company Restrictions on New Service. When you cannot pay a prior bill with the utility or afford the security deposit, there are still ways to obtain utility service. Look for a house or apartment that includes utilities in the rent. Another option is to establish utility service in the name of someone else with a good payment history. However, since that individual becomes responsible for any unpaid bills, this approach must be

considered carefully, with full disclosure of the risks to the individual assuming responsibility for the bills.

Special Telephone Link Up Program. In most states, households in financial distress can obtain steep discounts on new service installation charges under the link-up program run by the local phone company. You may also be eligible for a significant discount on telephone monthly charges under the "Lifeline" program. Contact the public utility commission or telephone company for details.

Adapted from National Consumer Law Center, *Surviving Debt* (2d ed. 1996), available from: NCLC, 18 Tremont Street, Boston, MA 02108

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ATTACHMENT A

Schweinfurt Law Center
Legal Assistance Information

German Landlord-Tenant Law

Please note that this Information Paper only provides basic information and is not intended to serve as a substitute for personal consultations with a Legal Assistance Attorney. For an appointment dial (DSN) 353 - 8505/ 8384 or (CIV) 09721 - 96 - 8505/ 8384.

I. INTRODUCTION

a. Effective September 1, 2001 tremendous changes have taken place in the area of the German Landlord-Tenant Law. Tenants living on the economy will be faced with rental agreements subject to German law and, therefore, they should know some of the basic German rules that govern the landlord-tenant relationship. Furthermore, the legislator modernized the German Civil Code ("Bürgerliches Gesetzbuch" – BGB), effective as of January 1, 2002.

b. Tenants, looking for private rentals, should seek assistance from the Housing Referral Office (HRO). Furthermore, they need to familiarize themselves with the area to consider their individual needs. For example, for tenants with children, it may be good to know where the School Bus Transportation routes are.

c. The HRO keeps lists of landlords that frequently caused trouble or proved to be unreliable landlords in the past and it informs the tenant about possible allowances, *e.g.*, Moving in Housing Allowances (MIHA). Furthermore, the HRO might be able to convince the landlord to use the official HRO rental agreement or at least talk to the landlord about possible modifications in the light of the tenant's special situation. One of the primary aims is to make a PCS termination clause part of the agreement.

II. THE RENTAL AGREEMENT

A. Sources of Law

a. Generally the landlord presents a preprinted, standard rental agreement to the tenant. An exception applies where the USAREUR HRO rental agreement is used. However, any contract not individually negotiated but presented in a preprinted form will be scrutinized by the rules governing the general terms and conditions of trade ("Allgemeine Geschäftsbedingungen" - AGB) as codified in § 305 - § 310 BGB. In a preprinted, standard rental agreement any inconsistencies or ambiguities are construed against the party that presented the preprinted contract and are settled in the other party's favor (§ 305c para. 2 BGB).

b. Basically the parties are free to define their relationship by whatever they agree upon. The courts will uphold their agreement. If the parties fail to address a specific aspect of their rental relationship, the provisions provided for in the applicable law will be applied. The legislator has passed legislation to ensure a minimum of arm's length negotiations and fair dealings as well as to balance the bargaining positions of the parties. Those provisions are mandatory and, therefore, have to be obeyed by all parties. Any clauses to the contrary are voided by law. The provisions provided for in the applicable law will supersede those clauses.

c. § 535 BGB contains a simple statement, making it clear that only temporary usage in consideration for some compensation, *e.g.*, monetary one or services performed, is considered to be a lease under German law. § 535 BGB reads as follows: "CONTENTS AND CONTRACTUAL MAIN OBLIGATIONS OF THE RENTAL AGREEMENT. (1) By the lease contract the landlord shall be obligated to grant usage of the leased object during the term of the lease to the tenant. The landlord shall turn over the leased object in suitable condition for the contracted usage to the tenant and shall keep it in such condition during the lease. He shall be obligated to bear the encumbrances on the leased object. (2) The tenant is obligated to pay the agreed upon rent to the landlord."

d. The German rental law provisions in the BGB are contained in the §§ 535 - 580a BGB. They also set forth guidelines for rent increases. However, utilities and operating costs are addressed in the II.BV ("Zweite Berechnungsverordnung" - Second Computation Ordinance).

B. Types of Contract

1. Fixed Term Lease

a. German rental law distinguishes two types of contracts: fixed term lease contracts and indefinite term lease contracts.

b. A fixed term lease contract should be avoided. It only runs for a specific fixed-term and cannot be terminated by the tenant (but by the landlord for a reason) during the fixed-term. Generally it allows the landlord to easily evict the tenant once the contract runs out. It does not serve the U.S. Forces personnel's interests. Despite an unexpected early PCS move or an order to move into government housing, the soldier will not be able to get out-of the contract but remain responsible for his/her obligations under the contract.

c. A fixed term lease can become an indefinite term lease by operation of law if the Landlord lets the tenant stay on after the fixed-term is up or if the Landlord fails to provide upfront in writing a reason why there is a fixed-term (§ 575 BGB). Only one of the following three reasons can justify a fixed-term: (i) personal need, (ii) planed major renovation and improvements, (iii) to be leased to an employee

2. Indefinite Term Lease

The indefinite term lease constitutes the most common residential lease type in Germany. If no specific mention is made, the contract runs for an indefinite period of time, *i.e.*, until one party terminates it.

III. FORMATION

1. Meeting of the Minds

a. In order to form a contract, there must be a meeting of the minds. A lease is concluded, when the parties agree upon the following essential parts:

- leased object (size & accessories)
- purpose of the lease (residential or business)
- duration of the lease (fixed-term or indefinite)
- consideration. It is sufficient if the parties agree on monetary compensation as consideration. It is not necessary to agree to a specific amount. In such a case the amount will be determined in accordance with the applicable laws.

2. Form

a. Oral rental agreements are valid and fully enforceable. Only a fixed-term lease in excess of 1 year must be in writing (§ 550 BGB). But even if that requirement is violated, it will not invalid the oral agreement. Instead the lease will be considered to be merely for an indefinite term.

b. Generally speaking a written agreement is preferable. Oral stipulations may be forgotten, denied or remembered differently by the other party. Only a written agreement enables the parties to adequately prove the terms of the agreement and to clarify each other's obligations thereunder. All terms should be reduced to writing and have to be personally signed by the parties or their duly authorized representatives. Where more than one party lives in the house, rules of the house ("Hausordnung") are incorporated into the rental agreement by reference. These create further obligations.

c. Yet, there are also advantages to an oral agreement because those are usually very short. The landlord does not subject the tenant to all the detailed conditions usually contained in a written agreement. The tenant's obligations are less burdensome. Furthermore, the codified rental law provisions apply, which are otherwise often modified in a written agreement to the landlord's favor, whenever the landlord presents the standard preprinted contract form.

3. Parties to a Rental Agreement

a. Privity of contract exists only between the contracting parties. Nevertheless, a tenant is generally free to have his/her friend, fiancé(e) or spouse move in without the landlord's consent. Such a person is not a party to the rental agreement and, therefore, will not assume the rent obligation, unless the person becomes a contracting party as well. The landlord owes the contractual duties only to the contracting party and that party remains liable for the rent - until a termination becomes effective - even if that party moves out and his/her partner remains in the premises.

b. The moving-in party acquires an inherent possessory and usage right in respect to the apartment. The landlord owes an obligation to protect all members of a household against injuries. However, this obligation does not apply to mere visitors. Yet, the tenant can have visitors of both sexes without nighttime limitations. Furthermore, he/she may have visitors stay as long as 2 months. Up to that time, it would not be considered a sublease, which by contrast, would require approval by a landlord (§ 540 BGB).

c. Where two tenants enter in a rental agreement with the landlord, both are also jointly and severally responsible for the performance of the contractual duties. Without a power of attorney no spouse can execute a rental agreement on behalf of the other spouse. However, a rental agreement usually contains a clause empowering one spouse to act on behalf of the other spouse, *e.g.*, to receive correspondence. The landlord normally favors to have both spouses sign the agreement so the landlord gets two debtors and avoids any problem with respect to the landlord's lien.

d. If one of the co-tenants intends to move out, that tenant should obtain a rent release from the landlord. The remaining co-tenant has to agree (impliedly or expressly) to it as well, otherwise the other tenant can exercise a termination right.

e. According to § 18 HausratVO a judge may award as part of an upcoming or pending divorce procedure one spouse's property to the other spouse upon request by one spouse. Where there are children, the family home will normally be awarded to the custodial parent in case of a separation or pending divorce.

IV. OPERATIONAL ISSUES

A. Financial Obligations

a. A thorough study of the rental agreement is essential. The prospective tenant should not rush into the contract but consider his/her financial situation as well to see whether the desperately desired apartment is affordable. Once the rental agreement comes into effect, there are substantial costs involved. On the one hand there is a financial commitment, while on the other hand it may take a while before all the allowances go into effect to help the tenant pay for those costs.

- the rent as well as the utilities and operating costs have to be paid on a monthly basis
- the security deposit have to be paid during the first three months
- telephone set up fees

b. The rent is due in advance no later than the third working day of the month (§ 556b BGB). By definition Sundays and official German holidays are no working days (§ 193 BGB). For the purpose of rent payments, Saturdays are not considered working days neither because all banks are closed on Saturdays. The term "on the landlord's account" means that the money must be posted at the landlord's bank, not the German Post Office. The burden of proof is fully on the tenant to show he/she paid the rent on time.

c. Provided the tenant informed the landlord in writing one month in advance, he/she can set off any claim for damages against the rent due. If the landlord files for bankruptcy, the rent has to be paid to the administrator of the landlord's assets upon proper notification of the bankruptcy procedure.

d. According to Art. 60 para. 5b SA, members with SOFA status are exempted from radio and television usage fees, collected by the GEZ ("Gebühreneinzugszentrale"- Central Fee Collection Agency). Furthermore, according to Art. 6 para. 1 SA, they are also exempt from German regulations in the field of registration of residence (“Meldewesen“) and aliens control (“Ausländerpolizei“), except with respect to registration in hotels and similar establishments (“Beherbergungsstätten“)

1. Utilities and Operating Costs

a. The tenant will have to pay only for those utilities and operating costs mentioned in the rental agreement. However, the landlord may put a clause in the agreement referring to § 27 II BV (§ 556 para. 1BGB). § 27 II BV is an umbrella provision that lists exclusively all applicable utilities and operational costs in six categories:

- public charges and fees (*e.g.*, costs for water, sewage, garbage, electricity, rainwater, street cleaning and real estate taxes)
- heating and hot water costs (*e.g.*, costs involving emission checks, service fees)
- cleaning costs (*e.g.*, chimney sweeping, bugs, floor)
- costs for common area lights
- insurance premiums (*e.g.*, property and liability insurance)
- miscellaneous fees (*e.g.*, costs for gardening, common antenna)

b. Tax relief is generally not available on utility bills. Individuals are not entitled to tax relief in their own name. According to Art. 67, 68 SA only an agent of the U.S. Forces can make tax-free purchases, *e.g.*, Moral Welfare Recreation Funds (MWRF).

c. Utilities are just advance payments. Consequently, they are only estimates of how much it will cost. The landlord rarely agrees to a fixed amount. However, the landlord will have to present to the tenant a detailed list of the overall actual utility costs, unless the parties agreed on a fixed amount. Such a list has to be presented within 12 months following the (annual) billing cycle, otherwise the landlord is prevented from asking for additional amounts to cover the actual annual utility and operational costs (§ 556 para. 3 BGB). Likewise the tenant has 12 months, following the receipt of the landlord’s list on utility and operational costs to present any objections he/she might have or else be loose the right to protest.

d. Depending on whether there is a plus or an amount still owed on the annual utilities and operational cost bill, the tenant will either have to pay the rest of the amount owed or be entitled to a reimbursement of any surplus. Based on the utility and operational costs for the past billing cycle, both parties can demand a modification of the advance payments. If there had been a surplus, the landlord may demand smaller monthly advance payments, while the landlord can demand higher monthly advance payments if there had been a debt.

e. A detailed list of the overall actual utility costs will also have to provide information concerning the exact manner in which those costs are split between the tenants actual calculations, and credit for the tenant's advance payments. The landlord can base the apportioned share of the overall costs on actual consumption or the size of the apartment. It can only be based on the number of persons living in the apartment if specifically agreed thereon. In some instances there are also special regulations the landlord has to adhere to, *e.g.*, the HeizKVO ("Heizkostenverordnung" - Regulation Concerning the Computation of Heating and Hot Water Costs) requires that at least 50%, up to a maximum of 70%, of the total heating costs are computed on the basis of measured consumption. Watch out for clauses in the lease authorizing the landlord to choose a calculation method.

d. Example: Three tenants live in an apartment house with a total floor space of 300 square meters, every apartment having the same size (100 sq. meters). The measured heat consumption in the apartment is: 80 units for tenant A, 95 units for tenant B, and 105 units for tenant C. The heating costs for the year are € 5,000 and the landlord calls for the maximum of 70% of measured consumption.

Basic heating cost portion:
30% of € 5,000 = € 1,500
€ 1,500 : 300 (sq. meters) = 5 €/sq. meter
5 €/sq. meter x 100 (sq. meters) = € 500

measured consumption portion of the heating costs:
70% of € 5,000 = € 3,500
€ 3.500 : 280 (units) = 12.50 €/unit
12.50 €/unit x 80 units (for tenant A) = € 1,000

annual heating bill for tenant A in this case = € 1,500
(€ 1,500 : 12 (months) = € 125 would have been a good monthly utility advance payment for the heating costs in tenant's A case)

e. A fixed flat rate for utility costs might be preferable to the tenant, if he/she is not used to the high German energy costs and the fresh water preserving approach. On the other hand, if the tenant already knows he/she will be absent from home most of the time a flat rate is less advisable, *e.g.*, deployed single soldier. Watch out for clauses in the lease reserving the right to increase the “fixed” flat rate.

2. Rental Security Deposits

a. By German law, landlords may ask for a deposit not to exceed three-month rent (§ 551 BGB). However, the tenant has the right to make the rental security deposit payments over a three-month period. If the landlord and the tenant agree, the tenant may instead of paying the rental security deposit into an account, present a bank guarantee to the landlord. A good compromise is usually to put the security deposit in a joint savings account which can only be touched with both the landlord's and the tenant's consent.

b. Anyway, the landlord has to keep the rental security deposit apart from his/her other assets in an interest accruing way. The interest drawn by the deposit accrues to the tenant annually and increases the rental security deposit. The landlord is not allowed to subtract any amount for expenses he/she incurs.

c. A higher deposit may be charged if the tenant needs to make constructional changes to the apartment to make it fit for a handicapped person (§ 554a BGB). However, the tenant has to restore the original condition of the apartment once he/she moves out.

d. Unless the landlord agrees, the tenant shall not set off the rental security deposit against any rent payments due. An exception may apply in case of the landlord's bankruptcy. By contrast, the landlord may use the rental security deposit if the tenant defaults on his/her rent. Thereafter, the tenant has to settle the rental security account, again.

e. A tenant is entitled to a return of the deposit only after the premises have been turned back to the landlord. However, the landlord has been afforded a reasonable period of time - usually up to 6 months - to examine possible claims against the tenant. The moving out protocol should help to speed up this process.

f. If the premises have been sold, the new owner/landlord has to pay back the rental security deposit to the tenant, even if the former owner/landlord did not transfer it to him/her (§ 566a BGB). In any case, the former owner remains liable as a secondary debtor if the tenant cannot obtain the rental security deposit from the new owner/landlord because the obligation to repay that money does not run with the land but is primarily considered a personal indebtedness between the original contracting parties. Watch out for any clauses in the agreement trying to limit the former owner’s responsibility on the return of the rental deposit.

3. Decorative Repairs

a. The German term for decorative repairs is "Schönheitsreparaturen". Decorative repairs include any kind of painting and redecoration within the apartment. In absent of an agreement to the contrary, the tenant is not responsible for the decorative repairs. It is the landlord's obligation to maintain the premises in an appropriate condition. However, most landlords insist to have a clause put into the rental agreement that stipulates that the tenant must carry out decorative repairs during the lease term.

b. For non-smokers decorative repairs in the house usually become necessary every 3 years with regard to the kitchen and bathrooms and every 5 to 7 years with regard to all other rooms. There sometimes also exist renovation clauses and there are a lot of judgments around dealing with the single issue how such a clause needs to be phrased in order to be upheld in court of law.

4. Rent Increases

a. A request for a rent increase has to be transmitted in a letter or via fax, email, SMS or the like ("Textform"). It may be based on one of the following aspects:

- after improvements to the living quarters, e.g. renovation or energy conservation measures (§§ 559, 559b BGB). The annual assessment is limited to 11% of the overall costs.
- when operating expenses have increased (§ 560 BGB),
- where the parties have agreed on a staggered rent or an index rent in the first place (§§ 557a, 557b BGB), or
- to correspond to compensation for comparable living quarters (§§ 558 ff BGB), if:

(1) the rent a tenant has been paying is unchanged for at least 15 months
(2) the combined rent increase for a 3 year period must not exceed 20% (global rent increase limit) and
(3) the rent does not exceed the customary rents negotiated for an apartment of comparable type, size, furnishings, quality and location during the preceding 4 years in the community or in comparable communities for living space not subject to price control
    (i) rent survey, § 558c BGB or qualified rent survey, § 558d BGB. The later one must always be mentioned if it exists even if it is not used to justify the rent increase
    (ii) rent data base, § 558e BGB
    (iii) appraiser report, § 558a BGB
    (iv) naming three comparable apartments
(4) Please note, any rent increases based on § 559 - § 560 BGB will not be taken into consideration when determining a rent increase IAW § 558 BGB.

b. A qualified rent survey ("qualifizierter Mietspiegel") is prepared IAW recognized scientific rules and principles and has been recognized either by the county or by representatives of landlord and tenants organizations. It is presumed to contain the customary rents and shall be updated every two years. However, the communities and counties are under no obligation to prepare a qualified rent survey.

c. Exorbitant rents are rents that exceed the "average market rent", *i.e.*, the customary charges paid in the community or in comparable communities for the residential lease of rooms of comparable kind, size, facilities, conditions and location. An excess of approximately 20% or more, subject the landlord to criminal prosecution based on either § 5 WiStG ("Wirtschaftsstrafgesetz" - Economic Offenses Act) or in more severe cases, like an excess of more than 50%, on the usury provision § 291 StGB ("Strafgesetzbuch" - Criminal Code). Given these circumstances, the tenant has a claim for unjust enrichment (§ 812 BGB) against the landlord, limited to the actual overpayment of more than 20% with respect to the "average market rent".

d. The rent may, however, not be increased where the parties entered into a fixed term rental agreement, unless that right is expressly reserved in the agreement (§ 557 BGB).

e. The landlord is not allowed to terminate the rental agreement in order to increase the rent (§ 573 BGB). Instead the tenant has to expressly agree to the increase (§ 558b BGB). The tenant has until the end of the second month following the month in which he/she received the demand for a rent increase, to consent to the increase. There is no implied consent if the tenant does not respond to the landlord's request for a rent increase. After the deadline for consent has run out, the landlord has 3 months during which he/she can initiate an action for consent (§ 558b BGB). That issue will be settled in court then.

f. Where a landlord's agent submits a demand for rent increase and fails to submit an original power of attorney, the tenant can immediately and for this reason reject the demand (§ 174 BGB); but this protest has to be made expressly and at once.

g. Example: The landlord sends a demand for a rent increase. If the demand for the rent increase is received on June 2nd, the tenant may consider the demand until August 31st. Upon lack of expressed consent, the landlord has until November 30th to bring a lawsuit against the tenant on this issue.

B. Disturbances

1. Landlord's Entry Right

a. The landlord has the right to inspect the apartment leased to the tenant but only if he/she gives reasonable advance notice of his/her wish and obtains prior approval from the tenant.

b. Only in emergency cases, the landlord may enter forcibly without permission. The landlord shall not retain a key to the apartment, unless the rental agreement states differently.

2. Rent Reductions

a. A landlord is responsible for maintenance, and for performing necessary repairs to assure that the premises meet minimum standards. In residential leases it is implied the landlord will maintain the premises fit for human habitability and will repair any condition that is dangerous or detrimental to safety or health. It is the principal duty of a landlord to maintain an apartment, including fixtures and common areas, in the condition specified in the rental agreement. If a landlord fails to do so and if the failure reduces the utility of the premises or detracts from it, the tenant may be authorized to reduce the rent (§ 536 BGB).

b. The amount of reduction depends on how much the defect destroys or diminishes the leased thing's fitness for the stipulated use. In a residential lease, the decisive factor is if and how far the habitability is affected by the defect. A rent reduction is not justified where

- only minor defects exist
- the tenant's behavior contributed to the defect
- the tenant lives with the defect without complaining about it (forfeiture)
- the leased thing is, at the time of handing over to the tenant, affected with a defect, known to the tenant, unless the landlord had promised to cure that defect (§ 536b BGB)

c. The tenant must report any defects to the landlord right away or else he/she will not only loose all his/her rights to seek damages or reimbursement but be subject to a claim for damagers himself/herself if the defect became worse (§ 536e BGB). If the tenant knows or should have known about the defects before he/she signed the lease, the tenant is prevented from exercising any remedial rights against the landlord (§ 536b BGB).

d. If the tenant knows about a defect, he/she should reserve his/her remedial rights when signing the contract by listing the defects and the remedial acts that need to be taken. It will be almost impossible for the tenant to receive any money back if he had the right to reduce the rent but it not make use of it (§ 814 BGB). However, if the defect still exists, he can exercise his remedial rights at any time (with respect to the future).

e. The tenant has the burden of proof to show the defect exists. Through the HRO an expert may be retained to investigate the alleged defect. The costs for the expert report can be set off against the rent due, if the report confirms the defects.

f. A rent reduction is only possible while and as long as the defect still exists. Yet, it is very difficult to properly assess the amount of rent reduction and an unjustified rent reduction may expose the tenant to an eviction! The following are some examples of defects triggering rent reductions and the percentage that the rent may be reduced:

- no heat during 4 months of the winter: 100%. The heating period usually runs from October through April.
- no hot water during two-thirds of a month: 25%
- no hot water: 10%
- unusable storage room in the cellar: 10%

g. If the landlord fails to cure the defect for which he/she is responsible, the tenant can:

- sue the landlord to compel him/her to perform the repair,
- do the repair and sue the landlord for the expense of the repair (§ 536a BGB), or
- contract to have the repair done and take the cost out-of the monthly rent, provided the tenant had given the landlord at least a month's advance notification

h. Where mold exists the air is either too moist due to the fact that the tenant does not ventilate enough fresh air or the walls are too cold because the constructor deviated from construction regulations. Frequently, the landlord and the tenant argue about the cause and most of the time both reasons contributed to it.

Example:	contracted rent	reduced rent
net rent	€ 450	€ 324 (20% of € 630 = € 126)
utilities advance payments	€ 180	€ 180
Gross rent	€ 630	
reduced amount (20%)	- € 126	
	€ 504	€ 504

	contracted rent	reduced rent
net rent	€ 450	€ --- (80% of € 630 = € 504)
utilities advance payments	€ 180	€ 126 (€ 450 - € 504 = - 54)
gross rent	€ 630	
reduced amount (80%)	- € 504	
	€ 126	€ 126

The landlord needs to credit € 126 to the tenant on the utilities bill.

3. Damages to the Premises

a. There is a rebuttable resumption that damages to an apartment were caused by the tenant. The tenant is responsible for any damages exceeding normal tear and wear (§ 538 BGB). The standards for what constitutes normal tear and wear are, however, often in dispute, *e.g.*, stains on walls, cigarette burns on the carpet or damage done to floors caused by pointed heels would not be considered normal wear and tear.

b. The tenant's only defenses are that the damages were preexisting or are consistent with normal tear and wear. The argument of preexisting damages can be best supported by a moving in protocol. Every crack, dent, chip and scratch needs to be pinned down in that list. It is the only way to make sure, that the defect, which will clearly be listed on the moving out protocol, can be identified as pre-existing.

4. Unpaid Rent

a. Under German law the landlord has the remedy of distress (§ 562 BGB). He/She may retain personal property of the tenant as security where there are unsettled bills but only in so far as legally feasible. In such a case the tenant is not allowed to remove the property out-of the premises without the landlord's consent.

b. Moreover, the landlord may choose whether he/she uses the security deposit as a set off or sues the tenant in a court of law for the unpaid balance or - if the requirements are met - terminates the lease.

5. Sale of the Premises

a. The sale of the premises does not terminate the residential lease (§ 566 BGB). However, before a house is sold, a landlord can terminate the agreement under an extraordinary hardship provision, *i.e.*, only if he/she would lose out at least 20% in value due to the lease. By operation of law, the new owner assumes the position of the old landlord in the rental agreement.

b. The purchaser will only be considered the new owner once he/she is registered in the "Grundbuch" (Real Estate Register). The notarized purchase agreement does not make him/her the owner.

6. Pet Policies

a. The tenant may keep small pets such as tropical fish or exotic birds. Yet, the landlord can specifically prohibit bigger animals like dogs and cats. If the landlord is still undecided on that issue the internet page http://www.canismajor.dog.com/dog/apart.html#Policies offers to dog owners some advice and a strategy to follow:

"Those who rent an apartment must be prepared to abide by the conditions as set down by the owner of the property. If this means no pets because some pet owners in the past have caused trouble, the pet owner has three options: give up the pet, give up the apartment, or change the landlord's mind. Those who choose the third approach have their work cut out. Most important is to keep cool, gather information to provide the benefits of pets to people and to a stable environment in the apartment building or complex, and point out that responsible pet owners are likely to be responsible tenants as well. Provide documents to back up your contention and your willingness to compromise. A sample pet policy for the landlord's consideration, a pet resume, references, and a schedule of pet care that shows your efforts to be a responsible owner are necessary. The schedule can include everything from regular veterinary visits to grooming appointments, daily walks, training lessons, participation in pet-facilitated therapy or education programs - in short anything you do with the dog that proves your sense of responsibility. Be willing to concede a point our two. For example, allow the landlord to check up on the apartment or the pet occasionally, make sure Rambo is neutered, and don't let Fifi urinate in the flowerbed. If the landlord wants to see an obedience class certificate, either go to a class, [take the AKC Canine Good Citizen test,] or prove that the dog obeys to simple commands he would learn in class. Vow to keep the apartment free of fleas and promise you'll never allow Ranger outside without a leash. Ever, even he has an advanced obedience title."

b. All German States have strict rules concerning dangerous dogs. Some dogs are not even allowed to be kept in Germany, *e.g.*, Pit Bull, Bandog, American Staffordshire Bullterrier, Staffordshire Bullterrier, Tosa-Ina are considered illegal.

c. Anyway, all dogs need to be registered and for those who keep a dog in Germany, it might be a good idea to get a dog liability insurance. Under German law there exists strict liability concerning damage caused by dogs and other domestic animals (§ 833 and § 834 BGB). Exemptions to that rule are very limited. There is no first bite is free rule. Every German keeps his/her dog insured because of the legal consequences of the strict liability. *E.g.*, a dog owner would be fully liable where the dog runs loose, crosses a street and the driver of a car while avoiding to run over the dog smashes his/her vehicle against a tree.

d. There is a dog tax, collected by the municipalities, from which members with SOFA status are exempted as long as they do not hold German citizenship.

IV. GERMAN CUSTOMS & CULTURAL DIFFERENCES

a. To know the rules and customs should help the tenant to understand what the neighbors might expect of him/her or why they behave the way they do. It is the key to a pleasant living surrounding.

b. Germans generally live a clean and quiet life at home. Sweeping the sidewalks and sometimes even the streets very early on Saturday mornings is not uncommon at all, especially in the smaller towns in Germany. Furthermore, the windows of a house are cleaned at least once during all four seasons, not only to ensure a good look outside but also to prevent dirt from washing down on the paint when it rains.

c. It is against German law to wash cars on the street unless no other cleaning compounds are used than just pure water.

d. Sundays are considered a day of rest. Generally shops are closed. Noise and work should be avoided on Sundays, including household chores and washing and working on cars. Loud music and barking dogs on balconies are the best way to ruin a good relationship with a neighbor. For even during the week there are so-called quiet hours, usually from noon to 14:00 and after 22:00 through the next morning at 7:00.

e. Recycling is another big topic in Germany. The trash is separated into different categories and placed into cans accordingly. Most towns have large bins marked "Altpapier" (old paper), "Altglas" (old glass), "Batterien" (batteries), "Dosen" (cans), "Biomüll" (biodegradable).

VI. TERMINATION

A. Terminating the Rental Agreement

1. Basic Requirements

a. In residential leases only written termination notices are valid (§ 568 BGB).

b. When the landlord seeks to terminate the lease, he must state the reason for the termination and inform the tenant of his/her right to protest. The tenant never needs to give a reason, except in case of an extraordinary termination (effective immediately). With very few exceptions, a landlord may terminate a rental agreement only for cause. An important exception, however, exists where a tenant lives in one of two apartments in a house and his/her landlord occupies the other apartment because in such a case, no reason needs to be given but if so then the notice period is prolonged by 3 months (§ 573a BGB). Watch out for a clause in the lease abolishing – for the landlord as well as the tenant - the requirement to submit a written specific

circumstance IAW § 569 para. 4 and 5 BGB when exercising an extraordinary termination (effective immediately).

c. The tenant's notice period is no more than 3 months.

d. The notice period for the landlord's termination may not be shortened to less than the statutory minimum. However, the statutory minimum period for a landlord varies depending on the kind of residential lease and the length of the lease. After 5 and 8 years of occupation by a tenant, the landlord's period to give notice increases to 6 and, finally, 9 months (§ 573c BGB). Since the German Constitution, the GG ("Grundgesetz" - Basic Law), grants to everybody the right of privacy of the home and emphasis the social commitment on property, the tenant's interest and the landlord's interest need to be weighed against each other to justify the different termination periods ("asymetrische Kündigungsfristen").

e. Germans do not move easily. Often they stay in the same area for generations. The law reflects this attitude by providing a variety of balancing mechanisms to ensure a landlord gets a return on his investment and the tenant is protected in a reasonable manner in which he/she can enjoy life "within his/her (own) four walls". A tenant will not move but for a reason, *e.g.*, change of jobs, a bigger family, or a move into a home for the elderly and, therefore, the tenant needs to be able to move out within a short period of time. Often the tenant cannot afford to pay two rents, particularly given the financial obligations at the beginning of a lease. The landlord on the other hand primarily uses the premises for its economic value. The landlord's termination notice forces the tenant to give up his/her social integration into the neighborhood.

f. The new termination periods apply even to lease contracts signed before September 1, 2001 if the lease contract repeated the statutory termination periods in force at that time. Only where an individual agreement had been made (to either shorten the tenant's termination notice or to prolong the landlord's termination notice) that clause will remain in force.

g. The landlord may terminate the entire lease contract or limit his termination to parts of the premises (§ 573b BGB).

h. Notice periods for landlord termination of residential leases which are not let to a family for permanent use or/and where the landlord lives in the premises as well differ considerably from the above standard periods (§ 549 and § 573c BGB):

(i) If the landlord lives in the apartment as well, he can give a notice of termination by the 15th of the month to be effective on the last day of that month (§ 573d BGB).

(ii) If the landlord lives in one of the two apartments himself § 573a BGB applies and, therefore, no reason needs to be given but the landlord's statutory termination period is prolonged by 3 month.

i. Since Germany generally does not follow the mailbox rule, the termination notice is to be received on or before the third working day of a month to become effective at the end of the second month following the month of receipt of the notification. Note, that by definition Sundays and official German holidays are no working days (§ 193 BGB). Saturdays are only considered no working days if a Saturday would be the day on which the deadline expires, *i.e.*, the 3rd working day.

j. Example: A soldier and his/her dependents live in an apartment building. They plan to move out and, therefore, sent a termination notice to the landlord. The landlord receives the notice on April 4th (the 3rd working day because the month started with a weekend: Saturday (1st day: 04/01), Sunday (doesn't count), Monday (2nd day: 04/03), Tuesday (3rd day: 04/04). The termination will be effective on June 30th. If the April 4th had been the 4th working day, the termination would become effective on July 31st. In case the 3rd working day would have been a Saturday (Thursday, 1st day: 04/01), the termination period would be prolonged till Monday (3rd day: 04/05), April 5th.

2. Termination Clause and Termination Agreement

a. Even though the landlord shall not shorten the statutory minimum period for a termination, there are two exceptions to that rule. Both parties can agree on an early termination either upfront in their contract (b.) or after the fact (d.)

b. Firstly, the tenant is free to put a termination clause in the rental agreement that allows him/her to terminate the lease even before the statutory minimum period is up. The tenant does not have to wait the ordinary 3 months. Particularly in cases where a PCS move occurs, the soldiers will seldom have the time to plan exactly for his/her leave. Moreover, the soldier might be required to move into the barracks or government controlled housing for other reasons. Therefore, the tenant should insist on a special termination clause in the rental agreement.

c. Usually the HRO should talk to the landlord and convince the landlord of the necessity of such a special termination clause. If the contract has been already signed and the landlord refuses to agree to a modification, an ordinary termination may be threatened and the tenant should start looking for another apartment up for rental. A possible termination clause may be phrased as follows but please note, that such a termination clause is a flat one and does not allow a 3 working day extension:

- Supplement to the rental contract between __ and ___: The tenant is granted the right to terminate the lease by giving the landlord 30 days advance written notice effective the 15th or the last day of a calendar month in case the tenant is transferred to a new duty station or returns permanently to the USA. In addition, the tenant is granted the right to terminate the lease by giving the landlord 15 days advance notice effective the 15th or the last day of a calendar month in case the tenant is required to move into US Government controlled accommodations. In case the termination date is not adhered to, the termination notice will be to the next possible permissible date.
- Zusatzvereinbarung zum Mietvertrag zwischen ___ und ___: Bei dienstlicher Versetzung des Mieters oder dauerhafter Rückkehr in die USA hat der Mieter das Recht dem Vermieter unter Einhaltung einer Frist von 30 Tagen zum 15 oder zum letzten Tag eines Monats schriftlich zu kündigen. Zusätzlich, bei dienstlicher Anordnung in eine US-Dienstwohnung zu ziehen, hat der Mieter das Recht dem Vermieter unter Einhaltung einer Frist von 15 Tagen zum 15. oder zum letzten Tag eines Monats schriftlich zu kündigen. Wird die Kündigungsfrist nicht eingehalten, so gilt die Kündigung zum nächst möglichen zulässigen Termin.

d. Secondly, the tenant and the landlord are free to enter into a termination agreement at any time. If all parties can agree on the issues, they are not bound by the statutory minimum period for a termination. However, it is rather risky to rely on such a happy ending. These cases happen only too rarely.

3. Ordinary Termination (for Cause) § 573 BGB)

a. An ordinary termination by the landlord requires a cause:

- continued use of the premises in a manner violative of the rental agreement despite a landlord's warning notices, or
- existence of a compelling personal need for the premises because the landlord himself or a member of his/her family need to move in. A landlord's mere wish to live in his/her own home is not sufficient cause for an eviction, or
- prevention of adequate economic utilization and thereof resulting severe disadvantages to the landlord, *e.g.*, the landlord may also terminate the lease in an old building in poor condition which is uneconomically repairable and must be torn down. Yet, the possibilities to obtain a higher rent or the mere fact of an upcoming sale of premises (without a severe disadvantage demonstrated) do not constitute good reason.

b. Only the reasons given in the landlord's termination notice will be considered, when determining whether there was a good reason. Additional reasons will only be excepted if they occurred after the fact. Therefore, the landlord is prevented from suddenly coming up with other reasons to justify his termination notice if they had been in existence before he sent his termination notice.

c. Rental agreements for a fixed term may not be terminated early by ordinary termination notice at all, unless the parties enter into a termination agreement (§ 542 BGB). The biggest myth that exists is that a tenant just needs to present three potential tenants that are willing to rent the premises and if the landlord refuses to pick one, the tenant is no longer bound by the rental agreement. This is completely wrong. Instead the tenant may seek rescue to a legal trick. The tenant may request the landlord's permission to sublease the apartment to reduce his/her loss. The landlord usually does not favor to have someone living in the apartment whom he/she does not know and to whom no contractual relationship exists. Therefore, the landlord often withholds his/her permission and if that proves to be unreasonably given the factual situation, the tenant may terminate the rental agreement according to the general rules. However, the tenant needs to keep in mind, he/she will remain responsible for the rent obligation and additionally responsible for some acts of the sub-tenant.

4. Extraordinary Termination (effective immediately) (§ 543 and § 569 BGB)

a. In order for an extraordinary termination to be effective immediately, it has to be unreasonably for a party to be expected to continue the lease because of extraordinary circumstances, which have to be stated in the termination notice or else it cannot be effective.

b. The extraordinary circumstances are exclusively defined in the rental provisions of the Code, preventing the landlord from inventing new ones (§ 569 para 5 BGB).

- serious offenses, threats or assaults are committed
- one party persistently disturbances the peace of the house
- the landlord does not grant in time or deprives the tenant access and/or usage of the premises. The burden of proof is on the landlord

- the tenant cannot exercise his/her extraordinary termination right, if he/she knew or should have known at the time of concluding the lease contract that this problem exists
- the tenant can always exercise his/her extraordinary termination right if living in the premises constitutes a substantial threat to the tenant's health
- the tenant violates the landlord's rights unreasonably by neglect of due care with respect to the premises and thereby exposing it to unreasonable danger
- if the extraordinary circumstance result from the violation of a contractual duty in the lease contract, the landlord has to give first a warning notice with an adequate deadline to cure the violation before he will be allowed to send a termination notice. However, no warning notice is required, where
  (i) a deadline would be futile
  (ii) after weighing both parties' interests, an immediate termination is justified due to special circumstances
  (iii) the tenant defaults on the rent payments as defined in § 543 para. 2 No. 3 BGB.
- the tenant fails to pay the rent or a substantial amount of the rent (usually amounting to one-month's rent) for a consecutive period of two months or the arrears amount to a sum equal to a two months' rent (§ 543 para. 2 No. 3 BGB).
  (i) the landlord cannot terminate the lease if he receives the rent before the tenant receives his termination notice
  (ii) the landlord's termination notice becomes invalid if the tenant has the right to set off a claim against the rent and he exercises that right immediately after receipt of the termination notice
  (iii) the landlord's termination notice also becomes invalid if the tenant actually pays the rent due within the first two months following the filing of a lawsuit for eviction against him/her or if a public agency or institution legally obligates itself to pay the rent in full. Yet this exception does not apply if had been already used within the previous two years (§ 569 para. 3 Nr. 2 sentence 2 BGB).
- if the landlord has obtained a judgment against the tenant for his/her agreement to a rent increased, the landlord has to give the tenant two months to comply with it before he can base his termination notice on the tenant's non-payment of rent due IAW § 543 para. 2 No. 3 BGB. However, this does not apply if the landlord can base his termination notice on the non-payment past rent due (not just the increased amount) as defined in § 543 para. 2 No. 3 BGB.

5. Extraordinary Termination (with statutory notice period)

a. See, no termination by death.

b. The termination will not be effective immediately.

6. Termination upon creating Condominiums

a. Once an apartment house is turned into condominiums, the purchaser of such a condominium is prevented from exercising his/her termination right as long as it is based on personnel own need or his intent to resell for three years following the purchase. Moreover, the then applicable statutory termination period will be added to the three-year period.

b. Each German State Government is authorized to pass regulations extending this deadline up to 10 years. However, such a regulation has to be renewed every two-years.

7. Tenant's Right to Protest

a. According to § 574b BGB, the tenant may protest the termination no later than 2 months before the lease terminates on two grounds. The tenant can either dispute the stated reasons for the termination or claim a case of (social) hardship, *e.g.*, adequate substitute housing cannot be obtained under reasonable conditions like in cases of families with numerous children.

b. § 574 para. 1 BGB reads as follows: "The tenant may protest the termination of a lease and request a continuation of the lease, if the termination of the lease would constitute a hardship for the tenant, his family or a dependent of his household, which cannot be justified even considering the proper interests of the landlord. This does not apply if circumstances exist, allowing the landlord to give an extraordinary termination notice without a statutory notice period."

c. Only the reasons mentioned in the termination notice will be considered. The landlord is not allowed to bring additional reasons thereafter, unless the reason arose after the notice was sent

d. Yet, any protest is precluded where:

- a fixed-term lease exists
- premises have been let only for temporary use, such as a holiday apartment
- the tenant has given notice of termination
- an extraordinary termination without statutory notice against the tenant is justified

8. No Termination by Death or Destruction

a. A tenant's death does not terminate the lease (§ 563 BGB). By operation of law and in the priority listed, the following persons become a party to the rental agreement on condition that there had been a joint household:

- surviving spouse
- children and/or a partner of the same or opposite sex
- children and/or other family members
- children and/or any other person (if there was more to it than just a joint household)
- the tenant's heirs become under the German universal succession right a party to the rental agreement (§ 564 BGB) e.g. where the soldier's German parents-in law decease, that soldier's spouse becomes a party to the rental agreement.

b. Within one month after they have learnt of the tenant's death, persons in the joint household can declare they do not want to become a party to the contract. The tenant's heirs do not have that option. If they "inherit" the contract, they may, however, exercise an extraordinary termination right (with statutory notice period).

c. Within one month after persons in the joint household have taken over the lease contract the landlord may terminate by extraordinary termination for a reason. Where the

tenant's heirs take over the contract, the landlord may terminate the lease within a month by extraordinary termination for no reason.

d. The lease continues even if the building burns down. There is no duty to rebuild a building that is destroyed, even if it was insured. Yet, the tenant has the right to withhold the rent. However, that scenario can be contracted away in the rental agreement.

9. Eviction and Holdover Tenant

a. If a judgment orders the tenant to vacate the apartment, the tenant may nevertheless be granted a reasonable time for vacating the premises, either at the tenant's request, made at least as a precaution during the court procedure or upon the court's own motion according to § 721 and § 794a ZPO. A request for extension can also be filed in writing with the court no later than 2 weeks prior to expiration of the stated period for vacating the apartment.

b. However, the landlord will be entitled to a compensation for loss of usage. The amount claimed could be the agreed amount of rent or the rent, which is customary in the locality for comparable apartments (§ 546a BGB). In addition to compensation for loss of usage, the landlord will also be entitled to claim damages if the tenant continues to occupy the apartment after expiration of the vacating time (§ 571 BGB).

B. Statute of Limitations

1. General Rule

a. The German Statute of Limitation (SoL) concerning civil claims is incorporated in the BGB, too. According to § 199 BGB the period of limitation starts with the end of the year in which

(1) the claim arose and
(2) the creditor knew about the circumstances giving rise to the claim as well as the identity of the debtor or without gross negligence should have gained knowledge thereof.

b. If the debtor wants to allege that the creditor's claim is time-barred, he has the burden of proof to demonstrate that the creditor gross negligently failed to obtain the above-mentioned information sooner, thereby leading to an earlier start of the limitation period. Absent gross negligence the creditor's maximum deadline for obtaining the information is often 10 years (§ 199 para. 4 BGB) or even longer. Yet, once the debtor possesses the information he must commence some action against the debtor at the earlier of either the end of the SoL or the end of the applicable maximum deadline or loose his claim.

c. The SoL distinguishes between a mere suspension (§ 208 BGB) and an actual new beginning (§ 212 BGB) of the limitation. Whereas a suspension, like a granted delay, only delays the time before the claim is tolled, a new beginning lets the full period begin anew. Negotiations about the claim as well as a court procedure, *e.g.*, payment order, are merely considered suspensions. The claim will be time barred at earliest 3 months after the suspension ended, *i.e.*,

the negotiations failed. However, an enforcement procedure lets the full period always begin anew, just like an acknowledgment of the claim by the debtor.

2. Lapse of Time

a. The general SoL for a claim is 3 years (§ 195 BGB).

b. Once the landlord has assumed possession of the apartment vacated, he has only 6 months to pursue a claim for damages against the tenant (§ 548 BGB). The recording of the damages on the inventory form normally is not considered a tenant's acknowledgment of obligation to pay damages and a landlord's letter asserting his claim during the 6-month period will not toll the SoL.

c. By contrast, a landlord has 3 years to pursue his claim for rental and utility payments against the tenant. This period starts with the end of the year during which the claim for payments arose.

d. As long as the landlord has not repaid the rental security deposit, he may at any time set off that amount against his claim, even if the claim would be otherwise time barred.

e. Example: The landlord assumes possession of the premises on December 31, 2002. A claim for damages is barred on July 1, 2003. A claim for unpaid rent is barred on January 1, 2006. The landlord assumes possession of the premises on January 1, 2003. A claim for damages is barred on July 2, 2003. A claim for unpaid rent is barred on January 1, 2007!

Prepared by Joerg C. Moddelmog, German Attorney-Advisor

APPENDIX A

INTERNET RESOURCES[1]

The purpose of this list is to provide useful information to DoD and Coast Guard legal assistance practitioners. Inclusion of any site on this list does not constitute endorsement by The Judge Advocate General's School, The Department of the Army, The Department of Defense, or any other agency of the United States Government.

Web Sites with Useful Consumer Law & Legal Assistance Information	
SITE	**SUMMARY**
General Applicability	
http://www.va.gov/	The Department of Veterans Affairs web page. Lots of useful information about VA benefits ranging from guaranteed home loans to survivor benefits, to dependency and indemnity compensation. The place to start for many of the casualty assistance/survivor benefits issues.
http://www.jagcnet.army.mil/	The Army JAGC Web Site. The place to go if you need any products put out by the Army JAGC, like TJAGSA publications. Some sections require a password which attorneys can request online.
http://www.hqmc.usmc.mil/hqmcmain.nsf/frontpage	Official information site for the Marine Corps. Contains links to a variety of information about the Marines including links to digital publications and Marine Messages.
http://neds.nebt.daps.mil/usndirs.htm	The official site for Navy directives and forms.

[1] All of the websites were verified on 9 June 2003. If you find any changes or have any recommendations for additional websites, please contact me at Jeremy.ball@hqda.army.mil or my replacement at TJAGLCS, Administrative and Civil Law Department.

Web Sites with Useful Consumer Law & Legal Assistance Information	
SITE	**SUMMARY**
https://aflsa.jag.af.mil/php/dlaw/dlaw.php https://aflsa.jag.af.mil/cgi-bin/user/home.pl	The Air Force JAGC Web Site. The top cite is where you must go to register first and the bottom cite is the FLIGHT home page. . There is a link provided on JAGCNET.
http://www.usapa.army.mil/	Official site for Army regulations, pamphlets in electronic format.
http://www.defenselink.mil/pubs	The DoD Pubs page. Links to DoD directives, the MCM and UCMJ.
http://www.uscg.mil/hq/g-s/g-si/g-sii/sii-3/sii-3.htm	The official directives and publication site for the U.S. Coast Guard.
http://www.uscg.mil/legal/	The official Coast Guard JAGC Website
http://afpubs.hq.af.mil/	The official site for Air Force publications and forms.
http://www.dfas.mil/	Defense Finance and Accounting Service Site. Lots of useful information about pay rates, involuntary allotments, etc. Applicable to many types of legal assistance cases.
General Consumer Law	
www.ftc.gov	Summaries and documents from FTC actions. Plain language summaries of federal consumer protections suitable for issue directly to consumers – great for preventive law.
http://www.consumer.gov/idtheft/	U.S. government's central website for information about identity theft. Induces an Identity Theft Affidavit which can be downloaded.

Web Sites with Useful Consumer Law & Legal Assistance Information	
SITE	**SUMMARY**
www.pueblo.gsa.gov	The government's Consumer Information Center. Consumer Resource Handbook online and available for download. All free pubs and info in Consumer Resource Catalog available for download. Comprehensive links on a variety of subjects. **GREAT SITE!**
http://www.consumer.gov	The ***U.S. Consumer Gateway*** -- **"consumer.gov"** -- is a "one-stop" link to a broad range of federal information resources available online. It is designed so that you can locate information by category -- such as ***Food***, ***Health***, ***Product Safety***, ***Your Money***, and ***Transportation***. Each category has subcategories to direct you to areas within individual federal web sites containing related information.
http://www.notice.com/	CENTRAL NOTICE -- A service of **The Notice Company**, brings you important consumer and legal announcements including class actions and product recalls.
www.cpsc.gov/cpscpub/prerel/category/topic.html	Consumer Product Safety Commission lists recalls from 1995 to the present, categorized by topics/types of products.
www.consumerlaw.org	National Consumer Law Center Home Page. Order NCLC publications. Links to other sites. Some consumer news.
www.bbb.org	Online Business reports -Information, phone numbers, etc. for all state offices. Links to reports on charitable institutions. Buying Guide Pamphlets. Links to domestic and international agencies (including Europe & Korea).

Web Sites with Useful Consumer Law & Legal Assistance Information	
SITE	**SUMMARY**
www.emich.edu/public/coe/nice/nice.html	National Institute for Consumer Education at Eastern Michigan University. Good collection of fact sheets, mini-lesson outlines. Lists of Articles categorized by subject. Some links to other sites.
www.consumerworld.org	Comprehensive set of links to consumer information resources on the internet. Site has menu links plus it is searchable Includes available links to state AG offices under the "agencies" link. A great place to start your internet searching.
www.federalreserve.gov	Federal Reserve Board Home Page. Some good info on enforcement actions and FRB news releases. Some stats on consumer issues.
www.fraud.org	National Fraud Information Center run by the National Consumers League a longstanding private consumer group. Good information telemarketing fraud. You can report fraud on-line or though a listed 800 number. Scam alerts sorted by subject. Site is searchable.
www.nsclc.org	National Senior Citizens Law Center. A very helpful web site for the latest information on issues of particular interest to seniors. The focus is on Social Security, Medicare and other health issues.
www.naca.net	National Association of Consumer Advocates. Provides a listing of consumer attorney members throughout the country, divided by practice area. Also includes updated information on hot consumer topics and other events.
http://www.abiworld.org/	American Bankruptcy Institute. This website provides bankruptcy information for consumers and lawyers.

Web Sites with Useful Consumer Law & Legal Assistance Information	
SITE	**SUMMARY**
www.nvla.org	National Vehicle Leasing Association. Good consumer information on vehicle leasing.
http://www.kbb.com/	Kelley Blue Book. You can get new and used car values for your clients before they buy or sell a car.
Credit Reporting Agencies	
http://www.experian.com/consumer/index.html	Experian Corporation bought TRW's consumer credit reporting business several years ago. They have a very nice site with lots of useful information as well as the ability to order client credit reports online. Of course these reports are not free, so you have to enter a credit card number. There is also valuable information on this site about risk scores and how they are calculated.
http://www.transunion.com/	Another nice site that allows you to order credit information online. The ordering site is secure and you have to charge the order to your credit card. This also contains some useful consumer information including info on credit card fraud.
http://www.equifax.com/consumers/consumers.html http://www.myfico.com/myfico/Home.asp	Another quality site with features similar to the others. The nicest feature, however, is an available sample credit profile that you can view and print for consumer education. A cite with credit scores. Your FICO scores are a measure of your financial responsibility, based on your credit history. Most lenders will look at your FICO scores when evaluating your credit or loan applications.

APPENDIX B

TABLES OF STATE STATUTES[1]

1. Lemon Laws and Unfair & Deceptive Acts and Practices Statutes.
2. Lemon Buyback Laws and Salvage Vehicle Laws.
3. Telemarketing and Debt Collection Statutes.

[1] If you find an error or addition please contact me at oren.mcknelly@conus.army.mil or my successor at TJAGLCS, Administrative and Civil Law Department.

State Consumer Protection Laws Quick Reference		
STATE	**LEMON LAW**	**UDAP STATUTE**
Alabama	Ala. Code § 8-20A-1	Ala. Code § 8-19-1 to 8-19-15
Alaska	Alaska Stat. § 45.45.300	Alaska Stat. § 45.50.471to 45.50.561
Arizona	Ariz. Rev. Stat. Ann § 44-1261	Ariz. Rev. Stat. Ann. § 44-1521to 44-1534
Arkansas	Ark. Code Ann. § 4-90-401	Ark. Code Ann. § 4-88-101to 4-88-207
California	Cal. Civ. Code § 1793.22	Cal. Civ. Code § 1750 to 1785 (West) Cal. Bus. & Prof. Code §§ 17200 to 17594 (West)
Colorado	Colo. Rev. Stat. § 42-10-101	Colo. Rev. Stat. § 6-1-101 to 6-1-115
Connecticut	Conn. Gen. Stat. Ann. § 42-179	Conn. Gen. Stat. § 42-110a to 42-110q
Delaware	Del. Code Ann. tit. 6 § 5001	Del. Code Ann. tit. 6 § 2511 to 2527,& 2580 to 2584, & 2531 to 2536
District of Columbia	D.C. Code Ann. § 40-1301	D.C. Code Ann. § 28-3901 to 28-3913
Florida	Fla. Stat. Ann. § 681.102 (West)	Fla. Stat. Ann. § 501.201 to 501.213 (West)
Georgia	Ga. Code Ann. § 10-1-780	Ga. Code Ann. § 10-1-370 to 10-1-375& 10-1-390 to 10-1-407
Guam		Guam Code Ann. Tit. 5, §§ 32101 to 32603
Hawaii	Haw. Rev. Stat. § 481I-2	Haw. Rev. Stat. § 480-1 to 480-24

State Consumer Protection Laws Quick Reference		
STATE	**LEMON LAW**	**UDAP STATUTE**
		& 481A to 481A-5
Idaho	Idaho Code § 48-901	Idaho Code § 48-601 to 48-619
Illinois	815 Ill. Comp. Stat. § 380/1	815 Ill. Comp. Stat. 505/1 to 505/12 & 510/1 to 510/7
Indiana	Ind. Code § 24-5-13-1	Ind. Code Ann. § 24-5-0.5-1 to 24-5-0.5-12(Burns)
Iowa	Iowa Code Ann. § 322G.1	Iowa Code Ann. § 714.16 to 714.16A (West)
Kansas	Kan. Code Ann. § 50-645	Kan. Stat. Ann. § 50-623 to 50.640 & 50.675a to 50.679a
Kentucky	Ky. Rev. Stat. Ann. § 367.840	Ky. Rev. Stat. § 367.110 to 367.990
Louisiana	La. Rev. Stat. Ann. § 51:1941 (West)	La. Rev. Stat. Ann. § 51:1401 to 51:1420 (West)
Maine	Me. Rev. Stat. Ann. tit. 10 § 1161	Me. Rev. Stat. Ann. tit. 5 § 205A to 214 & tit. 10 § 1211 to 1216
Maryland	Md. Code Ann. Com. Law § 14-1501	Md. Code Ann. Com. Law §§ 13-101 to 13-501 &14-101
Massachusetts	Mass. Gen. Laws Ann. ch. 90 § 7N l/2	Mass. Gen. Laws Ann. ch. 93A §§ 1-11
Michigan	Mich. Comp. Laws § 257.1401	Mich. Comp. Laws § 445.901 to 445.922
Minnesota	Minn. Stat. Ann. § 325F.665	Minn. Stat. Ann. §§ 8.31, 325D.43 to 325D.48, 325F.67, & 325F.68 to 325F.70 (West)
Mississippi	Miss. Code Ann. § 63-17-151	Miss. Code Ann. § 75-24-1to 75-24-27
Missouri	Mo. Stat. Ann. § 407.560 (Vernon)	Mo. Rev. Stat. § 407.010 to 407.307

State Consumer Protection Laws Quick Reference		
STATE	**LEMON LAW**	**UDAP STATUTE**
Montana	Mont. Code Ann. § 61-4-501	Mont. Code Ann. § 30-14-101 to 30-14-142
Nebraska	Neb. Rev. Stat. § 60-2701	Neb. Rev. Stat. § 59-1601 to 59-1623 & 87-301 to 87-306
Nevada	Nev. Rev. Stat. § 597.600	Nev. Rev. Stat. §§ 41.600 & 598.0903 to 598.0999
New Hampshire	N.H. Rev. Stat. Ann. § 357-D	N.H. Rev. Stat. Ann. § 358-A: 1 to 358-A: 13
New Jersey	N.J. Stat. Ann. § 56:12-30	N.J. Stat. Ann. § 56:8-1 to 56:8-91 (West)
New Mexico	N.M. Stat. Ann. § 57-16A-1	N.M. Stat. Ann. § 57-12-1 to 57-12-22
New York	N.Y. Gen. Bus. Law § 198-a; N.Y. Veh. & Traf. Law § 417-a.	N.Y. Exec. Law § 63(12); N.Y. Gen. Bus. Law §§ 349 & 350 (Consol.)
North Carolina	N.C. Gen. Stat. § 20-351	N.C. Gen. Stat. § 75-1.1 to 75-35
North Dakota	N.D. Cent. Code § 51-07-16	N.D. Cent. Code . §§ 51-15-01 to 51-15-11
Ohio	Ohio Rev. Code Ann. § 1345.71	Ohio Rev. Code Ann. §§ 1345.01 to 1345.13 & 4165.01 to 4165.04 (Baldwin)
Oklahoma	Okla. Stat. Ann. tit. 15 § 901	Okla. Stat. Ann. tit. 15 § 751 to 763 & tit. 78 §§ 51 to 55 (West)
Oregon	Or. Rev. Stat. § 646.315	Or. Rev. Stat. § 646.605 to 646.656
Pennsylvania	Pa. Stat. Ann. Tit. 73 § 1951 (Purdon)	Pa. Stat. Ann. Tit. 73 §§ 201-1 to 201-1.3 (Purdon)
Puerto Rico		P.R. Laws Ann. tit.3§§ 341 to 341w

State Consumer Protection Laws Quick Reference		
STATE	**LEMON LAW**	**UDAP STATUTE**
		& tit. 10 §§ 257 to 273
Rhode Island	R.I. Gen. Laws § 31-5.2-1	R.I. Gen. Laws § 6-13.1-1 to 6-13.1-27
South Carolina	S.C. Code Ann. § 56-28-10 (Law. Co-op)	S.C. Code Ann. § 39-5-10 to 39-5-160 (Law. Co-op)
South Dakota	S.D. Codified Laws Ann § 32-6D-1	S.D. Codified Laws Ann. § 37-24-1 to 37-24-35
Tennessee	Tenn. Code Ann. § 55-24-201	Tenn. Code Ann. § 47-18-101 to 47-18-125
Texas	Tex. Rev. Civ. Stat. Ann. § 4413(36) (Vernon)	Tex. Bus. & Com. Code Ann. §§ 17.41 to 17.63 (Vernon)
Utah	Utah Code Ann. §§ 13-20-1, 41-3-406	Utah Code Ann. §§ 13-2-1 to 13-2-8, 13-5-1 to 13-5-18, & 13-11-1 to 13-11-23, & 13.11a-1 to 13.11a-5
Vermont	Vt. Stat. Ann. tit. 9 § 4170	Vt. Stat. Ann. tit. 9 § 2451 to 2480g
Virginia	Va. Code § 59.1-207.9 to 207.16	Va. Code Ann. § 59.1-196 to 59.1-207
Virgin Islands		V.I. Code Ann. Tit. 12A §§ 101-123 & 180-185
Washington	Wash. Rev. Code § 19.118.021	Wash. Rev. Code Ann. §§ 19.86.010 to 19.86.920
West Virginia	W. Va. Code § 46A-6A-1	W.Va. Code §§ 46A-6-101 to 46A-6-110
Wisconsin	Wis. Stat. Ann. § 218.015	Wis. Stat. Ann. §§ 100.18 & 100.20 to 100.264
Wyoming	Wyo. Stat. Ann. § 40-17-101	Wyo Stat. Ann. §§ 40-12-101 to 40-12-114

State Consumer Protection Laws Quick Reference II		
STATE	**LEMON BUYBACK LAW**	**SALVAGE VEHICLE STATUTE**
Alabama	Ala. Code § 8-20A-3, 8-20A-4, 8-20A-5	Ala. Code § 32-8-87
Alaska	Alaska Stat. § 45.45.335 & .340	Alaska Stat. § 28-10-211
Arizona	Ariz. Rev. Stat. § 44-1266	Ariz. Rev. Stat. Ann. §§ 28-1411, 28-321, 321.02
Arkansas	Ark. Code Ann. § 4-90-412	Ark. Code Ann. § 27-14-2301 to 2307
California	Cal. Civ. Code § 1793.23 & .24	Cal. Veh. Code §§ 6050, 111515.1, 111515.2, 24007 (West)
Colorado	Colo. Rev. Stat. § 42-10-101 to 107	Col. Rev. Stat. § 42-6-136
Connecticut	Conn. Gen. Stat. Ann. § 42-179(g), 42-179(i)	Conn. Gen. Stat. § 14-16c
Delaware	NA	Del. Code Ann. tit. 6 §§ 1412, 6717
District of Columbia	D.C. Code § 40-1302(g)(3)	D.C. Code Ann. § 40-1305
Florida	Fla. Stat. Ann. § 681.111; 681.112; 681.114(2), 319.14 (West)	Fla. Stat. Ann. § 319.14 (West)
Georgia	Ga. Code Ann. § 10-1-784 & 785	Ga. Code Ann. § 40-3-37
Hawaii	Haw. Rev. Stat. § 481I-3, -4, & -7	Haw. Rev. Stat. § 286-48
Idaho	Idaho Code § 48-901	Idaho Code § 49-524 & 525
Illinois	625 Ill. Comp. Stat. § 5/5-104.2 (West)	625 Ill. Comp. Stat. §§ 5/3-117.1, -118.1, 5/3-301 *et. seq.*
Indiana	Ind. Code Ann. § 24-5-13.5-10, -11, & -13	Ind. Code Ann. § 9-22-3-3

State Consumer Protection Laws Quick Reference II		
STATE	**LEMON BUYBACK LAW**	**SALVAGE VEHICLE STATUTE**
Iowa	Iowa Code Ann. § 322G.11 & .12	Iowa Code Ann. § 321.52
Kansas	Kan. Stat. Ann. § 50-645, 50-659	Kan. Stat. Ann. § 8-1,136; 8-1,137; 8-2408
Kentucky	Not Applicable.	Ky. Rev. Stat. § 186A.525, 186A.530
Louisiana	La. Rev. Stat. Ann. § 51:1945.1 & 1946	La. Rev. Stat. Ann. § 32:707
Maine	Me. Rev. Stat. Ann. tit. 10 § 1167 & 1168	Me. Rev. Stat. Ann. tit. 29-A, § 667
Maryland	Md. Code Ann. Com. Law. § 14-1502	Md. Code Ann. Com. Law § 13-506(b)
Massachusetts	Mass. Gen. Laws ch. 90 § 7N l/2(5)	Mass. Gen. Laws ch. 90D, §§ 20D & 20F
Michigan	Mich. Comp. Laws Ann§ 257.1403	Mich. Comp. Laws Ann. § 257.217c
Minnesota	Minn. Stat. Ann. § 325F.655(5)(a); 325F.665(5); 325.225(9)	Minn. Stat. Ann. §§ 168A.151, 168A.15
Mississippi	Miss. Code Ann. § 63-17-159	Miss. Code Ann. § 63-21-39
Missouri	Mo. Rev. Stat § 407.567	Mo. Rev. Stat. § 301-227, 301-573
Montana	Mont. Code Ann. § 61-4-525	Mont. Code Ann. § 61-3-212
Nebraska	Not Applicable	Neb. Rev. Stat. § 60-129, 60-130
Nevada	Not Applicable	Nev. Rev. Stat. §§ 482.245, 487.110
New Hampshire	Not Applicable	N.H. Rev. Stat. Ann. § 261.22
New Jersey	N.J. Stat. Ann. § 56:12-35	N.J. Stat. Ann. § 39-10-31 (West) N.J. Admin Code 13:21-22.15

State Consumer Protection Laws Quick Reference II		
STATE	**LEMON BUYBACK LAW**	**SALVAGE VEHICLE STATUTE**
New Mexico	N.M. Stat. Ann. § 57-16A-7	N.M. Stat. Ann. § 66-3-10.1
New York	N.Y. Veh. & Traf. Law § 417-a(2)	N.Y. Veh. & Traf. Law §§ 429, 430
North Carolina	N.C. Gen. Stat. § 20-351.3(d)	N.C. Gen. Stat. § 20-71.3
North Dakota	N.D. Cent. Code § 51-07-22	N.D. Gen. Stat. § 39-05-20.1, 39-05-20.2
Ohio	Ohio Rev. Code Ann. § 1345.76(1)	Ohio Rev. Code Ann. §§ 4505.11 & 4505.181 (Baldwin)
Oklahoma	15 Okl. St. § 901 (2003)	Okla. Stat. Ann. tit. 47 § 591.8, 1111 (West)
Oregon	Not Applicable	Or. Rev. Stat. § 803.015, 801.405
Pennsylvania	Pa. Stat. Ann. tit. 73 § 1960, 1961, 1962 (Purdon)	Pa. Stat. Ann. tit. 75 § 1117 (Purdon)
Rhode Island	R.I. Gen. Laws § 31-5.2-9; -10, & -11	R.I. Gen. Laws § 31-46-4
South Carolina	S.C. Code Ann. § 56-28-50, -100, -110 (Law. Co-op)	S.C. Code Ann. § 56-19-480 (Law. Co-op)
South Dakota	S.D. Codified Laws Ann § 32-6D-9	S.D. Codified Laws Ann. §§ 32-3-51.8, 32-3-51.12, 32-3-53
Tennessee	Not Applicable	Tenn. Code Ann. § 55-3-212
Texas	Tex. Rev. Civ. Stat. Ann. § 4413(36) § 6.07 (Vernon)	Tex. Code Ann. Trans. § 501.091 to 501.094 (West)
Utah	Utah Code Ann. §§ 41-3-406 to -414, 41-1a-522	Utah Code Ann. § 41-1a-1000
Vermont	Vt. Stat. Ann. tit. 9 § 4179, 4181	Vt. Stat. Ann. tit. 23 § 2093

State Consumer Protection Laws Quick Reference II		
STATE	**LEMON BUYBACK LAW**	**SALVAGE VEHICLE STATUTE**
Virginia	Va. Code § 59.1-207.15, 59.1-207.16:1, 18.2-11	Va. Code § 46.2-1605
Washington	Wash. Rev. Code § 19.118.061	Wash. Rev. Code Ann. § 42.12.075
West Virginia	W. Va. Code § 46A-6A-7 & -9	W.Va. Code Ann. § 17A-4-10(e)
Wisconsin	Wis. Stat. Ann. § 218.015(2)(d)	Wis. Stat. Ann. § 342.07 & 342.34
Wyoming	Wyo. Stat. § 40-17-101	Wyo Stat. § 31-2-104

State Consumer Protection Laws Quick Reference II		
STATE	**TELEMARKETING**	**DEBT COLLECTION STATUTES**
Alabama	Ala. Code § 8-19A	Ala. Code § 40-12-80
Alaska	Alaska Stat. § 45.63	Alaska Stat. §§ 8.24.041-380, 45.50.471-561
Arizona	Ariz. Rev. Stat. Ann. § 44-1271 *et. seq.*	Ariz. Rev. Stat. Ann. §§ 32-1001-57
Arkansas	Ark. Stat. Ann. § 4-99-101 *et. seq.*	Ark. Stat. Ann. § 17-24-101 to 404
California	Cal. Bus. & Prof. Code § § 17511,17538 *et. seq.*	Cal. Civ. Code §§ 1788-1788.32
Colorado	Colo. Rev. Stat. §§ 6-1-301 to 6-1-304, & 6-1-901 to 6-1-908, & 4 Colo. Code Regs § 723-22	Colo. Rev. Stat. § 5-1-101 to 12-105; 12-14-101 to 137
Connecticut	Conn. Gen. Stat. § 42-284	Conn. Gen. Stat. § 36a-645 to 647, 36a-800 to 810
Delaware	Del Code Ann. tit. 6 § 2505A	Del. Code Ann. tit. 30 §§ 2301
District of Columbia	D.C. Code § 22-3226.01 Only Criminal Statute	D.C. Code Ann. § 22-3423 to 25, 28-3814 to 3816
Florida	Fla. Stat. Ann. § 501.059 *et. seq.*	Fla. Stat. Ann. § 559.55 to 78
Georgia	Ga. Code Ann. § 10-5B-1 *et. seq.*	Ga. Code Ann. § 7-3-1 to 26
Hawaii	Not Applicable	Haw. Rev. Stat. § 443B-1 to 20
Idaho	Idaho Code § 48-1001 *et. seq.*	Idaho Code § 26-2222 to 2252
Illinois	815 Ill. Comp. Stat. Ann. § 413/1 *et. seq.*	815 ILCS 505/1 mentions debt collection under UDAP
Indiana	Ind. Code Ann. § 24-5-12-5	Ind. Code Ann. § 25-11-1-1 tp 13
Iowa	Not Applicable	Iowa Code Ann. § 537.7101 to 7103

State Consumer Protection Laws Quick Reference II		
STATE	**TELEMARKETING**	**DEBT COLLECTION STATUTES**
Kansas	Kan. Stat. Ann. § 50-670 *et. seq.*	Kan. Stat. Ann. § 16a-5-107
Kentucky	Ky. Rev. Stat. § 367.46951 *et. seq.*	Not Applicable
Louisiana	La. Rev. Stat. Ann. § 45:821	La. Rev. Stat. Ann. § 9:3576.1 *et. seq.*, 9:3510 to 3571
Maine	Me. Rev. Stat. Ann. tit. 32 § 14716	Me. Rev. Stat. Ann. tit. 32 § 11000 to 11054, 9A § 1-101 to 6-301
Maryland	Md. Comm. Law Code § 14-2201 to 14-2205 *et. seq.*	Md. Ann. Code Bus. Reg. 7-101 to 7-502, Md. Comm. Law Code § 14-201 to 204
Massachusetts	Mass. Gen. Laws Ann. ch. 159, 19E	Mass. Gen. Laws Ann. ch. 93 §§ 24 to 26 & 49
Michigan	Not Applicable	Mich. Comp. Laws Ann. § 339.901 to 920 & 445.251 to 258
Minnesota	Not Applicable	Minn. Stat. Ann. §§ 332.31 to 45
Mississippi	Miss. Code Ann. § 77-3-701to 77-3-737 *et. seq.*	Not Applicable
Missouri	Mo. Rev. Stat. § *407.1076* .	Not Applicable
Montana	Mont. Code Ann. § 30-14-502	Not Applicable
Nebraska	Neb. Rev. Stat. § 86-1201	Neb. Rev. Stat. § 45-601 to 620
Nevada	Nev. Rev. Stat. Ch. 599B	Nev. Rev. Stat. §§ 649.005 to .435
New Hampshire	N.H. Rev. Stat. Ann. § 359-E:1	N.H. Rev. Stat. Ann. § 358-c:1 to c:4
New Jersey	Not Applicable	N.J. Stat. Ann. § 45:18-1 to 6.1
New Mexico	N.M. Stat. Ann. § 57-12-22	N.M. Stat. Ann. § 61-18A-1 to 33

State Consumer Protection Laws Quick Reference II		
STATE	**TELEMARKETING**	**DEBT COLLECTION STATUTES**
New York	N.Y. Gen. Bus. Law § 399-P	N.Y. Gen. Bus. Law § 600 to 603
North Carolina	N.C. Gen. Stat. § 66-260 *et. seq.*	N.C. Gen. Stat. § 58-70.90 to .130 & 75-50 to 56
North Dakota	N.D. Cent. Code Ch. 51-18	N.D. Cent. Code § 13-05-01 to 10
Ohio	ORC Ann. 4719.01-20	ORC Ann. 1319.12
Oklahoma	Okla. Stat. Ann. Tit. 15 § 775A	Not Applicable
Oregon	Or. Rev. Stat. §§ 83-710, 646.551	Or. Rev. Stat. § 646.639 to 656 & 697.005 to .095
Pennsylvania	Pa. Stat. § 2241 *et. seq.*	Pa. Cons. Stat. Ann. 18 § 7311 & 73 § 201-1 to 9.2
Rhode Island	R.I. Gen. Laws § 5-61-1 *et. seq.*	Not Applicable
South Carolina	S.C. Code Ann. § 16-17-445	S.C. Code Ann. § 37-5-108
South Dakota	S.D. Codified Laws Ann § 37-30A-1 *et. seq.*	Not Applicable
Tennessee	Tenn. Code Ann. § 47-18-1526	Tenn. Code Ann. § 62-20-101 to 126
Texas	Tex. Bus. & Com. Code Ann. §§ 44.001 to 44.253 *et. seq.*	Tex. Rev. Civ. Stat. Ann. § 5069.11.01 to 11 & Tex. Fin. Code § 92.001 to 404
Utah	Utah Code Ann. §§ 13-26-1 *et. seq.*	Utah Code Ann. §12-1-1 to 9
Vermont	9 VT. Stat. Ann. § 2464 to 2464d	Vt. Stat. Ann. tit. 9 § 2451a to 2462
Virginia	Va. Code § 59.1-21.1	Va. Code § 18.2-213
Washington	Wash. Rev. Code § 13-26-1 *et. seq.*	Wash. Rev. Code Ann. § 19.16.100 to .950

State Consumer Protection Laws Quick Reference II		
STATE	**TELEMARKETING**	**DEBT COLLECTION STATUTES**
West Virginia	W. Va. Code § 46A-6F-101	W.Va. Code Ann. § 47-16-1 to 5 & 46a-2-122 to 129a
Wisconsin	Not Applicable	Wis. Stat. Ann. § 218.04 & 427.101 to .105
Wyoming	Not Applicable	Wyo Stat. § 33-11-101 to 116

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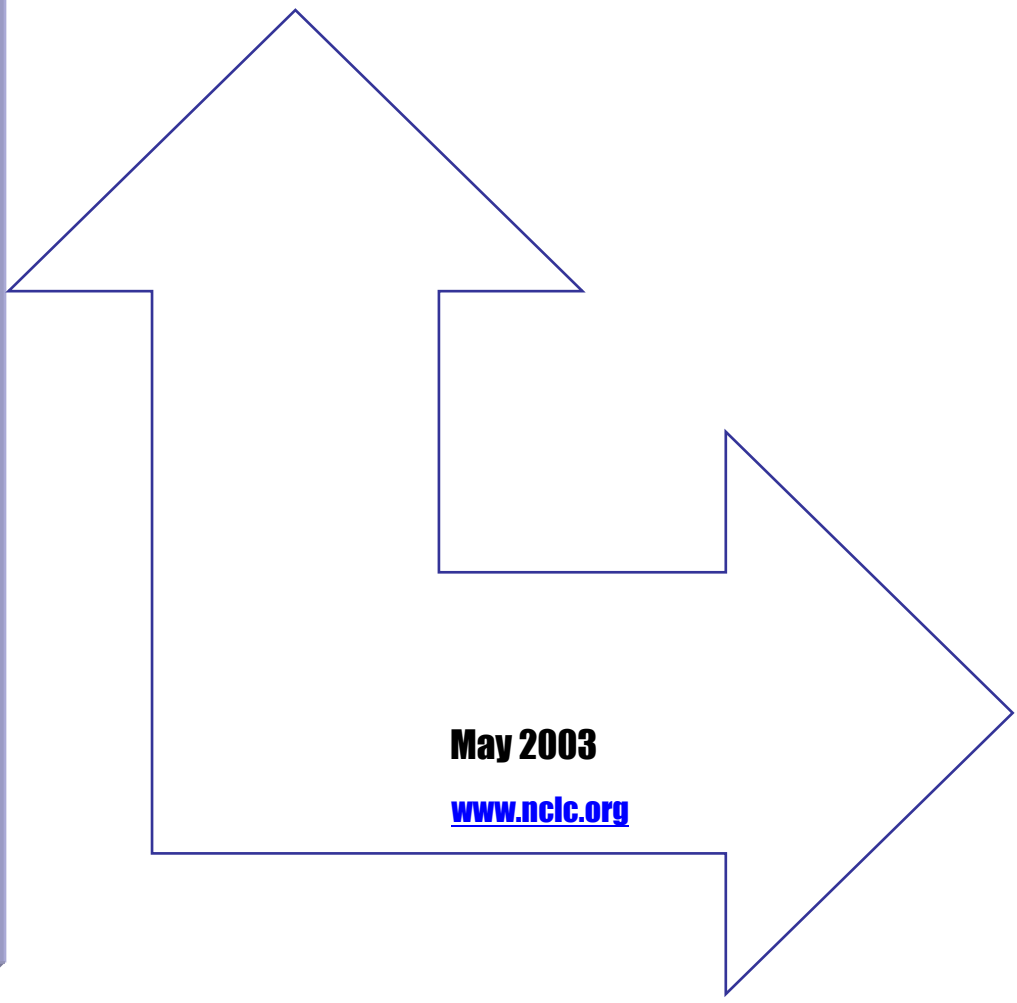
A National Consumer Law Center Report

IN HARM'S WAY – AT HOME:

Consumer Scams and the Direct Targeting of America's Military and Veterans



May 2003

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Consumer Scams and the Direct Targeting of America's Military and Veterans

A Report by
National Consumer Law Center
May 2003

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National Consumer Law Center is a non-profit organization with 35 years of working experience in consumer issues, especially those affecting low-income consumers. NCLC works with and offers training to thousands of legal-service, government and private attorneys, as well as community groups and organizations representing low-income and elderly people. Our legal manuals and consumer guides are standards of the field and can be ordered directly through our website.

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Copies of this report are available by mail for $30 each paid in advance (checks only), or by downloading from NCLC's website.

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FINDINGS AND EXECUTIVE SUMMARY

- Scores of consumer-abusing businesses directly target this country's active-duty military men and women daily. Military people citing numerous examples tell NCLC that clusters of these businesses exist near every base's gates -- an observation in line with what NCLC found on its own visits to three bases. **National Consumer Law Center's analysis finds many of these businesses violate the law or have far higher costs than are generally available elsewhere to the same consumers.**

- Veterans are targeted too, by an often-expensive scam where streams of their military benefits payments are purchased for a lump sum. The effective interest rates veterans pay for these buyouts are often very high. A National Consumer Law Center analysis, requested by Congress, of several such deals finds not only that those deals were very expensive but, more importantly, that **any such purchase of veterans' benefits is illegal under a federal law prohibiting assignment of those benefits.**

- Military personnel are ripe targets for consumer predators because many are low-income (always the most-targeted group) but have a far longer list of economically-attractive qualities than most low-income people. Periods of deployment like those for the recent war in Iraq are especially vulnerable times. And military conduct codes that stress the need for orderly personal lives, including orderly finances, may inadvertently be driving service people toward the quick fixes many consumer predators offer.

- Consumer-unfriendly businesses get *inside* bases by skirting on-base solicitation curbs and via ads in military newspapers. The nationally-published and widely-read military "Times" newspapers are apparently thought to be "official" by substantial numbers of service people even though they aren't, leading some to trust those papers' advertisers more than they otherwise might.

- "Affinity marketing" using military-sounding names, military symbols and ex-military people in sales and executive capacities further clouds the identities and goals of many businesses military people would do better to avoid.

- Military leaders are concerned that widespread financial stress in the ranks, a documented problem many of them partly attribute to scams, may be impacting readiness.

- Regional efforts to combat consumer scams aimed at the military have sprung up at bases around the nation and show some promise as a template for wider actions.

- Military leaders had decisive impact in at least one statewide battle to rein in predatory lenders who harmed their people. They've begun speaking out about predatory businesses and unfair or deceptive business practices in several states, tapping a previously-unrealized level of credibility, moral authority and clout in states where bases are a major economic force. But businesses that prey on service people have very powerful lobbying arms and are often stronger politically.

- Veterans' benefits buyout deals have attracted substantial attention from Congress and opposition from veterans' groups. The Senate passed a useful bill explicitly banning such deals last year – but it's important to note again that NCLC attorneys believe these deals are already illegal under existing law.

- The military is aware it needs to greatly bolster financial literacy training, including education about scams, but these efforts still have far to go.

RECOMMENDATIONS

- The numerous instances of law-breaking documented in this report point first to a need for far stronger enforcement of existing laws and pursuit of law-breakers. The military has a crucial role to play in more aggressively protecting its people through legal work, public advocacy, education and expanded use of existing military regulations like "off-limits" rules. The Federal Trade Commission, state attorneys general and private lawyers can also do more.

- Consumer protections must also be greatly expanded and protected. A federal law covering everyone, military and civilian, that sharply curbs predatory lending is a minimum first step. Amending the Soldiers' and Sailors' Civil Relief Act to cap interest rates on loans entered into during military service would sharply curb many harmful practices documented in this report. The problems outlined here are best addressed with comprehensive federal legislation for several reasons, but strong state and local laws would also be progress.

- Even though NCLC attorneys believe that veterans' benefits buyouts are illegal under existing law, the federal law prohibiting those deals can be usefully expanded and clarified as well as better enforced.

- The military must also address an aspect of its culture that inadvertently aids consumer predators: the notion that financial trouble means career trouble.

- Military consumers should learn that they can often get far less expensive credit than they're being offered. They should head first for credit unions, base financial counselors or military relief societies when money is an issue. They must also learn more about fundamental financial management and avoiding scams in the modern, less-regulated financial marketplace. This report contains a starter's list of basic suggestions for consumers.

INTRODUCTION

A torrent of consumer-abusing businesses directly target this country's military men and women daily. There are predatory lenders, check cashers, high-cost car dealers, overpriced insurance sales and more that we'll detail in this report.

Every military installation we visited or spoke with is ringed and infiltrated by a breathtaking assortment of these scams. And veterans are being targeted off-base by an exceptionally expensive scam aimed specifically at them. National Consumer Law Center's analysis of these scams shows that many of them violate the law, often through unfair or deceptive business practices, or have far higher costs than are generally available elsewhere to the same consumers.

This report is aimed at bringing these issues and ways of dealing with them to the attention of the public, the Congress, the news media, the legal community (especially the military legal community) and consumers. It documents:

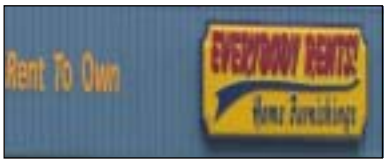
- The scope of the problems
- Why military personnel are especially ripe targets for these scams
- How these scams often fail to stand up to legal scrutiny
- The military's difficult and under-resourced struggle to control them

It also includes specific recommendations.

This report is only a start. It outlines potential legal, legislative, regulatory and educational paths to be followed. Given what's revealed here one hopes all four will be pursued, and we hope to do our part.

PART 1: TARGETING THE ACTIVE-DUTY MILITARY

I. THE VIEW FROM ROUTE 40 -- KINGSLAND AND ST. MARYS, GEORGIA:



Route 40 in Georgia's far southeast corner is the main road to the Kings Bay Naval Submarine Base. It's a four-lane boulevard off Interstate 95 that, with a turn onto the Route 40 Spur, leads directly to the base's two gates.

Base workers and their families conduct virtually all their everyday business here. Routes 40 and Spur 40 are thick with the standard fare of American commerce – restaurants, supermarkets, department stores and self-service gas stations.

They're also thick with businesses you *won't* find in many American communities. On this one road, near this single base, we found these:

- Kingsland Auto Pawn ("Cash on Car Titles")
- First American Cash Advance
- Advance Til Payday/Georgia Catalog Sales
- Pioneer Military Loans
- The Money Tree ("Fast Cash Loans/Tax Refund Loans")

- AAA Title Pawn & Gun ("Cash Advance - We Loan on Anything of Value")
- "Buy Here, Pay Here" used car dealer KDS Auto
- Camden Services Inc. ("Ask Us About a Tax Refund Loan")
- An H& R Block tax service advertising "instant money"
- $peedy Ca$h Title Pawn ("You Keep the Car")
- Everybody Rents! Home Furnishings (a rent-to-own furniture store)

Now, these types of businesses are hardly unknown to low-income communities. And with military salaries in the six lowest ranks -- nearly three-quarters of all active-duty military personnel[1] -- barely topping $30,000 a year and for most much closer to $20,000, many military families are low-income.

But even for low-income communities the sheer ubiquity of these businesses around bases is something that might shock families elsewhere. While we can't speak to the specific practices of each business listed above, we can say they're of types often known to be notoriously poisonous to consumers.[2]

The Kings Bay region is no anomaly. Cross the border into Florida, and the final two miles of Mayport Road that dead-end at Naval Station Mayport are another economic minefield. Drive 25 miles more to Naval Air Station Jacksonville and the story's the same.

Experienced military people from all service branches tell NCLC these sights are the rule everywhere they've served. "You must not know much about the military," chides Betty Hammack, a Defense Department employee who's worked at Air Force bases in six states. "Anytime you walk out the front gate of an installation you're going to find those businesses –

[1] Active-duty military personnel in the six lowest ranks total 1,041,697 of the 1,414,454 active-duty personnel, or 73.63%. Source: Department of Defense chart "Active Duty Military Personnel by Rank/Grade, February 28, 2003."
[2] For ease of reading, detailed descriptions of many consumer scams commonly aimed at the military can be found in Appendix A of this report.

the payday loans, high-interest rate commercial finance companies, car title lenders, pawn shops. You can find them anywhere."[3]

A Phone Call to Georgia Catalog Sales

St. Marys, GA, March, 31, 2003

(After visiting St. Marys, National Consumer Law Center Advocate Steve Tripoli phoned this business posing as someone interested in a loan and earning $1,400 a month:)

ST: I drove by your place the other day and was wondering how I can get that $500 instant cash (advertised in large letters on the window.)

CLERK: Depends on your income – bring in your pay stub. Are you military?

ST: No, I'm not -- I make about 1,400 a month.

CLERK: Well, once we verify your employment I would let you write (an instant-cash agreement) for $350 and you'd get $105 worth of catalog certificates. Instead of charging interest we do it that way. It's not a loan or anything.[4]

ST: So, how do I do this?

CLERK: You write a check for $455 (in order to get $350 instant cash) and we only hold it til your next payday. You can come in on payday and pay the amount on the check and we'll give you the check back, or if not we cash the check but we don't like to do that.

ST: What's for sale in the catalog?

CLERK: Oh, I'm not sure (moves away from phone to consult co-worker, then returns). We have some figurines, and a couple of leather jackets that someone returned because they were the wrong size.

NCLC ANALYSIS: In light of a recent court decision this company appears to be in the business of making loans at illegal rates under Georgia law.

In an early stage of the "Cashback Catalog Sales v. Price" case,[5] a Georgia federal court found -- despite claims similar to those we heard on the phone here – that another Georgia "catalog sales" business appeared to be primarily involved in lending. The court further stated: "it is unlikely that a reasonable mind could come to some other conclusion."[6]

And the court agreed with Mr. Price that the catalog certificates he was issued were a sham, saying: "a reasonable trier of fact could conclude that the amount of the gift certificates are (in substance) usurious interest" – in part because the goods they could buy would be so overpriced as to make the certificates virtually worthless.

Assuming the catalog certificates we were offered in our phone call are never cashed, which military sources tell us is quite often the case with these businesses for a host of reasons, a two-week loan of $350 carrying $105 interest generates an interest rate of 30% *every two weeks* -- or an annual percentage rate (APR) of 780%.

[3] Ms. Hammack currently works at Randolph AFB near San Antonio, Texas.

[4] This is a statement often made by payday lenders skirting the rules governing legally-defined loans.

[5] 102 F. Supp. 2d 1375

[6] Other courts have looked behind the bells and whistles of a transaction and found that the consumer actually got a loan. See, e.g., Turner v. E-Z Check Cashing, Inc., 35 F. Supp. 2d 1042 (M.D. Tenn 1999) ("check cashing" was really payday lending); Hamilton v. HLT Check Exchange, 987 F. Supp. 953 (E.D. Ky. 1997)(same); SAL Leasing, Inc. v. Arizona ex rel. Napolitano, 10 P.3d 1221 (Ariz. App. 2000) ("sale-leaseback" of car really a loan); State ex rel. v. The Cash Now Store, Inc., 31 P.3d 161 (Colo. 2001) ("assignment of tax refund" really a loan).

II. WHY TARGET THE MILITARY?

Why are military personnel such ripe targets for consumer predators? The short answer is that they have a far longer list of economically-attractive qualities than most low-income people.

In other low-income communities predators are drawn to the high number of people who have trouble getting credit, lack economic sophistication, and have a high prevalence of debt problems resulting in part from those factors.

But military communities have a greatly-expanded list of such vulnerabilities, including:

- Higher-than-average numbers of economically-unsophisticated young adults, away from home for the first time and anxious to experience new things.
- A working population that universally receives U.S. Government paychecks on a rock-solid schedule – a golden guarantee to the payday lending industry especially -- and that is in no danger of being laid off.
- A population that's easy for debt collectors to track.
- A military culture that urges people to keep their finances in order as part of good conduct codes – a culture, as we'll see, that is heavily exploited and whose penalties are greatly exaggerated by some predators targeting the military.

By all accounts significantly more of today's young military personnel than previous generations are married as well, increasing the economic pressures they face. Retired Navy Capt. Bill Kennedy, a former aircraft carrier commander who now heads Naval Station Mayport's branch of the Navy-Marine Corps Relief Society, says many young military people walk a razor-thin economic line.

"An E-3 (one of the lower ranks), married with one child, after base pay and other allowances has no money left at the end of the month. Zero," says Kennedy. "There's no

money for restaurants. No money to go to a movie or buy presents. A car repair or even a little mismanagement can wreck 'em. And the reason these businesses target the service member – and they won't say this – is they know what the pay is. And they know that, no matter what, those kids are paid on the 1st and 15th of every month, and they're not going to be laid off. They're easy targets."

Easy targets for the "$500 instant cash – NO CREDIT CHECK!" sign emblazoned across the storefront the soldier/sailor/airman has driven by a hundred times. Or the ones that say: "Make Your Next Payday Today" or "Instant Money."

Or, more insidiously, they're targets for the numerous large ads for fast cash and easy loans they've just read in that week's military newspapers. The nationwide ArmyTimes, NavyTimes, AirForceTimes and MarineCorpsTimes newspapers are NOT published by the military – they're independently published by the Gannett newspaper group. But many people told NCLC that substantial numbers of military personnel believe them to be "official" newspapers, and therefore believe their ads have been vetted to screen out undesirable businesses.[7]

These newspapers and their omnipresence *inside* military bases present special problems when it comes to consumer predators' access. Retired Capt. Dave Faraldo, head of the Navy-Marine Corps Relief Society's NAS-Jacksonville branch, puts it this way: "A Navy person, using a Navy office, on Navy time, with a Navy phone can do business with one of these companies they see advertised – after he found out about it by reading the Navy's newspaper."

The military in fact has virtually no control over these papers' advertising, a source of discomfort to many military commanders.

[7] See examples of these ads in Appendix B. It should also be noted that these same businesses have a heavy advertising presence on the "Times" newspapers' websites.

"I Just Kept Coming Up Short"

Anthony G., who didn't want his last name used, has already logged 10-1/2 years of Navy service though he's just 28.

"I got into trouble with the check cashers starting about two years ago," he says. "We were behind on bills and I was going through a divorce and I needed money."

That led him to Jacksonville Catalog Sales for a very small cash infusion. "You write 'em a check for $125 and they give you $100 cash," says Anthony. "The check's cashed on your next payday in two weeks. I got the (catalog) coupons but I just threw 'em away, I never even looked at them. I just didn't want to mess with them." [8]

This tiny loan seemed like a temporary expedient to Anthony, but like so many predatory loans it turned into something much worse. "I'd be short again on payday," he says, "then I'd go get a second one. I ended up going to more and more places because I just kept coming up short."

Each time, Anthony's agreement would give the lenders electronic access to his bank account for payment.

"I think there were 10 loans altogether when I was done," he says, with one being used to pay off the other. "It was, like, $100 to $150 in some places but in others it was $300 covered by a check for $388 [annual percentage rate 762%], or $400 covered by $475 [APR 487%]."

The house of cards of course collapsed. "It was definitely affecting me and my family as far as food, rent, and making us feel pretty crappy," says Anthony, who reluctantly went to his commander. He was referred to a lawyer, and Anthony then decided to close his credit union account to bar lenders' access to his money while things are worked out. [9]

The overall situation isn't resolved yet but Anthony says one thing is: "I learned to get a loan from the bank if I need one."

He's right about that for three reasons: A bank loan would be more affordable, it would allow payments to be made over time, and traditional lenders are far more likely than predatory lenders to screen out people who can't really afford loans.[10]

III. TAKING THE BAIT: CAREER WORRIES, DEPLOYMENT AND OTHER REASONS SERVICE PEOPLE BUY INTO SCAMS

It's easy to claim, as apologists for consumer scammers often do, that many military people who get involved with these scams do so with their eyes open. To be sure some do – and even many who were naïve or misled are strikingly willing to take their lumps and say they'd learned a hard lesson.

But there are more compelling reasons why military people take part. One factor specific to the military is the fear that disorder in one's personal finances can be career-

[8] Assuming the coupons aren't cashed – which for many reasons they often aren't -- a $25 interest charge for two weeks on $100 loaned equals an annual percentage rate (APR) of 650%. See Appendix A for reasons why catalog coupons, and other services sold to thinly disguise payday loans, are often not used by the consumers.

[9] It's telling that one of Anthony's lenders has cancelled his loan and paid a small settlement just on threat of a lawsuit.

[10] Predatory lenders may in fact have a perverse incentive to grant loans to bad credit risks: the chance of sucking them into a repeat-lending cycle, generating profits that far outweigh potential losses from default.

damaging. As stated earlier, military codes of conduct call for orderly personal lives – specifically including orderly finances. This creates an incentive to chase quick fixes when finances start slipping: Signs of trouble can be and often are reported to commanding officers by creditors.

"I get calls from higher-ups all the time," says Florida Legal Services attorney Lynn Drysdale, who represents many military people ensnared in consumer scams. She says her military clients "are just sitting ducks for bill collection" and the frequently intimidating tactics of bill collectors because they're easy to track and any time they fall behind on their debts a creditor or debt collector can contact their commander.

What many soldiers and sailors don't realize is that isolated instances of financial trouble almost never trigger military discipline. Some creditors work hard to create the opposite impression. Drysdale and others gave NCLC copies of loan contracts from Delaware-based Military Financial Network Inc. that prominently mention possible punishment, for instance.[11] After outlining the loan's payment terms one of the company's "Repayment Agreement" documents states:

> **"If I fail to provide these funds, I understand that this will be a violation of Article 123a and 134 of the UCMJ (Uniform Code of Military Justice), punishable by up to 6 months confinement, forfeiture of all pay and allowances, and a bad conduct discharge…..I authorize the Military Financial Network to contact my military superiors in these matters."**

That type of language, which NCLC attorneys believe is illegal in and of itself,[12] angers Retired Adm. Jerome Johnson. He's head of the Navy-Marine Corps Relief Society, which deals with many of those driven to seek assistance after becoming ensnared in consumer scams.

[11] See a copy of one such document in the Appendix B.
[12] NCLC attorneys believe this language unquestionably violates Unfair and Deceptive Acts and Practices (UDAP) standards and therefore should be referred by military officials to the Federal Trade Commission. It should also be specifically prohibited from future contracts.

Sure, says Johnson, financial problems *could* trigger action from superiors, but in all but serious repeat-offender cases "that is just not what a commander does." The far more likely response is to refer the troubled service person for financial counseling or legal help. The contract language "is there to intimidate and coerce," Johnson says.

If that's its purpose the language seems to work. Lynn Drysdale says that when some of her military clients fall behind on their debts "what happens is they're so afraid of what's going to happen next that they go to another payday lender to pay the first loan. I've seen clients so scared they spend a full day going from lender to lender," rolling one loan into paying off the next in a debt spiral that's virtually guaranteed to end disastrously.

So the fear of career damage can perversely drive a military person further into the arms of the scam artists. "With the military," says Drysdale, "the creditors have this extra hook."

The regular upheavals of military life can spring financial traps leading to consumer scams as well. Times of deployment, like the recent call-ups for the war in Iraq, can be especially vulnerable moments for lower-income military families, says Naval Station Mayport's Relief Society head Bill Kennedy.

"They're trying to get everything caught up, buy all the things the person going away needs to buy, there's a lot of stress, and the spouse left behind may not be the one normally in charge of finances," says Kennedy. "The paycheck's split, too," with some of it going to the service person's small needs on board ship or overseas.

Kennedy tells of one young military wife who came to the Relief Society frantically worried about her entanglement with a payday lender. As he describes her plight, this 30-year veteran who once commanded an aircraft carrier's awesome power twice stops to recover his

choked-up voice. "She was so proud of her husband, who was on deployment," he says, "and she was scared to death that she'd failed him."

"These Sailors Had Better Be Careful"

Peter Kahre recently retired from the Navy after 20 years but hasn't yet retired a predatory lending problem that started in 1996 and led him into bankruptcy.

It all started with a simple deployment to sea duty. The "basic sustenance" portion of his paycheck was reduced by $197 a month while his food was being provided on-board. That plus the arrival of a new baby were enough to upset the family's finances.

Kahre went to a "Cash Back II" store near his Jacksonville base, receiving a hundred-dollar cash advance secured by his $125 personal check. The money to cover that check wasn't there the following payday because of other bills, and Kahre's downward spiral began.[13]

"It just started snowballing to the point where I had nine of 'em [payday loans] with nine different ones. Every payday I'd get off work at 3:30 in the afternoon and go from one to the other, rolling them over and re-writing them again. By the time I got home it would be 6:30 at night."[14]

Kahre estimates he paid back $20,000 on loans for which he received just $2,000 to $3,000 before things came crashing down into bankruptcy.

"You talk about someone the system took advantage of, I was the idiot. You get into it thinking you can get out of it real quick, and some people can and some can't."

Kahre says fear of being reported to superiors kept him paying long after he knew things were out of control. "See, if you miss even one payment on this they'd either contact your CO (commanding officer) or send a nasty-gram."

He says one collection agency even harassed his mother in Missouri. "They called claiming they were the 'state attorney's office,' wanting to know where I was at. They said if she didn't tell they'd arrest her, bring her to Florida, and leave her in jail until she told them where I was."[15]

Kahre still hasn't settled all his problems. "All I can say is these sailors had better be careful," he says. "There are a lot of people who will take advantage of you whether they know it or not."

Other factors make increasing numbers of today's military vulnerable to scams. Chalker Brown, vice president of Jacksonville's 300,000-member VyStar Credit Union, says many young people entering the service these days may be doing so in part *because* they're financially at-risk. "Many more are married, they aren't making it on the outside and credit problems are almost the norm," Brown says. "These kids are over their credit limit, their

[13] One insidious practice encountered while researching this report, though not in Mr. Kahre's case, was an instance of a payday lender electronically dunning a borrower's checking account 10 times on a single payday when money owed wasn't there – each time triggering a $25 penalty fee for a total of $250.

[14] The fact that many payday borrowers take multiple loans each year debunks the industry's contention that the loans aren't harmful because, high interest rates and all, they're a small and infrequent convenience. See Adm. Jerome Johnson's references to payday borrowers' lending frequency in his letter to the North Carolina legislature, in Appendix B. Also, as of last October Florida law prohibits any individual's having more than one payday loan at a time, or taking out a new payday loan within 24 hours of terminating another one.

[15] Behavior fitting this description is a gross violation of the federal Fair Debt Collection Practices Act.

account's been frozen, or they have no credit at all. So after being turned down (for lower-priced credit) numerous times it may be they've been burned so much they just don't ask anymore. Or they just see a simple solution when they see those storefront signs when they're coming down the road."

VyStar, a credit union with military roots, has its own special window on the prevalence of scams in Jacksonville's military community. Brown says VyStar's two branches nearest to the Jacksonville Naval Air Station recently decided to count the number of post-dated checks brought to the credit union by payday lenders (these again are the checks borrowers write, to be cashed on payday, in exchange for what is usually a very high-interest short-term loan.) In a single two-week pay period Brown says those two branches alone cashed 270 such checks.

When Brown says credit-starved young military people see fast cash as a "simple solution" he's pointing up another aspect of this problem – the "simple" solution is often irresponsibly simple. Financial counselor Pat Kelly at North Carolina's Camp Lejeune says young Marines there are attracted to quick-cash scams because those businesses "don't hold the kids responsible" for having credit good enough to get a loan -- the way businesses following sound lending practices would.

There's no incentive for sound lending practices. Easy money brings in customers, and sky-high interest rates and fees make it profitable to lend to all comers with little regard for their financial state or default risk. After all, a few bad loans at these prices still leave a healthy bottom line -- and the wreckage to individual lives and families is someone else's problem.

IV. AFFINITY MARKETING: THE "WHOLE LOT OF AUTHORITY" IN IMPLIED MILITARY TIES

Two more aspects of this targeting of the military deserve consideration. The first is the number of private companies using names that imply a military connection. Some examples targeting both active-duty military and veterans include:

- Force One Lending Inc.
- Armed Forces Loans
- Loans for Military
- Military Financial, Inc.
- Pioneer Military Lending
- Retired Military Financial Services
- Veterans First Financial Services
- American Military Debt Management Services

The list is hardly exhaustive. Military and former military personnel tell us that some of these companies' principals or high-visibility representatives are former service people as well, a source of anger to many still serving.

Like military-sounding names, these *human* military connections are also exploited in marketing high-cost goods and services to military people, or goods and services of questionable utility. Marketing experts refer to this use of people who hail from the targeted group as "affinity marketing."

Air Force Col. Marcus Beauregard, who oversees a service-wide financial literacy program at the Pentagon, tells of a report he received from commanders at Lackland AFB in Texas about insurance salespeople – many of them former military. On-base solicitation rules

ban them from bases so they station themselves along San Antonio's popular Riverwalk, a magnet for tourists and off-duty military.

It's easy to pick out the young airmen and women even in civilian clothes, and easy for salespeople who've experienced military life to strike up a conversation. "They come across with a whole lot of authority," says Col. Beauregard, but the real purpose of the faux-comradeship is to sell whole-life insurance policies with premiums of $100-125 a month.

The policies are real but this expenditure of a substantial chunk of many military paychecks is often unnecessary. Why? All military members have access to government-sponsored Servicemembers' Group Life Insurance, where coverage can be had automatically for about $12 a month. The products aren't identical – the whole-life policies do have a savings component, for instance – but the higher-price policies aren't a purchase many financial planners would recommend to young people who already have good life insurance.

And many of those who buy these over-priced policies already do have SGLI, says Beauregard. So what drives them to buy the more-expensive policy?

"Because someone talks them into it – someone with credibility," he says. "They say 'this is something you need for your future.' They get sold that this is a way of putting your money away. It's savings. It's an investment."

An insurance-related scam using similar "affinity" tactics was reported to NCLC by commanders of the San Diego region's Navy and Marine Corps bases. According to an e-mail from Lt. Mei-ling Marshall of military Legal Assistance, a company called Trans-World Assurance that "claimed to be a non-profit organization providing financial services exclusively to active-duty military" has been operating there.

Lt. Marshall continues: "Its representatives go to some mid-level command official and offer to give no-cost GMT (general military training) to captive command audiences, and

then rely on Sailors to 'pass the word.' In reality, in certain circumstances the non-profit organization operated as an umbrella 'for-profit' life insurance company, thereby running afoul of DoD directives regarding improper solicitation on base." Lt. Marshall says she recently cautioned commanders of a ship heading for deployment to check the background of another life-insurance company offering an on-board presentation to departing sailors.

Affinity marketing is also highly visible in the promotional materials of companies targeting the military – companies consumers might well be better off avoiding.

Pioneer Services, for instance, uses an American-flag background on the cover of a promotional booklet and prominently quotes retired military figures inside. The overall theme is Pioneer's devotion to military families' financial well-being -- a devotion that might be called into doubt on examining a high-cost lending agreement from one of the company's partners.[16]

V. FINANCIAL STRESS AND MILITARY READINESS

Some military leaders have begun to question whether military readiness is impacted when large numbers of their people are struggling with financial distress and the weight of high-cost loans in particular. Rear Admiral David Architzel, commander of the Navy's 83,000-person Mid-Atlantic Region, recently told the TV news magazine "Inside Edition" when discussing his command's struggle against payday lending:[17] "You want to know that (service men and women) are focused and paying attention. When they are not paying attention bad things happen."

[16] See agreement for a high-interest, fee-laden Pioneer loan in Appendix B.
[17] The segment aired July 22, 2002.

Former aircraft carrier commander Bill Kennedy agrees. "If it's a dangerous job, like loading ordnance, and his or her mind is on 'doggone it, back home they're going to take [re-possess] the car,' they're not doing their job correctly, and there's a potential for an accident."

And Ret. Adm. Jerome Johnson, head of the Navy-Marine Corps Relief Society, told the North Carolina legislature that in the case of payday lenders in particular "the negative impact on military readiness is profound."[18]

"It Just Drove Me Into the Ground"

Marine Sgt. Robert Farris had been stationed in Phoenix for a year when unexpected bills came up, and he remembered the "Cash One" store near the Marine Corps Reserve Center where he's on the active-duty staff.

"I saw them (the quick-cash shops) on the corner, they were there, and I went," he says. Since his credit rating "is not great," Farris says, "it came down to the lesser of two evils."

Or so he thought. Over 12 months, a $125 loan became a long-running series: a $170 loan costing "about" $220 to re-pay in two weeks, then ever-larger loans, and finally a 10-day, $500 loan costing $587.50 to re-pay. The "deferred presentment agreement" offered by Amos Financial, LLC, stated the annual percentage rate – 638.75%.

"I saw the error of my ways in month two of the twelve months but I couldn't get out of it," Sgt. Farris says.

By the end, Farris believes he borrowed close to $10,000 in dribs and drabs, never pocketing much because most all of it went to paying off previous loans.

His total payments? "Oh my goodness. Huge," is all he'll say.

"It just drove me into the ground," he says a year after taking that fateful first loan. "I was about to get my car re-po'ed (re-possessed) and just now I have it worked out so all the debt collectors understand what was happening.

"I've never been a drug addict, but it's kind of like smoking and you want to quit but you're captured and you have no choice. It really starts to hurt because when all's said and done you're having a hard time feeding your family. I've got a new family and a new baby and I thought: 'I didn't drag my wife all the way out here (to Phoenix) to put her through this.'"

How does he feel about the whole experience? "In my opinion, if you're speaking to higher-level commanders in Washington," he tells this report's authors, "I think it should be illegal for service members to do this. I was making almost $3,000 a month as a sergeant – not bad money -- so if some junior troop gets into this it'll destroy him financially in no time."

VI. MILITARY RECOGNITION OF THESE PROBLEMS, AND RESPONSES THAT HAVE MET WITH VARYING SUCCESS

Driven in part by worry that "financial problems have impacts on readiness and productivity," the military has begun taking a closer look at overall financial awareness with a

[18] See Admiral Johnson's letter to the legislature in Appendix B.

special eye toward consumer scams and their impact. The Defense Department's March 2002 "Report on Personal and Family Financial Management Programs" – from which the quote above is drawn -- says more than half of all service members in the lowest six pay grades describe themselves as having at least occasional difficulty (and often worse) making ends meet.

"Many young enlisted members do not anticipate the consequences of acquiring debt or paying off debts at high interest rates," says the report. "Easy availability of credit and credit cards makes it possible for members to live beyond their means for a while, but the short-term extravagance then creates a crisis to pay off bills."

All four branches of the service offer financial training as part of basic training, with the Army, Navy and Air Force each covering at least nine of 10 financial topics listed in the report. The Marine Corps falls short here, covering only two of the 10 topics and leaving out such fundamentals as "establishing savings," "credit management" and "consumer scams."

Individual bases, credit unions,[19] the various branches' assistance programs and some non-military counselors add to the financial literacy mix, but Pentagon financial literacy coordinator Col. Marcus Beauregard is blunt in saying "we have a lot further to go." The Department of Defense report outlines several paths to improving or increasing financial training.

And the DoD is paying special attention to scams. Last December, it joined the Federal Trade Commission in launching the Military Sentinel Web site. The site, which is slowly coming into full operation, allows military personnel to directly report consumer complaints for investigation and also offers consumer education.

[19] Navy Federal Credit Union, the nation's largest credit union with two million members, offers free budgetary counseling to all members as one example.

In the meantime individual efforts to combat consumer scams aimed at the military have sprung up across the nation. Some examples:

- Army commanders in the Fort Campbell, Kentucky, area negotiated a "Code of Ethics" with nearby auto dealers in response to problems ranging from overcharging to misleading buyers about warranties.[20] Dealers who sign onto the code get "preferred billing" acknowledging their commitment, and Betty Geren of the base's Financial Readiness Program says complaints about dealers have dropped between 75 and 80 percent since the program began.
- A five-year campaign to rein in the excesses of Florida's automobile "title pawn" lenders[21] turned decisively on the military's intervention, says Florida Legal Services' Lynn Drysdale. An effort to change the legally-permissable 264% annual interest rate on these loans had bogged down, Drysdale says, because of industry contributions to key legislators. But when the military got involved "it changed the whole complexion of the issue." Commanders and others went to Tallahassee to testify to the personal destruction they'd seen such loans wreak – debunking industry claims that such lending is a service to those who cannot otherwise get credit -- and eventually the maximum interest rate on title-pawn loans was knocked down to 30% a year.

  The campaign had one delightful and one perverse outcome. Apparently not satisfied to lend out money at a mere 30% interest, the title-pawn industry all but dried up in Florida. But just over the border near the Kings Bay Submarine Base in Georgia "you would not believe it," says Gail Tate of the base's Relief Society branch. "Within days,

[20] Auto dealers and repair shops near bases nationwide pitch special deals that often aren't so special directly to military personnel. There are also substantial problems near bases in some regions with so-called "buy here/pay here" used-car dealers whose modus operandi are detailed in Appendix A.
[21] See description of title-pawn lending in Appendix A.

literally (of Florida's passing the new law), they were opening up here, just over the state line."

- Military leaders have begun taking part in other legislative campaigns as well, or have asked military judge-advocate's offices to open discussions with businesses thought to be causing problems. In some cases those discussions led to companies voluntarily rescinding onerous contracts.[22]
- Jacksonville-area base personnel, frustrated by advertisements for high-priced loans and other scams in their local base newspapers, countered in those papers either by having (in one case) a base commander order such lenders to prominently display their annual interest rates in ads (resulting in many of the ads being discontinued) or by drafting their own "counter-ads." The counter-ads, designed to look like those from the lenders, prominently displayed such slogans as "0% On Any Loan" – the true rate charged for Relief Society emergency assistance – or, "We'll cash no check before its time!" – a reminder that the Society can straighten out family budgets without demanding post-dated "payday" checks in return.[23]
- The joint command of the San Diego/Orange County-area bases in California is among those that have placed businesses charging super-high fees for goods or services "off limits" to military personnel. Capt. Cory Picton of that region's Armed Forces Disciplinary Control Board says a business "doesn't have to be illegal" to be placed off-limits. Board regulations give commanders wide discretion to do so if they believe, after a proper hearing at which the affected businesses are allowed to take part, that a

[22] See letters to the North Carolina legislature and Florida officials from Retired Adm. Jerome Johnson, and to the Virginia House of Delegates from Rear Adm. David Architzel in Appendix B. The use of judge-advocates was reported by officials in the San Diego area, but military officials in several other places have begun pressuring local businesses that pose problems for service people as well.

[23] See copies of the "counter-ads" and the ads that inspired them in Appendix B.

business may affect "good discipline…..health, morale, safety, morals (or) welfare of armed forces personnel."[24]

- A military-wide code governing solicitation on bases is in the process of being tightened, partly in response to incidents where high-priced insurance salesmen (some of them ex-military) were admitted to bases either by soft-pedaling or misrepresenting their intent with friends inside the military.[25]

[24] Two good examples of results from such actions in this region are the cases of lenders Loans For Military and Armed Forces Loans. Once placed off-limits, military officials say in an e-mail, the two businesses "provided written assurances they would cease and desist their predatory practices and were removed from the off-limits list."

[25] In one incident reported by a Federal Trade Commission staff member an investment products salesman skirted the on-base solicitation rule in a novel way: He hired a bus to pick up members of an entire unit and take them off-base to lunch – a lunch where the main course turned out to be investment-program pitch.

PART 2. REWARD FOR SERVICE: A SCAM TARGETING VETERANS' BENEFITS

Military-sounding business names, "affinity marketing" appeals, and promises of quick cash unfortunately don't end with active military duty. A worrisome and enormously expensive scam – one that can easily cost individual veterans tens of thousands of dollars – is drawing scrutiny from Congress and cries of alarm from veterans' groups.[26]

Welcome to the world of "advance funding" or benefits buyouts, where lump-sum payments are offered in exchange for streams of veterans' benefits that often represent a lifetime of work. These buyouts' workings are simple: A veteran receiving monthly cash benefits needs, wants, or is pitched a quick cash infusion. A private lender offers that infusion in exchange for a fixed stream of the veteran's monthly cash.

The catch? The lump sum is often a rip-off, a horrible deal paying the consumer just a few dimes on the dollar. **These deals are illegal as well**, according to an NCLC analysis discussed below.

"Advance funding" marketing appeals are similar to what we've seen with services targeting active-duty military. The Internet home page of Veterans First Financial Services, for instance, features an undulating American flag, and at the top an eye-grabbing, full-color display of military insignias in motion across the screen. A three-part message flashes over those insignias: "You've worked hard – invest your money the way YOU want – If you're a retired veteran, VFFS, Inc., can help!"

The hints of military affiliations are unmistakable, and the printed message on the home page couched in the language of economic empowerment. It discusses how military

[26] Groups backing new legislation explicitly banning this practice include Disabled Veterans of America, Vietnam Veterans of America, AMVETS and Paralyzed Veterans of America, according to U.S. Sen. Bill Nelson's (D-Fla.) office.

pension-holders "deserve the same benefits many non-military retirees enjoy" – in this case the right to cash out a stream of benefits for a lump sum. The product is called the "Cash-Out Retirement Program," or CORP – another military echo.

One Veteran's Story

Michael Ward Elliott was in a pinch. "My daughter was getting married, I was behind on the rent and other things, and I didn't have the credit rating to go out and get the money I needed elsewhere," says the retired 20-year Navy veteran.

That's when he learned about C&A Financial Programs in an all-too-common way: "They had an ad in the NavyTimes." And before Mr. Elliott knew it he had a deal -- $15,000 cash in exchange for three years' worth of $900-a-month payments from his Navy retirement check – almost the entire check.

That's $32,400 over three years in exchange for that $15,000.

Except it wasn't really $15,000, because Mr. Elliott paid C&A Financial $631.18 from that sum for insurance covering his payments to them should he die. And then C&A took the first two months' payments from the lump sum, meaning he only got $12,568.82.

Now, counting those first two $900 payments in the loan amount, borrowing $14,368.82 and re-paying $900 a month for three years works out to an annual interest rate of over 63%.

"I was rather stupid and I took it," says Mr. Elliott, "but I was in quite a pinch and telling myself, 'let me get out of this spot and see what I can do down the road.'

"Well, it didn't get any better. I got the wolf away from the door but there was less income."

Mr. Elliott was working a civilian job so the pension check fortunately wasn't his only support. "After two or three months debt just started snowballing again. I've never felt quite that stressed out, and I'm not used to that. And my wife was even worse."

The Elliotts asked C&A for a payment moratorium and were told if they tried that they'd quickly be hearing from an attorney. They finally landed in the arms of Navy-Marine Corps Relief and say they've made the tough decision, after paying off the buyout principal and then some, to withhold further payments while awaiting C&A's response. They are getting legal advice.

And that limbo is where things stand as of April 2003.

Elliott says he's learned a few things from the experience. "I would recommend to anybody who asks don't do it, absolutely do not do it (sell your benefits)," he says.

"And I came to find out that the Navy has nothing to do with NavyTimes. Being that the ad was in NavyTimes I thought, surely they must screen the advertising. From what I know when I was on active duty I'd say over 50% of us have the perception that the Navy actually has a say in that newspaper."

Michael Ward Elliott's got lots of company, and not just in his misperceptions about the major military newspapers. You might even call him lucky given the truly horrendous deals going to other veterans who sell their benefits (details below).

Veterans' benefits buyouts have attracted substantial Congressional attention, with the Senate last September approving legislation co-sponsored by Florida Democrat Bill Nelson and Arizona Republican John McCain banning the practice and making it punishable by stiff fines and jail time. Nelson's office says "dozens of companies" are engaged in the business.

The House may be a harder sell, but Sen. Nelson leaves little doubt about his feelings. "People who rob veterans of their retirement should be punished," he says. "Veterans benefits are a reward for serving our country, and they shouldn't be for sale."

There is high-level interest in the House. Illinois Congressman Lane Evans, ranking Democrat on the House Veterans' Affairs Committee, asked National Consumer Law Center to analyze three individual buyout cases. We found all three to be terrible deals for consumers, much like Michael Elliott's detailed above, but more importantly **NCLC's analysis finds that veterans' benefits buyouts, even without new legislation proposed to curb them, are illegal under existing federal law prohibiting the assignment of veterans' benefits.**

The three cases provided us by Rep. Evans' office have the following rather eye-popping provisions:

CASE A: Veteran receives approximately $66,100 – an $80,000 loan minus $10,000 broker's fee and an additional $3,900 insurance premium – in exchange for 10 years' worth of monthly benefits – 96 months at $2,195 a month and 24 months at $1,207. The veteran must also pay a $110 per month "management" fee plus $439 a month into a "pooled investment" fund which may or may not be returned once the loan is paid. By NCLC's calculation that's $302,928 in payments for the $66,100 received – an annual percentage rate (APR) of 49.15% interest.

CASE B: The veteran receives $6,000 initially and then at the *lender's* option two separate loans for an additional $13,500. The three loans carry APRs of 106.21%, 92.22% and 79.82%. The veteran receives a total of $19,500 and pays back $36,637.92.

CASE C: Veteran receives an initial loan of $10,250, with repayment terms of $500 a month for 35 months. According to an addendum signed 10 months into the repayment, the veteran receives an additional $5,000 ($6,000 loan minus $1,000 processing fee) and in return

adds $50 a month to the remaining 25 payments on the original loan while extending those $550 monthly payments for an additional 24 months. In total, this veteran receives $15,250 and pays back $31,950, with an average APR of just over 39%.

These types of transactions are ripe ground for consumer protection-law violations, and veterans who've sold their future benefits for up-front cash may have consumer law remedies as well. Based on the contracts reviewed by NCLC, these lenders often mischaracterize the nature of these loan transactions and fail to provide federally required disclosures.

Federal Truth in Lending Act disclosures exist so that consumers can make informed decisions about the cost of credit. By referring to these transactions as something other than loans (for example one contract explicitly states "This is not a loan," while another characterizes the transaction as a purchase), the lenders attempt to circumvent this important consumer protection law. This is not a new tactic, and courts routinely see through the smokescreen and apply consumer credit laws to such transactions regardless of how they're characterized by the parties.

In addition to Truth in Lending disclosure violations, these lenders may be violating state unfair and deceptive acts and practices (UDAP) laws prohibiting fraudulent, unfair, or deceptive practices in the marketplace. State usury laws placing a cap on allowable interest rates may also be violated.

PART 3. RECOMMENDATIONS

Predatory lending, high-priced goods and services and other scams plaguing military communities drain wallets in ways that destroy the basis for wealth-building, leaving many in those communities permanently cut off from the American Dream. These wealth-destroyers plague all low-income communities, but as we said earlier the military's special attractions make the sheer ubiquity of these businesses around bases something that might shock even low-income families elsewhere.

It seems a funny way to treat those of whom we ask so much.

Experience shows that even sophisticated, highly-educated consumers need protection from those determined to take advantage of them. And the level of vulnerability rises as maturity, education and financial sophistication levels drop. A comprehensive response is needed, including the following:

I. INCREASED ACTION BY THE MILITARY

The military can play a crucial role in cleaning up illegal and unscrupulous practices that prey on military personnel. It can use its authority and resources to expand law enforcement, limit service people's access to certain businesses, target advertisers, and increase financial education and counseling. Such efforts could have a real impact on the lives of service members. Here's a brief look at all four options:

a. Expand Law Enforcement

Military leaders can expand their challenges to the practices of predatory lenders and other abusive businesses targeting their people. By bringing actions on behalf of military people, the Judge Advocate General ("JAG") corps holds national and local businesses accountable for illegal lending transactions and other unsavory deals. Because some

businesses that target the military are national in scope, and their transactions often standardized, even a limited number of legal actions can greatly limit problem practices aimed at the military.

b. Make More Businesses "Off-Limits"

Military leaders can also make more muscular use of their power to designate certain businesses off-limits to service members. This can be done by identifying categories of businesses that should be avoided; naming national chains with standardized, problematic practices; researching local companies with a history of abusive transactions and establishing standards commanders can use to evaluate local businesses.

Some companies clearly break the law. While such firms are obvious candidates for law enforcement actions, in some cases other approaches can also be effective. By barring service members from doing business with such companies the market would quickly dry up -- leaving the company to move or clean up its act.

Military decision makers can be on the lookout for a variety of legal violations. Lenders may be issuing loans without providing proper disclosures under the Truth in Lending Act, or by advertising deals deceptively or including deceptive, harmful terms in their standard-form contracts. Payday lenders may not be complying with state provisions regulating such transactions. Companies also may be skirting state usury ceilings or using abusive collection tactics in violation of state law. Examples of such actions can be found throughout this report. In addition to banning service people from doing business with such companies, military officials should consider referring these companies to the Federal Trade Commission and state enforcement agencies for further action.

The military also has the authority and responsibility to go beyond law-breaking businesses in its efforts to protect service members. As noted above, commanders have broad

discretion to designate a business "off-limits" because it may affect "good discipline . . . health, morale, safety, morals (or) welfare of armed forces personnel." A variety of businesses that target military personnel appear to fit this description. They may "push the envelope" in one state, while violating the standards in another. Payday lenders and cash-advance shops may argue they are following the letter of the law by disguising their transactions as something other than lending. Yet many are effectively charging higher interest rates than allowed by law for loans. Officials may decide that the human damage caused by business practices described in this report is sufficient for determining, after a full evaluation, that certain businesses are off-limits even in states where their practices are not patently illegal.

One area where the military may want to apply this approach is unfair or deceptive conduct. Because the Federal Trade Commission Act provides broad guidelines, it may not be clear whether the FTC would find that a lender's conduct meets the FTC Act standard for unfair and deceptive acts and practices. Nevertheless, military personnel could make an independent assessment of the practice at issue.[27]

The FTC has defined deceptive conduct as an act or practice likely to deceive consumers.[28] A showing that specific consumers were actually deceived is not necessary and an act can be deceptive even if it is an industry-wide practice. Deceptive practices include both actual misrepresentations and failure to disclose material information. Conduct is unfair where it "causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to

[27] Military leadership also may want to consider asking the Federal Trade Commission to make a determination, through a rule-making, that specific practices violate the general standards of the FTC Act.

[28] *See* FTC v. Gill, 265 F.3d 944 (9th Cir. 2001).

consumers or to competition."[29] Most state unfair practices laws go further, banning activities that offend public policy or are immoral, unethical, oppressive, or unscrupulous.

Outside of any legal analysis, military leaders may determine that certain practices that prey on service people should be declared off-limits simply because of their harmful effect. Because of the unique role the military plays in protecting its members from situations that might interfere with readiness or individual welfare, it is wholly appropriate to evaluate unscrupulous businesses with a broader approach.

c. Address Newspaper Advertising by Problem Businesses

The nationwide Army/Navy/AirForce/MarineCorps "Times" newspapers pose special problems because so many service people apparently see them as "official" military publications when in fact they are not. That gives their advertisements more credibility than they often deserve, and thus a greater ability to draw in customers and deceive readers. The military can demand that Gannett, the publisher of the "Times" newspapers, clearly state on every page and website that the publication is not an official Department of Defense publication and is not condoned or checked by the Defense Department. If the newspapers balk at such a request, they can be banned from all military bases. Similar efforts can also be made to clarify the roles of local base newspapers, which are more under the control of base and regional commanders.

d. Additional Steps

As noted in this report, a variety of solutions already developed by the military provide an interesting template for further action. Local and occasionally service-wide efforts to

[29] The Federal Trade Commission Act Amendments of 1994, Pub. L. No. 103-312 §9, adding a new 15 U.S.C. §45(n) (Aug. 26, 1994).

increase financial education and counseling, rein in unscrupulous car dealers, and change laws have all met with success.[30]

The easiest recommendation is to expand these efforts, but that first requires a greater commitment of resources. The military recognizes this need at least in principle; turning it into reality still has, as one Pentagon-level official put it, "a way to go."

Broadening and strengthening education efforts is a good start. A major component of existing financial-literacy education takes place during basic training, but several officials told NCLC that is not a good time for these efforts because young people, trying hard to learn their jobs and get used to military life, often have little mental or emotional room left to absorb it. So financial education should probably be moved back a bit -- but without being long delayed in order to get new people started off right.

The Defense Department's own 2002 report on personal financial management advocates more comprehensive "life cycle" economic literacy training that updates and expands on initial efforts throughout a military career. The idea is to both keep knowledge fresh and adjust it to life's changing financial challenges, and it's one that needs speedier implementation. We note here that the military has begun taking steps in this direction with its May 8th kickoff of a service-wide "Financial Readiness Campaign." Officials also might want to raise awareness of the new Military Sentinel website that allows service people to blow the whistle on illegal and abusive businesses.

The local and national military news media should also be encouraged to do more journalism that exposes consumer-scamming businesses *by name* and actively educates consumers. Given the youth and turnover of military personnel these should be ongoing efforts, regularly repeated.

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[30] The military also has initiated some of the actions recommended above, such as confronting powerful advertisers and making certain businesses "off-limits" to service personnel.

Increasing the military's public witness and legislative advocacy in fighting financial abuses seems especially worthwhile right now. When military leaders "changed the whole complexion" of Florida's title-pawn lending battle they tapped into a perhaps-unrealized level of credibility and moral authority. They have the ear of political leaders at all levels, the credibility to debunk scam-industry apologists, the facts to illustrate the human toll and an especially-high profile at present. Those are powerful weapons that should be more freely employed.

Finally, an aspect of military culture that has inadvertently aided consumer predators also needs addressing: the notion that financial trouble means career trouble. While it's understandable that good conduct codes call for financial rectitude – and further that repeat offenders may be subject to discipline -- the notion that any scrape with money trouble will be damaging needs to be much more forcefully refuted. This is especially true in the face of the clear efforts to exploit those fears documented in this report. Too many military people have been driven further into the arms of predators by fear of being punished for their problems, and its accompanying desire to keep the news away from superiors. Much damage can be prevented if there's less fear of seeking help.

II. EXPAND CIVILIAN LAW ENFORCEMENT

The Federal Trade Commission, state attorneys general and private lawyers can also do more to fight scams targeting the military. The FTC can take a bigger role in analyzing suspected violations of its UDAP standards and other federal laws by businesses targeting service people. It can then follow up with appropriate enforcement actions against violators. The FTC's Military Sentinel website can serve as one source for such investigations.

Attorneys general – especially in states with a large military presence – also can be mindful that service people are more often targeted for scams. They can increase enforcement of state UDAP provisions and other laws, and investigate potential violators accordingly.

More private legal actions challenging scams that violate UDAP standards, federal Truth in Lending Act provisions, state and federal usury laws, and other mandates are also needed. Private actions are always an important component of effective law enforcement.

III. BAN THE PURCHASE OF VETERANS' BENEFITS

As reported in Part 2, NCLC attorneys believe the assigning of veterans' benefits in "advance funding" and other lump-sum buyout deals is illegal under existing law. To ensure that benefits intended to support veterans and their dependents are used for that support, however, the federal law prohibiting the assignment or sale of those benefits could be both clarified and better-enforced.

The approach in proposed legislation has been to clarify the law by explicitly prohibiting transfer of these future benefits for a lump sum, and by including fines and criminal penalties for violations of the law in order to aid enforcement. Although this approach does address the immediate issue, a broader and more open-ended approach would have a greater long-term effect. The size and shape of new consumer scams is limited only by the imaginations of the unscrupulous – we've already reported attempts by these buy-out companies to disguise the true nature of these assignments in order to avoid the federal prohibition. Broader-reaching language in new legislation to address not only this particular type of assignment (future benefits for a lump-sum payment now) but *any* transaction that is in essence an assignment will have greater impact; it can unequivocally prohibit the new and creative schemes that undoubtedly will appear. New legislation should explicitly ban not only the present version of the scam on veterans' benefits but any future variations.

The Nelson-McCain bill that passed the Senate last September (2002 SB 2237) included an outreach program to educate veterans about the ban on these assignments. Education is also an important part of protecting these benefits. Veterans receiving regular, guaranteed federal payments each month are attractive targets, and better education regarding this increasingly prevalent illegal scam will help reduce the number of victims. The bill, however, is unlikely to pass the Senate again during this session, nor is the current House likely to pass something similar. Nevertheless, the Veterans Administration can voluntarily send out notices to educate veterans about the ban on assigning benefits.

IV. STRENGTHEN AND EXPAND EXISTING LAW

A new federal law sharply curbing predatory lending and its usurious interest rates and fees for everyone, military and civilian alike, is a minimum first step toward improving the current situation.

The problems outlined in this report are best addressed with comprehensive federal legislation for several reasons, not least of which is the tendency of one state's problems to "bleed" over neighboring borders when only the first state toughens its laws.[31] But strong state and local legislation would be progress as well.

On the federal front NCLC attorneys have drafted, at the Defense Department's request, an amendment to the existing Soldiers' and Sailors' Civil Relief Act of 1940. The Act currently prohibits lenders, in many cases, from charging military personnel more than 6% interest on loans entered into *before* they entered the service.

The amendment adds a flat cap of 36% interest (defined as the annual percentage rate as used in the Truth In Lending Act) for all loans entered into *during* military service. This

[31] See reference to the perverse outcome for Georgia to Florida's successful battle against title-pawn lenders on pages 22-23 of this report.

amendment expands the law to prevent lenders from making very high-cost loans to military personnel during their tenure in the military and without any exceptions. Payday loans, auto title loans, and other forms of expensive obligations would effectively be banned. Responsible lending to U.S. service people would not be affected.

In addition, businesses that seek to exploit lending-law loopholes by claiming they're not actually lenders – such as the catalog, internet and phone card "sales" businesses described in this report – would appear to be good targets for new or strengthened laws. As stated earlier, NCLC attorneys believe existing law can curb many practices of businesses that disguise their actual intent, but the ever-changing ingenuity of those who would evade the law strengthens the case for new legislative counter-measures as well.

V. WHAT CONSUMERS CAN DO

A major frustration with these scams is that so many who become entangled with them need never do so. Many consumers simply don't realize they have access to far less costly, better-quality credit than that offered by many of the businesses they patronize. So credit unions, financial counselors, relief societies and others serving the military should be approached first when money is an issue. They can often steer people to a better credit source and, more importantly, help individuals and families control debt and move toward long-term financial stability.

Self-education also matters. The modern financial marketplace is far less regulated and offers many more choices than previous generations had. Marketers complement these choices with a steady stream of "do it now" temptations. So service people should think of "basic training" in more than just a military sense. "Financial awareness basic-training" should include the fundamentals of budgeting and spending, debt control, use of credit, insurance, long-term goal-setting, consumer scams and more.

Here are some of the basics for steering clear of scams:

- **Save now for unexpected expenses.** Even putting aside a small amount each week will help. Try saving money *before* there's an unexpected expense so you can avoid borrowing. You can talk with budget or financial-planning counselors -- most military bases have them -- who can help you understand how you spend your money each month and how you might save.

- **Shop around.** Don't immediately accept a lender's statement that you're a "sub-prime" borrower who must pay very high interest rates to get credit. You should always shop around rather than accept higher-than-normal loan rates. You may have perfectly good credit in the eyes of another lender. Even if you are considered high-risk by all those you contact, there are many types of sub-prime loans. You should shop among the different sub-prime lenders until you find a reasonable rate and terms. And don't just look at the monthly payment. Compare the interest rate (also called the "annual percentage rate," or APR), the total amount you'll repay, the number of payments, and the fees added to the loan.

- **Avoid the most common scams.** The list in Appendix A is not a complete one, and new scams constantly emerge while old ones change form. The main message is that services aimed at people with bad credit or other financial problems are often rip-offs. If they seem too good to be true, they probably are. And here are a few additional scams to watch out for:

  - *Paying for credit repair*. No credit repair agency can clean up your credit record if you've been behind on many debts. Promises to do so are lies designed to get you to pay for something that can't really help you.
  - *Taking high-rate loans to tide you over.* Some lenders offer high-rate loans to help you get back into the credit market. The worst of these are high-interest loans secured by your home – you can lose your home for non-payment! These lenders are counting on your belief that you can't get credit on better terms elsewhere. They also may make false promises that the rate can be reduced if you establish a year or more of timely payments. Lenders offering high-rate credit in these circumstances are only trying to rip you off.
  - *Doing business with companies that advertise claims such as "no credit check" or "bad credit no problem."* These companies are either loan brokers or lenders looking for borrowers who consider themselves too risky to pass a credit check -- and who are therefore willing to sign up for high rates. You may discover when reputable lenders evaluate your credit record that you're a better credit risk than you think.

- **Read before you sign.** Make sure you or someone you trust reads the loan papers *before* you sign them. If a lender won't let you take the papers home to study them or tries to rush you, that's a sign of trouble and you should walk away.

- **Ask for help.** If you borrowed money from one of these lenders and want to know your legal rights, you can get free assistance from your local legal services office or, in the military, your JAG office. You may also want to contact your state Attorney General's office, the local Better Business Bureau, or the Federal Trade Commission's Internet-based consumer complaint hotline Military Sentinel at http://www.consumer.gov/military/. You can also find more detailed information about common consumer scams and your legal rights on the websites of National Consumer Law Center (www.nclc.org), Consumers' Union (www.consumersunion.org), Consumer Federation of America (www.consumerfed.org), the various state Public Interest Research Groups (reachable through the U.S. PIRG website's home page at www.uspirg.org), or in NCLC's "Guide to Surviving Debt."

APPENDIX A: DESCRIPTIONS OF SCAMS COMMONLY AIMED AT THE MILITARY

Payday lenders, cash advance and other "fast cash" businesses: Most all these businesses operate in similar ways, lending small amounts of cash for short terms at exceedingly high interest rates. Many take a post-dated check to be cashed on the borrower's next payday for the principal and interest owed, and some require electronic access to a borrower's bank accounts for payment purposes – see examples throughout this report.[32] Some of these lenders have been known to soft-pedal sky-high annual interest rates they're legally obliged to disclose, using spiels like: "Sure, the form says 520% a year but you're only borrowing the money for two weeks, and it's only 20% for two weeks." They also soft-pedal their interest rates in print ads, like one we found in the NavyTimes that says "Pay only for the time you have the money"[33] -- as if that were a privilege.

Automobile-related scams: Cars are a big source of financial trouble for service people. The Navy-Marine Corps Relief Society, for instance, gives the largest single portion of its cash aid to military families – nearly a quarter of all its aid – for car-repair assistance. Three big auto-related scams aimed at the military are:[34]

"Title Pawn" lending: This goes on in a number of states and has been sharply limited in a few. It's a form of short-term lending where instant cash loans -- usually for no more than a quarter of the car's value – use the car's title as collateral. Interest rates are

[32] More traditional lenders targeting the military (those not of the "instant cash" variety) also have problems, including high interest rates and very high costs. Some charge double-digit interest rates while at the same time larding on fees that greatly raise the real cost of the loan, for instance.
[33] See this and other ads from military newspapers in Appendix B.
[34] An interesting look at car-related scams aimed directly at the military in California is an April 2, 2003 "Your Wheels" column in the Los Angeles Times: "Scamsters preying on military families" by Ralph Vartabedian. Also, military Legal Assistance officials in the San Diego region told NCLC that high-priced used car sales are "the single largest consumer (contract) problem that we see here in Legal Assistance."

usually very high, and there are many cases of cars being lost to lenders for what amounts to a fraction of their value.

"Buy Here/Pay Here" used car dealers: Lynn Drysdale of Florida Legal Services describes typical operations in her region this way: "These dealers finance usually rather old used cars with a large down payment – often equal to the car's value – then put the customer on a bi-weekly (payment) plan for 'the rest.' The car breaks down, the payments stop, they repossess the vehicle and sell it again. They're just churning cars, basically."[35]

"Spot Delivery" or "yo-yo sales": A form of bait-and-switch. Several sources describe these fundamentals: Buyer buys car, signs financing agreement, and drives the new purchase away. The dealer calls later and says buyer's credit has not been approved, and in order to keep the car buyer will have to agree to either a higher interest rate, a larger down payment or both. If a trade-in was involved the buyer is often told the trade-in has already been sold and is not recoverable. Dealer then offers the option of buyer's losing the value of the trade-in if he or she wants to keep the remaining terms of the original deal.

Catalog, internet and phone card "sales": NCLC's analysis shows these are often nothing more than thinly-disguised forms of high-priced lending, with the disguise in the form of up-front cash either exchanged or called a "rebate" for the purchase of very high-priced goods or services. Examples of how catalog sales businesses operate can be found in the main report's sections "A Call to Georgia Catalog Sales" and "I Just Kept Coming Up Short." Former military financial counselor Ray Meaux was one of many who told us catalog-sales customers rarely use the catalog coupons that supposedly make these cash advances "not a loan," because the catalog goods are often some combination of very high-

[35] Ray Meaux, a former financial counselor at military bases in South Carolina and Georgia, says his investigation of one "buy here/pay here" dealer in Charleston, South Carolina showed the dealer had sold the same car 18 times!!

priced, very low-quality, or subject to outrageous shipping and handling charges that make the "purchase" not worthwhile.

Internet sales: According to counselors who've dealt with ensnared military personnel one of these businesses in Florida, called Florida Internet,[36] offers customers a series of instant-cash "rebate" options in exchange for Internet service. One option is a $480 "rebate" when customers commit to a year's Internet service. The cost is $80 every two weeks for up to eight hours' service, and the Internet can only be accessed at the company's handful of storefront sites – we visited two of them and between them they had four terminals, none in use. The company also arranges for payments to be automatically deducted from customers' bank or credit-card accounts. The math? First of all, unlimited Internet access on a home computer can be had for less than $20 a month or $240 a year in most places. Customers buying the $480 rebate option are being asked to pay $2,080 ($173.33 per month) for a year of limited service (eight hours every two weeks,) minus the "rebate" that brought the price down to $1,600 or $133.33 a month. Looked at another way, a $480 loan that triggers $173.33 monthly payments for 12 months as this "purchase" does would be a loan carrying a 421.6% annual interest rate.

Phone card sales: This is quite similar in structure to the Internet sales scam above except that the product's different. In a reported example near the Marine Corps' Camp Lejeune in North Carolina, local counselors say those joining a "phone card membership club" got an instant $300 "cash back" rebate in exchange for their agreement to purchase 300 minutes' worth of phone cards twice a month over a year. The cost was $67.50 each time or $135 a month. Setting aside that 600 minutes' worth of phone cards can be purchased at many stores for a fraction of that price (and that even at very high prices the

[36] See copy of a Florida Internet contract in Appendix B.

phone cards have some usable value), a $300 loan triggering $135 in monthly payments for a year would be a loan carrying a 533% interest rate.

Other sales ripoffs:

The list includes:

- ✓ High-priced life insurance sales reported around the country (the insurance is often unnecessary as well as high-priced).
- ✓ "Education" scams where military personnel are verbally "promised" a college degree but only receive study materials, an encyclopedia or a computer purchased as "part" of the program.
- ✓ Sales of very high-priced "lifetime" camera, film and film developing packages reported to NCLC by San Diego-area military officials.[37]
- ✓ Miscellaneous door-to-door sales and attempts to circumvent rules banning these sales on base. One Pentagon official reports that salespeople normally banned from Air Force bases work hard to gain access as "exhibitors" during the spring and summer exhibition air show season.

Rent-to-Own: A common presence in low-income communities nationwide, RTO businesses are essentially furniture and appliance retailers who lease their products to those who can't pay cash or obtain market-rate credit. Those customers who rent long enough to actually assume ownership of the goods have often paid two to three times the retail price by the time they've stopped renting – and of course many only rent at what turn out to be very high prices.

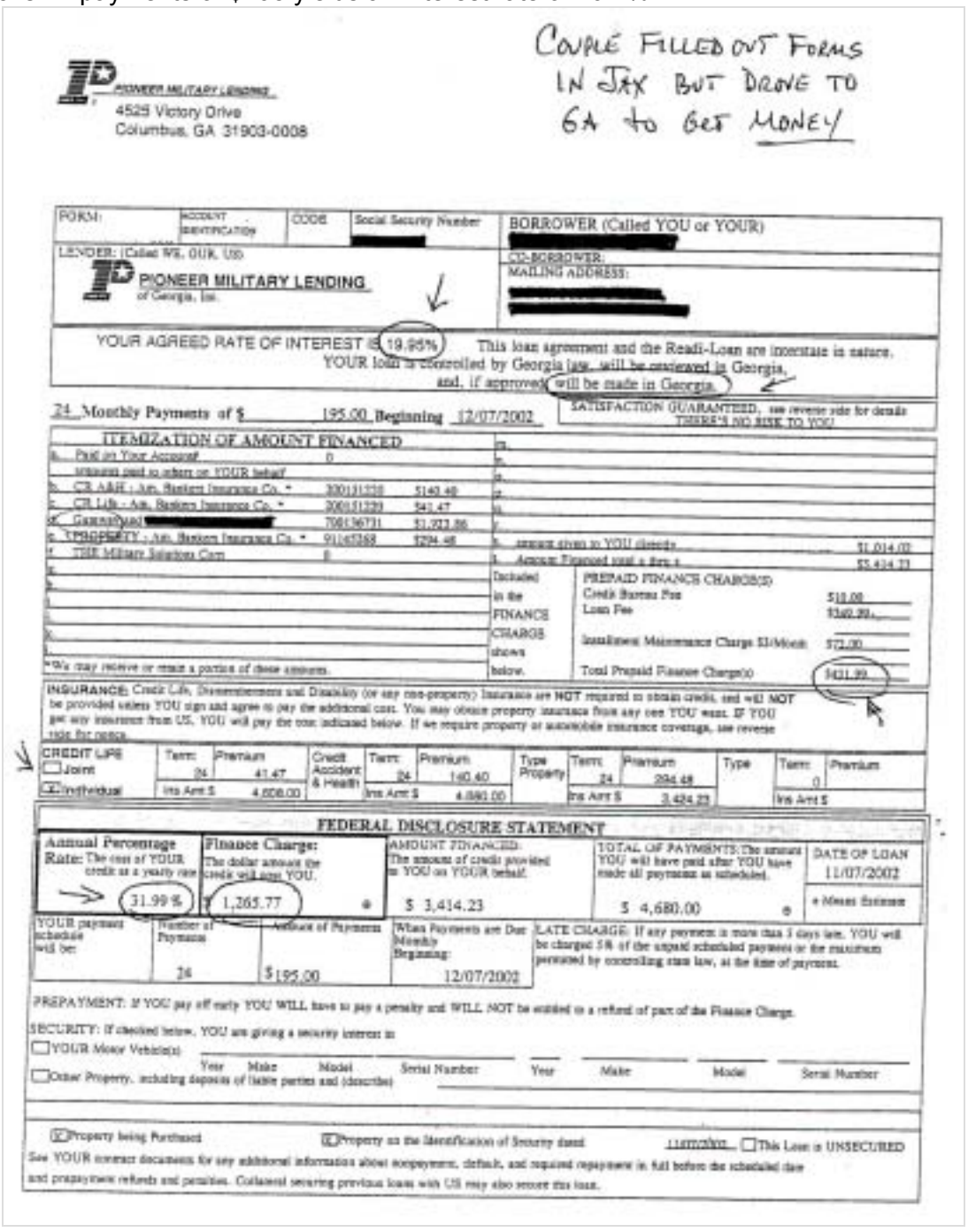
[37] The military Judge-Advocate's office for that region tells NCLC that one such business, Focus Point/Photo World -- "also formerly known as ABC Finance Company," was placed off-limits to military personnel by regional commanders. The business "has a long history with Legal Assistance attorneys," wrote an office representative, who added: "when the issue arises, almost every contested contract is voluntarily rescinded by (the) company's attorney."

Benefits buyouts aimed at veterans: This is one of the most costly scams for individuals, who can lose tens of thousands of dollars' worth of future benefits payments in exchange for a lump-sum, "advance funding" buyout. Fully described in Part 2 of the main report, "Reward for Service: A Scam Targeting Veterans' Benefits."

APPENDIX B - EXHIBITS

HIGH FEES JACK UP LOAN'S COSTS - PIONEER MILITARY LENDING

This loan agreement with Pioneer Military Lending adds $431.99 in fees to the finance charge, changing the listed 19.95% "agreed rate of interest" to 31.99%. And the original loan includes $476.35 for insurance premiums, so the money actually pocketed by the borrower in exchange for this deal's 24 payments of $195 yields an interest rate of 49.4%.



COUPLE FILLED OUT FORMS IN JAX BUT DROVE TO GA to GET MONEY

PIONEER MILITARY LENDING
4525 Victory Drive
Columbus, GA 31903-0008

FORM: | ACCIDENT IDENTIFICATION | CODE | Social Security Number [redacted] | BORROWER (Called YOU or YOUR) [redacted]

LENDER: (Called WE, OUR, US) PIONEER MILITARY LENDING of Georgia, Inc.

CO-BORROWER:

MAILING ADDRESS: [redacted]

YOUR AGREED RATE OF INTEREST IS 19.95% This loan agreement and the Readi-Loan are interstate in nature. YOUR loan is controlled by Georgia law, will be endorsed in Georgia, and, if approved, will be made in Georgia.

24 Monthly Payments of $ 195.00 Beginning 12/07/2002

SATISFACTION GUARANTEED, see reverse side for details. THERE'S NO RISK TO YOU!

ITEMIZATION OF AMOUNT FINANCED

a. Paid on Your Account	0	
Amounts paid to others on YOUR behalf		
b. CR A&H - Am. Bankers Insurance Co. *	3001311720	5140.40
c. CR Life - Am. Bankers Insurance Co. *	3001311720	541.47
d. Guaranty[redacted]	7001367731	$1,272.86
e. TPROPERTY - Am. Bankers Insurance Co. *	911457268	$294.48
f. THE Military Solutions Corp	0	

g. Amount given to YOU directly $1,014.00

h. Amount Financed (total a thru g) $3,424.23

PREPAID FINANCE CHARGE(S) (Included in the FINANCE CHARGE shown below.)

Credit Bureau Fee	$18.00
Loan Fee	$360.99
Installment Maintenance Charge $3/Month	$72.00
Total Prepaid Finance Charge(s)	$431.99

*We may receive or retain a portion of these amounts.

INSURANCE: Credit Life, Disemployment and Disability (or any non-property) insurance are NOT required to obtain credit, and will NOT be provided unless YOU sign and agree to pay the additional cost. You may obtain property insurance from any one YOU want. IF YOU get any insurance from US, YOU will pay the cost indicated below. If we require property or automobile insurance coverage, see reverse side for notice.

CREDIT LIFE	Term	Premium	Credit Accident & Health	Term	Premium	Type Property	Term	Premium	Type	Term	Premium
☐ Joint	24	41.47		24	140.40		24	294.48		0	
☒ Individual	Ins Amt $	4,606.00		Ins Amt $	4,680.00		Ins Amt $	3,424.23		Ins Amt $	

FEDERAL DISCLOSURE STATEMENT

Annual Percentage Rate: The cost of YOUR credit as a yearly rate	Finance Charge: The dollar amount the credit will cost YOU.	AMOUNT FINANCED: The amount of credit provided to YOU or YOUR behalf.	TOTAL OF PAYMENTS: The amount YOU will have paid after YOU have made all payments as scheduled.	DATE OF LOAN
31.99 %	$ 1,265.77	$ 3,414.23	$ 4,680.00	11/07/2002

* Means Estimate

YOUR payment schedule will be:	Number of Payments	Amount of Payments	When Payments are Due: Monthly Beginning:
	24	$195.00	12/07/2002

LATE CHARGE: If any payment is more than 5 days late, YOU will be charged 5% of the unpaid scheduled payment or the maximum permitted by controlling state law, at the time of payment.

PREPAYMENT: If YOU pay off early YOU WILL have to pay a penalty and WILL NOT be entitled to a refund of part of the Finance Charge.

SECURITY: If checked below, YOU are giving a security interest in

☐ YOUR Motor Vehicle(s) Year Make Model Serial Number Year Make Model Serial Number

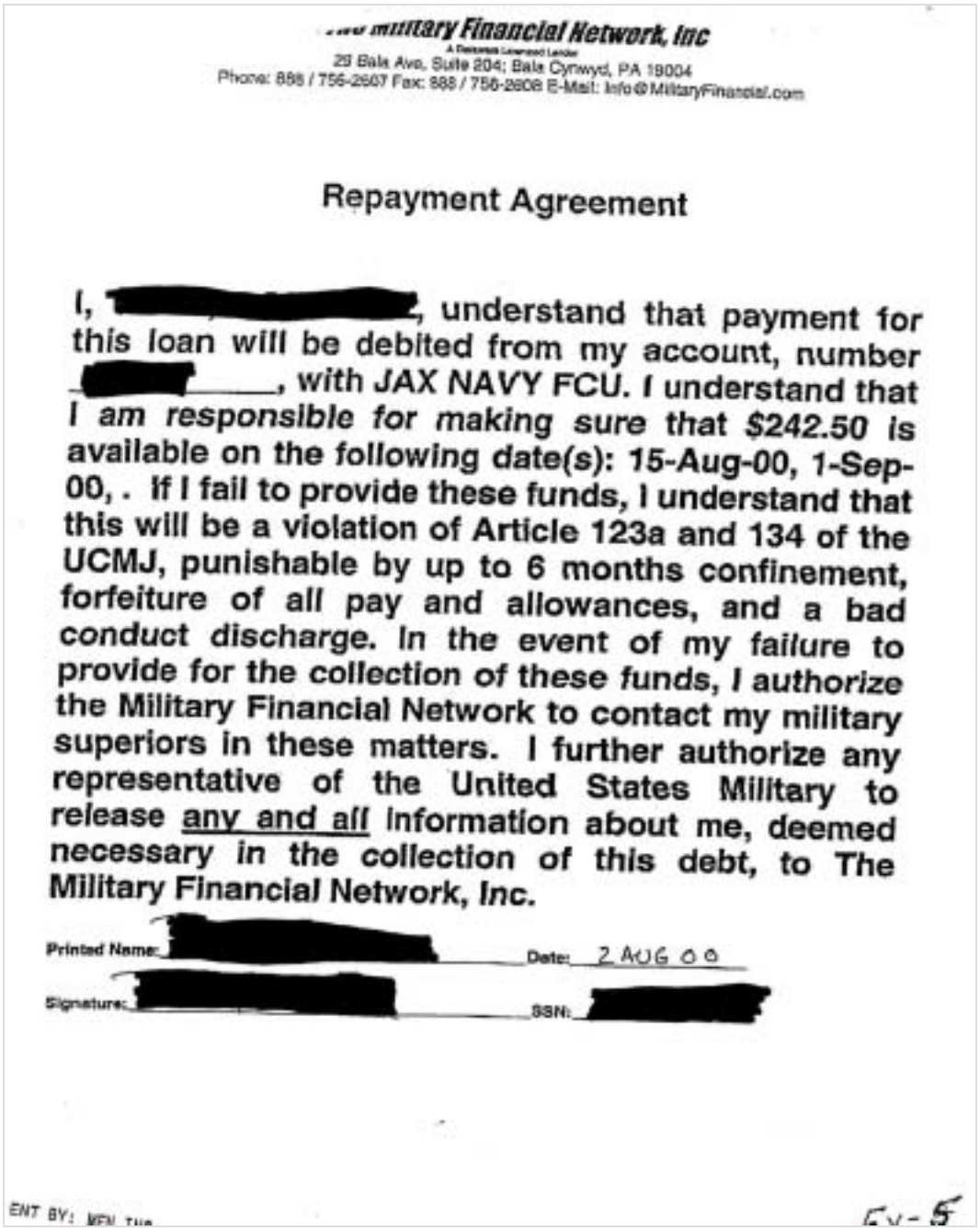
☐ Other Property, including deposits of liable parties and (describe)

☒ Property being Purchased ☒ Property on the Identification of Security dated 11/07/2002 ☐ This Loan is UNSECURED

See YOUR contract documents for any additional information about nonpayment, default, and required repayment in full before the scheduled date and prepayment refunds and penalties. Collateral securing previous loans with US may also secure this loan.

DECEPTIVE SCARE TACTICS - MILITARY FINANCIAL NETWORK CONTRACT

This Repayment Agreement from a Military Financial Network "Rapid Cash" loan (company-quoted annual interest rate of 365%) prominently notes that failure to repay could result in six months' confinement, a bad conduct discharge, and the borrower's being reported to military superiors. Though possible, those kinds of penalties for financial problems are virtually unheard of. One retired admiral says the contract language "is there to intimidate and coerce." NCLC believes this language unquestionably violates Unfair and Deceptive Acts and Practices (UDAP) standards and therefore should be referred by military officials to the Federal Trade Commission.



Military Financial Network, Inc
A Delaware Licensed Lender
29 Bala Ave, Suite 204; Bala Cynwyd, PA 19004
Phone: 888 / 756-2607 Fax: 888 / 756-2608 E-Mail: Info@MilitaryFinancial.com

Repayment Agreement

I, [redacted], understand that payment for this loan will be debited from my account, number [redacted], with JAX NAVY FCU. I understand that I am responsible for making sure that $242.50 is available on the following date(s): 15-Aug-00, 1-Sep-00, . If I fail to provide these funds, I understand that this will be a violation of Article 123a and 134 of the UCMJ, punishable by up to 6 months confinement, forfeiture of all pay and allowances, and a bad conduct discharge. In the event of my failure to provide for the collection of these funds, I authorize the Military Financial Network to contact my military superiors in these matters. I further authorize any representative of the United States Military to release any and all information about me, deemed necessary in the collection of this debt, to The Military Financial Network, Inc.

Printed Name: [redacted] Date: 2 AUG 00

Signature: [redacted] SSN: [redacted]

ENT BY: MFN TUE

Ex - 5

ERODING BORROWERS' PROTECTIONS -- LOANS FOR MILITARY CONTRACT

(next two pages)

This 2001 agreement specifically excludes the lender, Loans For Military, from exposure to any of the borrower's subsequent financial problems – leaving the borrower few protections and the lender with little incentive to responsibly screen borrowers. The boldface paragraphs on the first page say the loan must not be part of any future bankruptcy or debt-consolidation program the borrower might enter into. NCLC attorneys believe that clauses like the one excluding the lender from any bankruptcy proceeding filed by the borrower are not enforceable. On the second page, this loan's addition of a hefty fee not counted in the 17% "annual percentage rate" effectively turns this into 12 payments of $68.02 for a $500 loan – a 101.8% annual interest rate. NCLC attorneys believe the failure to include the $245.75 "Origination & Administration" charge in the box labeled "Finance Charge" is a clear violation of the federal Truth in Lending Act. An attorney representing Loans for Military recently advised NCLC that these documents were replaced in 2001 by documents in each contract "that are in direct compliance with the Truth-In-Lending Act."

Page 1

Loans For Military

Credit Release Authorization & Supplemental Loan Application Information

2ND LOAN APPLICATION PACKAGE

Name(Last) [redacted] (First) [redacted] (Middle) SS# [redacted] Rank E5

Date of Birth [redacted] Base NAS JACKSONVILLE, FL Duty Phone [redacted]

Off Duty Address NAVAL AIR RESERVE Apt#: [redacted] Home Phone [redacted]

NAVAL AIR
STAT 100 JACKSONVILLE

City JACKSONVILLE State FL Zip 32212-0004

Co-Borrower(Last) N/A (First) _____ (Middle) _____ SS # _____

I hereby authorize Loans For Military to contact any individual, business and company, corporation, or credit bureau to supply any information concerning my credit worthiness and credit history in case my loan goes into default. I hereby also give my permission for any individual business, company, corporation or credit bureau to release any and all information regarding my credit worthiness and credit reports permissible by all governing laws to Loans For Military for the same purpose..... [redacted] (X) initials

The applicant(s) has thoroughly examined his/her income and determined it is sufficient to repay the above referenced loan, including any other debts for which the applicant(s) is liable..... [redacted] (X) initials

The applicant(s) has no collections or debts in arrears, or in force, including charge-offs or repossessions, which have not been made known to the Lender..... [redacted] (X) initials

The applicant(s) has made known to the Lender any and all derogatory information, which would have bearing on the Lender's decision to make the requested loan..... [redacted] (X) initials

THE APPLICANT(S) IS NOT NOW IN ANY CREDIT COUNSELING PROGRAM, AND SPECIFICALLY AGREES TO EXCLUDE THE LENDER FROM ANY DEBT CONSOLIDATION PROGRAM INTO WHICH HE/SHE MIGHT ENTER ..... [redacted] (X) initials

IN THE EVENT OF AN UNFORESEEN OCCURRENCE, THE BORROWER(S) EXPLICITLY AGREES TO EXCLUDE THE LENDER FROM ANY BANKRUPTCY PROCEEDINGS INTO WHICH THE BORROWER(S) AY ENTER..... [redacted] (X) initials

The Borrower(s) EXPLICITLY AGREES not to discontinue any allotment payment being made to retire the debt without the EXPRESS, WRITTEN CONSENT of the Lender..... [redacted] (X) initials

The Borrower(s) EXPLICITLY Agrees to immediately notify the Lender when there is a change of Duty Station and provide the new address and telephone numbers to the Lender..... [redacted] (X) initials

I (We) have read and understand this agreement, and explicitly agree to its terms as a condition of obtaining a loan from Loans For Military..... [redacted] (X) initials

[redacted] X N/A [redacted]/01

Signature C[redacted] Signature Co-Applicant Date

LOANS FOR MILITARY

FEDERAL TRUTH-IN-LENDING DISCLOSURES

Note Number 2ND LOAN

ANNUAL PERCENTAGE RATE	FINANCE CHARGE	PRINCIPAL AMOUNT	AMOUNT FINANCED	TOTAL OF PAYMENTS
The cost of your credit as a yearly rate	The dollar amount the credit will cost you.	Loan Amount	The amount of credit provided to you or on your behalf.	The amount you will have paid after you made all payments as scheduled.
17 %	$70.44	$500.00	$745.75	$816.19

Payment Schedule

Number of Payments	Monthly Payment	When Payments Are Due
12	$68.02	Monthly

Charges That Increase The Annual Percentage Rate:

Prepaid Interest	0 days at 17.000%
Origination & Administration	$245.75
Nominal Interest Rate	17.000%
Effective Annual Rate	18.717%
Periodic Rate	1.417%
Equivalent Daily Rate	0.047%

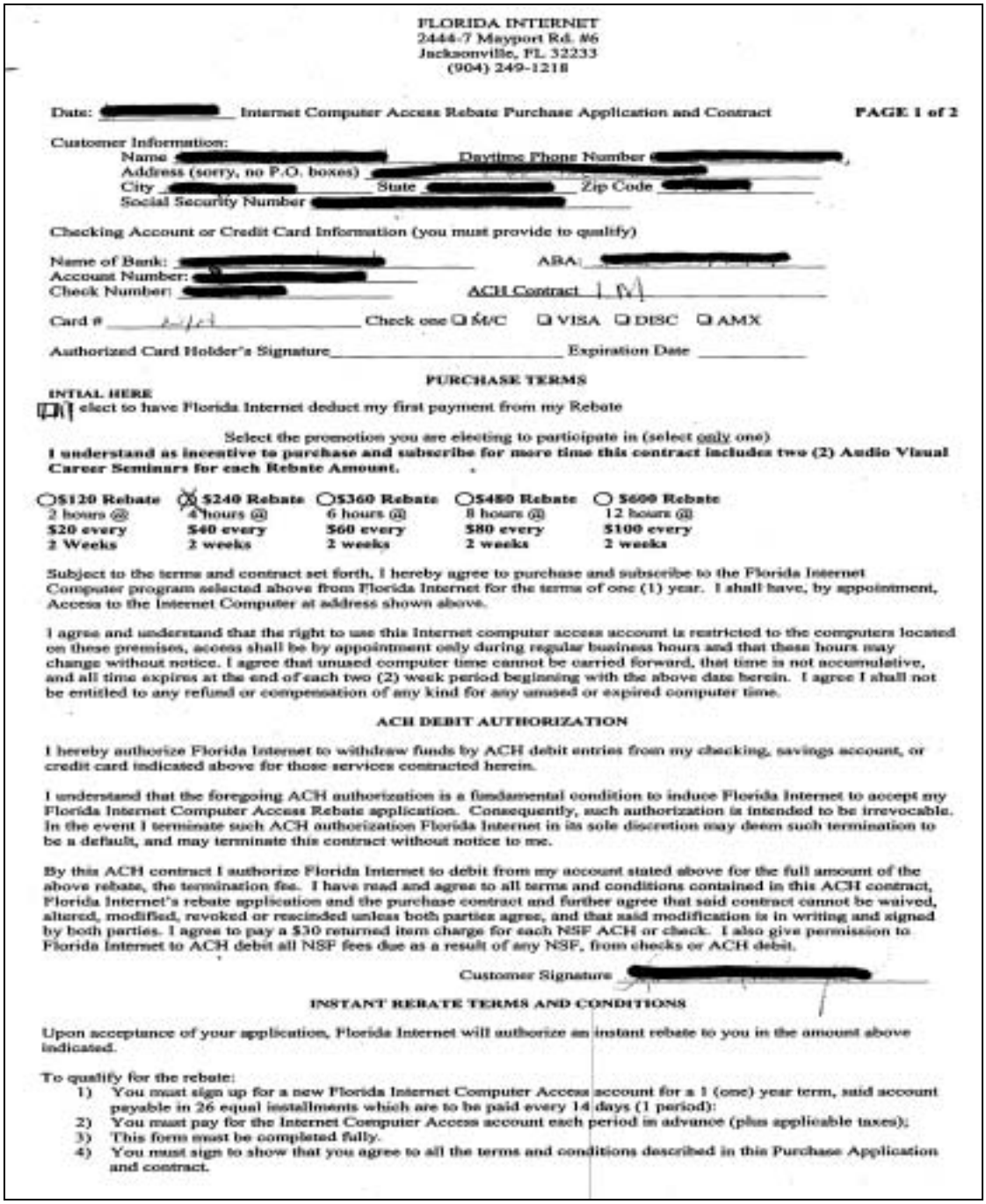
Summary of Total Payments

Loan Amount	$500.00
Interest	$70.44
Origination & Administration	$245.75
Total Payments	$816.19

NOTE: ALL LOANS ARE FOR 12 MONTHS

VIRTUALLY USELESS "PURCHASE" - FLORIDA INTERNET CONTRACT

Florida Internet's "computer access" purchase agreement more closely resembles a thinly-disguised and very high-priced loan. The Internet service "purchased" in this agreement is not only exceptionally expensive but subject to strict access limits that make it virtually useless to many. That makes the up-front "rebate" the only item of consequence in this transaction – pretty much a high-cost instant loan at over 400% annual interest. In order to get the $240 instant-cash "rebate" checked here, for instance, the borrower commits to payments of $1,040 over a year.



FLORIDA INTERNET
2444-7 Mayport Rd. #6
Jacksonville, FL 32233
(904) 249-1218

Date: [redacted] Internet Computer Access Rebate Purchase Application and Contract **PAGE 1 of 2**

Customer Information:
Name [redacted] Daytime Phone Number [redacted]
Address (sorry, no P.O. boxes) [redacted]
City [redacted] State [redacted] Zip Code [redacted]
Social Security Number [redacted]

Checking Account or Credit Card Information (you must provide to qualify)

Name of Bank: [redacted] ABA: [redacted]
Account Number: [redacted]
Check Number: [redacted] ACH Contract [✓]

Card # [redacted] Check one ☐ M/C ☐ VISA ☐ DISC ☐ AMX

Authorized Card Holder's Signature_____ Expiration Date _____

PURCHASE TERMS

INTIAL HERE
[✓] elect to have Florida Internet deduct my first payment from my Rebate

Select the promotion you are electing to participate in (select only one)
I understand as incentive to purchase and subscribe for more time this contract includes two (2) Audio Visual Career Seminars for each Rebate Amount.

○ $120 Rebate	⊗ $240 Rebate	○ $360 Rebate	○ $480 Rebate	○ $600 Rebate
2 hours @	4 hours @	6 hours @	8 hours @	12 hours @
$20 every	$40 every	$60 every	$80 every	$100 every
2 Weeks	2 weeks	2 weeks	2 weeks	2 weeks

Subject to the terms and contract set forth, I hereby agree to purchase and subscribe to the Florida Internet Computer program selected above from Florida Internet for the terms of one (1) year. I shall have, by appointment, Access to the Internet Computer at address shown above.

I agree and understand that the right to use this Internet computer access account is restricted to the computers located on these premises, access shall be by appointment only during regular business hours and that these hours may change without notice. I agree that unused computer time cannot be carried forward, that time is not accumulative, and all time expires at the end of each two (2) week period beginning with the above date herein. I agree I shall not be entitled to any refund or compensation of any kind for any unused or expired computer time.

ACH DEBIT AUTHORIZATION

I hereby authorize Florida Internet to withdraw funds by ACH debit entries from my checking, savings account, or credit card indicated above for those services contracted herein.

I understand that the foregoing ACH authorization is a fundamental condition to induce Florida Internet to accept my Florida Internet Computer Access Rebate application. Consequently, such authorization is intended to be irrevocable. In the event I terminate such ACH authorization Florida Internet in its sole discretion may deem such termination to be a default, and may terminate this contract without notice to me.

By this ACH contract I authorize Florida Internet to debit from my account stated above for the full amount of the above rebate, the termination fee. I have read and agree to all terms and conditions contained in this ACH contract, Florida Internet's rebate application and the purchase contract and further agree that said contract cannot be waived, altered, modified, revoked or rescinded unless both parties agree, and that said modification is in writing and signed by both parties. I agree to pay a $30 returned item charge for each NSF ACH or check. I also give permission to Florida Internet to ACH debit all NSF fees due as a result of any NSF, from checks or ACH debit.

Customer Signature [redacted]

INSTANT REBATE TERMS AND CONDITIONS

Upon acceptance of your application, Florida Internet will authorize an instant rebate to you in the amount above indicated.

To qualify for the rebate:
1) You must sign up for a new Florida Internet Computer Access account for a 1 (one) year term, said account payable in 26 equal installments which are to be paid every 14 days (1 period);
2) You must pay for the Internet Computer Access account each period in advance (plus applicable taxes);
3) This form must be completed fully.
4) You must sign to show that you agree to all the terms and conditions described in this Purchase Application and contract.

NavyTimes NEWSPAPER ADS

The "Finance Directory" of the March 3, 2003, NavyTimes newspaper is full of ads for fast loans (this page and next). Aside from quick-cash and other lenders, several of the small-print ads on the right (enlarged at bottom) are for companies that buy out streams of veterans' benefits – a worrisome phenomenon detailed in Part 2 of this report. The ads themselves can be misleading, as with Military Financial, Inc's. "Pay Only for the Time You Have the Money" line – a tactic frequently used by short-term lenders to soft-pedal super-high *annual* interest rates. But these ads can also mislead in a more subtle way: The nationally-circulated NavyTimes and its Army, Air Force and Marine cousins are not published or controlled by the military though many military people believe they are -- thus letting their guard down when reading ads like these.

FINANCE DIRECTORY

NEED A LOAN?

Installment loans for active military personnel

AFL ARMED FORCES LOANS

Qualify to borrow through our Armed Forces Loan programs.
- Bankruptcies OK
- No Advance Fees
- Lowest Rates
- No Credit? Not a Problem.
- Overseas? Call 702-868-6204
- Up To $3,000

Fill out an application online at...
www.armedforcesloans.com
AND
Fax Your L.E.S to 1-800-698-0914

Quick Phone Approval | Fast Funding
Why Pay More? Call 1-800-706-9676
ARMED FORCES LOANS OF NEVADA INC. 3824 S Jones Blvd. Las Vegas Nevada 89103

FORCE ONE LENDING, INC.

Bad Credit & Bankruptcies Welcome!!!

NEED MONEY TO GET BACK ON TRACK???
Attention Active Duty Members

Compare our cost to other Companies:

- No Originial Fee
- No Upfront Fees
- No Hidden Fees
- No Penalty for Early Pay Offs
- * No credit Check
- * You can apply from the tranquility from your home
- * Loans up to $3000
- * Overseas Applicant Welcome

Fax Your L.E.S. & ID Toll Free: (888) 565-3672
Call Toll Free: (888) 819-3672
For more information visit our WEBSITE:
www.force1loans.com

Se Habla Espanol

FORCE ONE LENDING, INC.
P.O. BOX 129, CAMUY PR, 00627
Licensed Lender in PR

Debt Consolidation - Military Allotments Available
Receive Cash Back Every 6 Months
Feel Good About Your Finances Again
Reduce Total Monthly Payments by 1/3 or More
Eliminate High Interest Rates & Fees
One Simple Low Monthly Payment
1-800-438-9179 Ext: 214
Brighton Credit Management Corp.
www.brightoncredit.com

Nearly 11% of military personnel have aviation specialties. Reach them through a classified ad in this newspaper.
1-800-424-9335 ext. 8902

Financial advice for those serving in the military can be found in the Financial Directory of each week's classified section.

Call to place your ad today.

1-800-424-9335 ext. 8902

A SPECIAL MENTION FOR BRAZENNESS

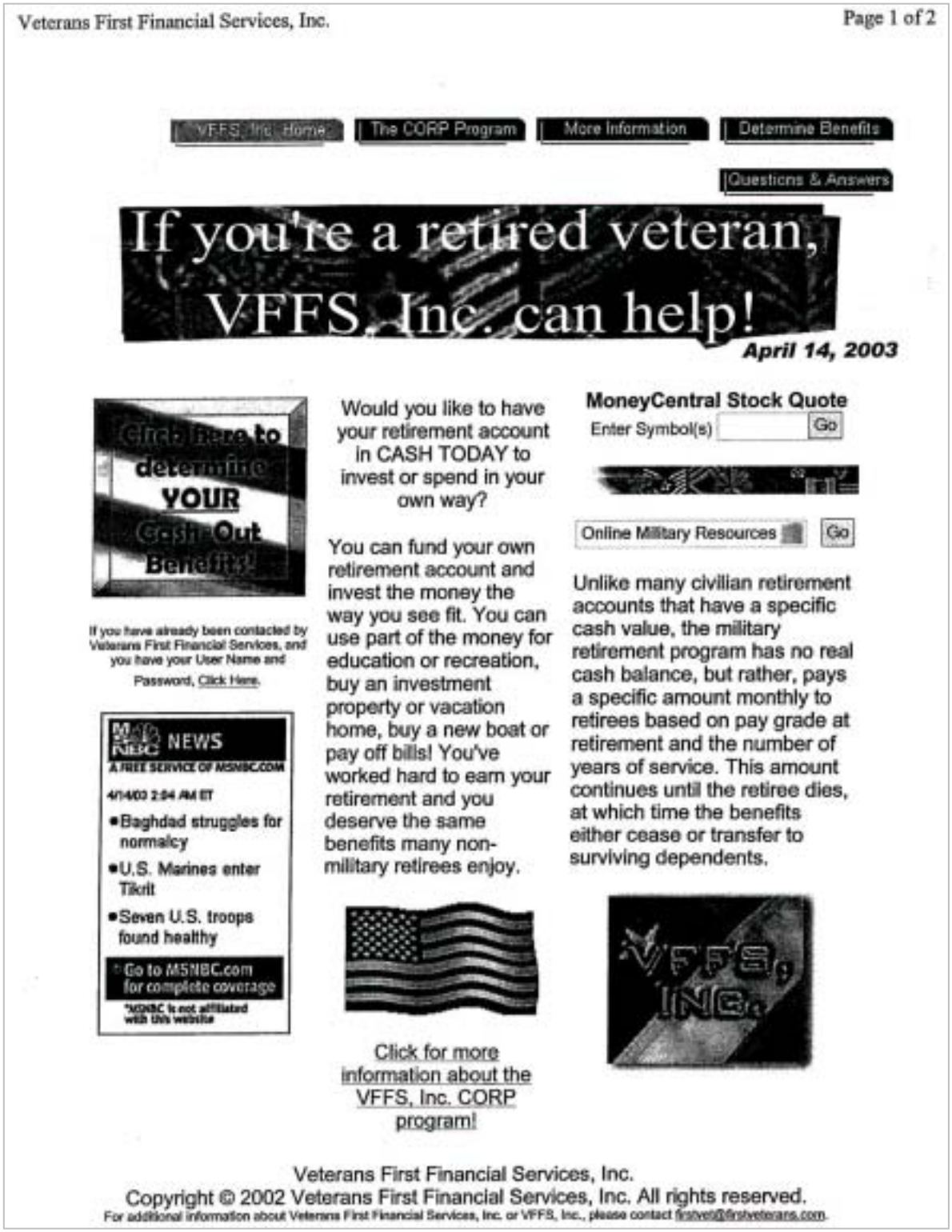
This Military Financial Network ad shamelessly declares "You Won't Believe How Low Our Rates Are!" before disclosing in smaller print that those "low" interest rates are a mere 365% a year.

"COUNTER-ADS" DESIGNED TO FIGHT HIGH-COST BUSINESSES

The "Counter-Ads" at right were created by Navy-Marine Corps Relief Society officials near Jacksonville, Florida, in response to the two ads on the left. The left-side ads for high-cost "instant cash" establishments ran in local base newspapers as did the subsequent counter-ads, which use similar wording and designs to point out that lower-cost alternatives exist to doing business with these "catalog sales" stores.

HINTING AT MILITARY TIES - VETERANS' FIRST FINANCIAL SERVICES

Insignias and a waving flag give this Web page for Veterans First Financial Services a military look, and the language hints at financial empowerment. But VFFS wants veterans to sell their streams of cash benefits for a lump sum, a type of deal that NCLC attorneys believe is illegal under federal law.



Veterans First Financial Services, Inc. Page 1 of 2

VFFS, Inc. Home | The CORP Program | More Information | Determine Benefits | Questions & Answers

If you're a retired veteran, VFFS, Inc. can help!

April 14, 2003

Click here to determine YOUR Cash-Out Benefits!

If you have already been contacted by Veterans First Financial Services, and you have your User Name and Password, Click Here.

MSNBC NEWS
A FREE SERVICE OF MSNBC.COM
4/14/03 2:04 AM ET
- Baghdad struggles for normalcy
- U.S. Marines enter Tikrit
- Seven U.S. troops found healthy

Go to MSNBC.com for complete coverage

*MSNBC is not affiliated with this website

Would you like to have your retirement account in CASH TODAY to invest or spend in your own way?

You can fund your own retirement account and invest the money the way you see fit. You can use part of the money for education or recreation, buy an investment property or vacation home, buy a new boat or pay off bills! You've worked hard to earn your retirement and you deserve the same benefits many non-military retirees enjoy.

Click for more information about the VFFS, Inc. CORP program!

MoneyCentral Stock Quote
Enter Symbol(s) Go

Online Military Resources Go

Unlike many civilian retirement accounts that have a specific cash value, the military retirement program has no real cash balance, but rather, pays a specific amount monthly to retirees based on pay grade at retirement and the number of years of service. This amount continues until the retiree dies, at which time the benefits either cease or transfer to surviving dependents.

VFFS, INC.

Veterans First Financial Services, Inc.
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For additional information about Veterans First Financial Services, Inc. or VFFS, Inc., please contact firstvet@firstveterans.com.

STRIKING BACK IN THE MEDIA - FINANCIAL EDUCATION FOR THE MILITARY

Examples from two local base newspapers (this page and next) of articles promoting financial literacy and anti-scam education. Military officials, concerned about the presence of consumer scams both in their communities and in the local and national military news media, are slowly beginning to use the media to put out their own counter-messages.

HEY MONEYMAN!

Hey, MoneyMan!

I just recently moved to Jacksonville and I keep getting these phone calls trying to get me to invest money.

I do not know anything about investments and I am afraid these people may rip me off. Do you have any recommendations on where I can go to get good advice?

MoneyMan Sez:

It is good that you are trying to plan ahead. There are lots of different ways to invest – some of them good and some, not so good!

Fortunately, the Fleet and Family Service Center is conducting training on a variety of personal financial management topics later this month.

On March 18 they will be talking about investing and financial planning. On March 19, they will focus on car buying strategies and on March 20 they will be discussing real estate and credit issues.

You can sign up for this free training by calling 542-2766, Ext. 151. Make a call and sign up.

This is great opportunity for everyone and I know they are going to bring in the "experts" to make sure the right information is provided.

After the training, give me a call and let me know how it turned out.

More questions? Call Hey MoneyMan at 778-0353.

BEWARE of PAYDAY LOANS

Loans are fast track to deep debt

By JO2 Jennifer Spinner
Periscope Staff

The loan advertisements are creative and enticing, and they lure consumers with promises of quick cash to help them make ends meet until their next payday. What the ads do not mention, however, is that these payday loans can come at a very high price.

"There are many different names for these loans," said Felipe Gonzalez, financial counselor at the Fleet and Family Support Center. "Some businesses refer to them as cash advance loans, others call them deferred deposit check loans. Regardless of what you call them, the process is the same. Check cashers, finance companies and other businesses are offering small, short-term, high-interest loans to consumers."

In most cases, the borrower writes a personal check, payable to the lender, for the amount borrowed plus a fee. The company gives the borrower the amount of the check in cash, minus a fee.

"These fees are usually a percentage of the face value of the check or a flat fee charged per amount borrowed," said Gonzalez. "If you extend or 'roll over' the loan, let's say for another two weeks, you pay the fees for each extension."

This is a very expensive method of attaining credit and it should only be used as a last resort, according to Gonzales. He used this example to illustrate the true cost of payday loans.

"Let's say you write a personal check for $115 to borrow $100 for up to 14 days. The check casher or payday lender agrees to hold the check until your next payday," said Gonzalez. "When payday comes, the lender deposits the check or you redeem it by paying the $115 in cash. If you can't pay the amount, you pay a fee to extend the loan for another two weeks."

Debt Problems?

Contact the Fleet & Family Support Center or the Navy-Marine Corps Relief Society for help in solving your financial troubles.

In this example, the cost of the initial loan is a $15 finance charge or an APR of 391 percent. If you were to extend the loan three times, the finance charge would climb to $60 for a $100 loan. Gonzalez said there are many alternatives to these costly loans.

"Consumers should really consider their options," he said. "When you need credit, shop carefully and compare offers. Look for the credit offer with the lowest APR or, even better, consider a small loan from your credit union, a small loan company or from family or friends. Always know the terms before deciding on a loan."

Gonzalez said consumers should also consider contacting creditors personally before taking out a quick payday loan.

"Ask your creditors for more time to pay your bills," he said. "Find out what they will charge for that service, whether it's a late charge or additional finance charge or even a higher interest rate, and compare that to what you would pay for a payday loan."

Of course, prevention is the best plan for avoiding credit emergencies. Setting a realistic budget and regularly setting aside money for savings, even in small amounts, can help keep consumers out of debt when emergencies and unexpected expenses pop up.

"This can give you a valuable buffer against financial emergencies, said Gonzalez. "The last thing you need when an emergency situation comes up is to have a mountain of debt to take care after everything is over."

Under the Truth in Lending Act, the cost of payday loans must be disclosed. The borrower must receive in writing the finance charge, expressed as a specific dollar amount and the annual percentage rate. The APR is the annual cost of the credit to the consumer.

The Kings Bay Fleet and Family Support Center offers many programs to educate and assist consumers with credit. If you would like help working out a debt repayment plan with creditors or developing a budget, contact your command financial specialist, the FFSC, or the Navy-Marine Corps Relief Society.

SPEAKING UP ABOUT SCAMS - LETTERS FROM MILITARY OFFICIALS

(next seven pages)

The following letters to officials in three states, from Ret. Admiral Jerome Johnson and Rear Admiral David Architzel, strongly detail the pitfalls for the military of payday lending, check cashing and other "fringe lending institutions" and include specific legislative recommendations. The first letter in the group, also the most recent from April 2003, notes that payday lenders' "negative impact on military readiness is profound."

The military is becoming increasingly vocal in the public arena about scams, and its unique credibility and moral authority on these issues appears to have had decisive impact in at least one state. But the backers of consumer-unfriendly businesses are often stronger politically. One day after Adm. Johnson's April 30, 2003 letter, the North Carolina House passed the bill he was warning against by a 79-32 vote. Adm. Johnson refers to payday lenders' support of the bill in his letter.

Navy-Marine Corps Relief Society
4015 Wilson Blvd., 10th Floor
Arlington, Virginia 22203-1978

Tel:(703) 696-4904
DSN 426-4904
Fax:(703) 696-0144

April 30th, 2003

The Honorable Representatives of the North Carolina House

Dear Representatives:

I am disappointed to learn that the House Financial Institutions Committee gave a favorable report April 29th to House Bill 1213. It is regrettable that you are being encouraged to pass legislation, which re-authorizes the predatory practice of payday lending. The Navy-Marine Corps Relief Society is opposed to charging exorbitant triple-digit interest rates for short-term deferred deposit loans using post-dated personal checks. Payday lending is harmful to our military readiness. It harms the financial stability of our military families and personnel who sacrifice so much to maintain our freedom.

Payday lenders and their national association support HB 1213. There are numerous flaws in this legislation. For example, this bill hurts consumers by imposing excessive interest rates, a compressed 14-day short term for repayment, and other unfavorable terms on borrowers. HB 1213 is designed to legalize the predatory elements of payday lending by trapping consumers in a continuous cycle of debt.

A more consumer friendly bill, HB 1005, has also been introduced but is currently held in the House Rules Committee. This bill is supported by state consumer affairs organizations. Transaction fees with their resulting interest rate and a 90-day period for repayment are more affordable and reasonable. Borrowers will be protected from the coercion and threats practiced by predatory lenders to encourage additional rollover transaction fees and entrapment in a cycle of indebtedness. HB 1005 is clearly the better option for borrowers and will help protect our military personnel from the predatory nature of payday lending.

For several years I have coordinated actions with military commanders and consumer organizations in North Carolina to protect military families from the violation of usury laws by payday lenders. The negative impact on military readiness is profound. For young members of the Armed Services who are experiencing the extraordinary pressure of family separation and deployments, these loans may seem to help with their emergency needs, but most often lead to greater hardship. In 2002, the Navy-Marine Corps Relief Society provided over $276,363 to over 750 service personnel to pay off their payday loans and to protect them from triple-digit interest rates. On no account should you support legislation like HB 1213. Rather, should you be determined to legalize payday lending, it is in the best interest of the targeted group of low-income families to pass HB1005 in its entirety.

Best wishes in your deliberations today and in the days to come and I thank you for your support of our military personnel in North Carolina.

Sincerely,

J. L. Johnson
Admiral, USN (Ret)
President/CEO

Navy-Marine Corps Relief Society
801 North Randolph Street, Suite 1228
Arlington, Virginia 22203-1978

Tel: (703) 696-4904
DSN 426-4904
Fax: (703) 696-0144

August 29, 2000

General Robert F. Milligan, USMC (Ret.)
Comptroller
101 East Gaines Street
Tallahassee, FL 32239

Dear General Milligan:

The purpose of this letter is to request your assistance in curbing abuses by deferred presentment establishments. We greatly appreciate the stand you took when "title lenders' were charging exorbitant interest rates in Florida. Now we need your assistance to rein in an industry that is an even greater financial menace to our service families.

As you know, our Navy-Marine Corps Relief Society is a private, non-profit service organization whose purpose is to provide financial, educational and other assistance to members of the Naval Services of the Unites States. Recently, we have observed a sharp rise in the number of "fringe lending institutions" throughout the United States. A number of euphemisms are used to describe these operators including, payday lenders, cash advance establishments, check cashing services, and cash express offices. No matter how they are described, they are simply lenders that charge extremely high interest rates. Every day a service member visits one of our Navy-Marine Corps Relief Society offices with financial problems that have been greatly aggravated by the usurious charges imposed by these operators. Some of them owe hundreds of dollars in ""fees." An officer for a Navy credit union in Florida recently reported that his credit union processes up to 600 of these checks each month!

These lenders circumvent banking and lending regulations by claiming to be "check cashing" operations. In fact they are accepting post-dated checks on accounts that have insufficient funds, and then holding these checks until payday. Since there is little or no money in the bank when cash is exchanged for the check and the check is held until the next payday before it is deposited, the transaction is, in reality, loan at triple digit interest rates.

The Maryland Division of Financial Regulation recently ruled that these actions were illegal and that the state usury laws would be enforced. Their action will prevent lenders from charging rates in excess of the usury limits and then attempting to enforce the collection of these loans.

A similar ruling in Florida that defines and separates check cashing from deferred presentment and treats the latter as a loan would go a long way toward resolving the problem.

Since 1904.... Helping the Navy and Marine Corps Take Care of Their Own

These transactions could then be governed by the same regulations that apply to other lending institutions.

Problems caused by payday loans and cash advances are similar nationwide. Payday loans become an ongoing financial trap. They are not used on a one-time basis as claimed by the industry. In fact, it has been estimated that only 2% of customers take out just one loan. According to a Wall Street analyst, the average customer makes 11 transactions per year. Payday loan rates are outrageously high. In Colorado, one of the few places in the country that collects actual data from the industry, payday lenders write-off only 3.0% while charging APRs of 485%. Banks write off 2.7% of credit card debt while charging APR's of 15 to 22%.

Despite industry claims to the contrary, there are viable alternatives to payday loans. One such alternative for service members is to seek assistance from NMCRS in the form of an interest free loan or a grant when they have an unforeseen financial need. Other alternatives include:

- Debt management training and education.
- Negotiating payment plans with creditors.
- Using credit cards or secured credit cards.
- Advances from employers.
- Seeking credit union assistance.
- Bank accounts with overdraft protection.
- Lines of credit from finance lenders.

We urge you to take action to stop these abuses. Thank you for your support in protecting the interest of service members and other consumers in Florida.

Sincerely,

Johnson
Admiral, USN (Ret.)
President

Navy-Marine Corps Relief Society
4015 Wilson Blvd., 10th Floor
Arlington, VA 22203-1952

Tel: (703) 696-4904
DSN 426-4904
Fax: (703) 696-0144

August 21, 2002

DEAR MEMBER-NORTH CAROLINA GENERAL ASSEMBLY:

It is my understanding that during the week of August 26th the North Carolina House Finance Committee will hear Senate Bill 104, "Regulate Deferred Deposit," or what is otherwise known as payday lending. I most strongly urge you to protect the men and women of our Armed Forces and other low-income families that are the target of the unscrupulous business called "payday lenders" or "fast cash" franchises. Please let me explain.

I currently serve as the President and CEO of the Navy-Marine Corps Relief Society. Our mission is to provide financial, educational, and other assistance to members of the Naval Services of the United States and their families. In spite of ongoing efforts to educate our Marines and Sailors about predatory lenders, our service members and families continue to borrow money from payday lenders that charge triple-digit interest rates. There can be no question that military families are among the "targeted group". A preponderance of payday lenders and cash advance offices are located in the immediate vicinity of our military installations at Camp Lejeune, Cherry Point, and New River, North Carolina. (Ft Bragg and Pope AFB also apply, but I am representing our experience from severe financial hardship among Marines and Sailors who have requested emergency assistance from the Navy-Marine Corps Relief Society).

Military Commanders such as Rear Admiral Jan Gaudio, Commander, Naval Region Southeast stated that he is "deeply concerned with the problems associated with our Sailors and Marines obtaining payday loans…this practice effects not only our service family, but also operational readiness of the command." The most obvious problem is the high cost for borrowers. Perhaps an even more serious issue is that the loans are designed to entrap the borrower into perpetual debt. One of our consumer studies reported that 77% of payday loans are to borrowers caught on the rollover treadmill with an average interest rate of 499%! In North Carolina in 2001 the average borrower took out 14 payday loans per year, and 96% of the payday loans were to borrowers caught on the repeat treadmill of at least 5 or more loans per year. Last year the NMCRS provided emergency financial assistance for 1086 service families amounting to $205,209 to buyout payday lenders and prevent financial entrapment.

How can you help? I encourage you to insist on the protection of NC consumers and the military families serving in your state. Should a new bill be enacted it must:

- Prohibit the use of a post-dated personal check as collateral for a payday loan. Borrowers have insufficient funds to cover the check and are forced into perpetual fees and rollover of short period loans at triple-digit interest/fees. Some contracts threaten and coerce the military member with prosecution and Bad Conduct Discharge for violation of the Uniform Code of Military Justice for failure to provide repayment funds.

Since 1904.... Helping the Navy and Marine Corps Take Care of Their Own

- Have a minimum loan term of 90 days and allow for partial payments to increase borrower's ability to repay.
- Set a maximum interest on these short-term loans of 36%. It is unscrupulous to violate NC consumer protection laws and charge 375% APR for a two-week loan of $200.
- Forbid payday lenders from using out of state banks and lender franchises as cover for their loan agreements. Again, NC usury laws are bypassed through this arrangement. This is a common practice in your state since August 2001 when the NC payday statute expired.

Thank you for your interest and concern for military families and the consumers of North Carolina.

Sincerely,

J. L. Johnson
Admiral, US Navy (Ret.)

DEPARTMENT OF THE NAVY
COMMANDER
NAVY REGION, MID-ATLANTIC
9324 HAMPTON BLVD
NORFOLK, VA 23505-1273

IN REPLY REFER TO
5800
Ser 00L3/12-02
28 JAN 1997

Virginia House of Delegates
House Commerce and Labor Committee
General Assembly Building
P.O. Box 406
Richmond, VA 23218

Dear Mr. Morgan and Committee Members:

This letter is in regard to HB 1197. The issue of "payday lending" is one of deep concern to the military, and, as Commander of the Navy's Mid-Atlantic Region responsible for the shore commands within Virginia, I want to take this opportunity to communicate my support for the Bill.

"Payday lending," and other similar practices, has a lasting detrimental impact on many of those enticed by the easy availability, yet who are unaware of the true costs. With the tight budgets that most junior enlisted personnel operate on, cash advances, regardless of interest rates, seem an appealing solution to their difficulties. However, for many of these personnel, most with young families, the practice of "payday lending" simply compounds their financial problems by subjecting them to the additional hardships of what are effectively unreasonable interest rates and payment schedules causing even tighter budgets. Although the military has the option of ordering individuals not to do business with certain establishments, by declaring those establishments "off limits," it does not have the authority or ability to sanction the businesses themselves.

The outright ban proposed by HB 1197 represents the most effective remedy for the problem of "payday lending" created for military personnel stationed in Virginia. However, the issue of unreasonable interest rates on short-term loans not covered by HB 1197 is also of concern to the military. This is not to say that the military objects to all short-term loans, only those whose interest rates unfairly burden those individuals who find themselves in financial difficulty despite their dedication to, and self-sacrifice for, their nation.

3883
Ser 00L3/06-00
28 JAN 200

Given my concern for the quality of life of the servicemembers in my Region, I would urge you to vote FOR HB 1197.

The other piece of pending legislation on this topic, HB 970, seems to send the message that "payday lending" is an acceptable lending practice despite the negative impact it has on those in financial hardship. This Bill's attempt to address the issue of unreasonable interest rates, while in theory laudable, fails to address several areas of concern. It does nothing to address lenders who make repeated transactions with the same individual over a short period of time. The proposed bill provides no safeguard for a consumer who makes repeated transactions with multiple lenders. Finally, the proposed transactional rate would still represent a 390% APR on a 14-day loan. For these reasons, I would urge you to vote against HB 970.

Thank you for your time. I hope this information will prove helpful to you in determining the disposition of HB 970 and 1197.

Sincerely,

David Archibel
Rear Admiral, U.S. Navy

2

Federal Register

Friday,
August 31, 2007

Part VI

Department of Defense

32 CFR Part 232

Limitations on Terms of Consumer Credit Extended to Service Members and Dependents; Final Rule

DEPARTMENT OF DEFENSE

Office of the Secretary

32 CFR Part 232

[DOD–2006–OS–0216]

RIN 0790–AI20

Limitations on Terms of Consumer Credit Extended to Service Members and Dependents

AGENCY: Department of Defense (DoD).

ACTION: Final rule.

SUMMARY: The Department of Defense (the Department or DoD) is amending 32 CFR by adding new regulations to implement the consumer protections provisions of Public Law 109–364, the John Warner National Defense Authorization Act for Fiscal Year 2007, section 670, ''Limitations on Terms of Consumer Credit Extended to Service Members and Dependents'' (October 17, 2006). Section 670 requires the Secretary of Defense to prescribe regulations to carry out the new section. The final rule regulates the terms of certain credit extensions to active duty service members and their dependents.

EFFECTIVE DATE: October 1, 2007.

FOR FURTHER INFORMATION CONTACT: Mr. George Schaefer, (703) 588–0876.

SUPPLEMENTARY INFORMATION:

I. Background

Today's joint force combat operations require highly trained, experienced and motivated troops. We are fortunate that today's All Volunteer Force is comprised of individuals who fit the stringent requirements needed for success on the battlefield. The military has seen many changes since it became an All Volunteer Force in 1973. The technological advances over the ensuing 34 years have made remarkable transformations to the capabilities of the Armed Forces.

These advances would not have been as easily attained if it were not for the All Volunteer Force. The members of this force have higher levels of aptitude, stay in the military longer, and as a consequence, perform better than their conscript predecessors. During the Vietnam era draft, 90 percent of conscripts quit after their initial two-year hitch, whereas retention of volunteers is five-times better today—about half remain after their initial (four-year) military service obligation. Said another way, two thirds of the military was serving in its first two years of service prior to 1973, where as today, the number is about one-fourth.

Today's Service members are still younger than the population as a whole, with 46 percent 25 years old or less. Thirty-eight percent of Service members 25 years old or less are married and 21 percent of them have children. This is compared with approximately 13 percent of their contemporaries in the U.S. population 18 through 24 who are married (2000 Census). The majority of recruits come to the military from high school, with little financial literacy education.

The initial indoctrination provided to Service members is critical, providing basic requirements for their professional and personal responsibilities and their successful adjustment to military life. Part of this training is in personal finance, which is an integral part of their personal, and often, professional success. The Department of Defense (the Department) continues to provide them messages to save, invest, and manage their money wisely throughout their career.

Service members and their families are experiencing the sixth year of the Global War on Terror. The Department views the support provided to military families as essential to sustaining force readiness and military capability. From this perspective, it is not sufficient for the Department to train Service members on how best to use their financial resources. Financial protections are an important part of fulfilling the Department's compact with Service members and their families.

Social Compact

The Department believes that assisting Service members with their family needs is essential to maintaining a stable, motivated All Volunteer Force. As part of the President's February 2001 call to improve the quality of life for Service members and their families, the Department developed a social compact reflecting the Department's commitment to caring for their needs as a result of their commitment to serving the Nation. The social compact involved a bottom-up review of the quality-of-life support provided by the Department, which articulated the linkage between quality-of-life programs as a human capital management tool and the strategic goal of the Department—military readiness.

The social compact is manifested in the programs the Department provides to support the quality of life of Service members and their families. This social compact includes personal finances as an integral part of their quality of life. The Department equates financial readiness with mission readiness. When asked in 2005 on a blind survey to rate the stressors in their lives, Service members (as a group) rated finances as a more significant stressor than deployments, health concerns, life events, and personal relationships. They only rated work and career concerns as a higher stressor in their lives. As part of the social compact for financial readiness, the Department established a strategic plan to:

- Reduce the stressors related to financial problems. The stress associated with out-of-control debt impacts the performance of Service members and has a major negative impact on family quality of life.
- Increase savings. Establishing personal and family goals, helps motivate Service members to control their finances and live within their means.
- Decrease dependence on unsecured debt. This reduces the stressors and vulnerabilities associated with living from paycheck to paycheck.
- Decrease the prevalence of predatory practices. This provides protection from financial practices that seek to deceive Service members or take advantage of them at a time of vulnerability.

The Department has taken action to obtain these outcomes by providing financial awareness, education, and counseling programs; by advocating the marketplace deliver beneficial products and services; and by advocating for the protection for Service members and their families from harmful products and practices.

Financial Education

The Military Services are expected to provide instruction and information to fulfill the needs of Service members and their families. To this end, the Department established a policy in November 2004: DoD Instruction 1342.27, *Personal Financial Management Programs for Service Members.*

As outlined in the Government Accountability Office (GAO) Report 05–348, the Military Services have their own programs for training first-term Service members on the basics of personal finance. These programs vary in terms of venue and duration; however, all Military Service programs must cover the same core topics to the level of competency necessary for first-term Service members to apply basic financial principles to everyday life situations.

The Department has tracked the ability of Service members to pay their bills on time as a reflection of their competency and ability to apply basic financial principles. Since 2002, self-

reported assessments through survey data have shown Service members are doing a better job keeping up with their monthly payments.

To assist the Military Services in delivering financial messages, the Department established the Financial Readiness Campaign in May 2003, which has gathered the support of 26 nonprofit organizations and Federal agencies. In the past three years, Service members have benefited from the materials and assistance from over 20 active partnerships. These partnerships are on-going and have been developed to allow the Military Services to choose which partner programs can best supplement the education, awareness, and counseling services they provide. The materials and services supplement but do not take the place of the programs offered by the Military Services.

Aspects of predatory lending practices are covered as topics in initial financial education training and in refresher courses offered at the military installations and aboard ships. The Military Services annually provide over 10,000 classes and train approximately 24 percent of the force, as well as nearly 20,000 family members. These classes are primarily conducted on military installations located in the United States.

In addition to these classes, Financial Readiness Campaign partner organizations conduct over a thousand classes informing over 60,000 Service members and family members per year. These classes are primarily provided by the staff of banks and credit unions located on military installations (military banks and defense credit unions). These institutions provide these classes as part of their responsibilities outlined in the DoD Financial Management Regulation. Other organizations involved include local Credit Counseling Agencies, State financial regulatory agencies, the InCharge Institute, and the NASD Foundation.

The Military Service financial educators, along with partner organizations, also distributed over 200,000 brochures and pamphlets, with the Military Services and the Federal Trade Commission primarily providing these products. In addition, *Military Money Magazine* has run several articles, to include two cover articles on predatory lending. The magazine is free and is distributed through military commissaries, family support centers and other service agencies on the installation, as well as to residents on installation and to addresses off the installation upon request. The distribution is approximately 250,000 per quarter.

Lending Practices Considered Predatory

As identified in GAO Report 05–349, *DOD's Tools for Curbing the Use and Effects of Predatory Lending Not Fully Utilized,* April 2005, the review of practices that are considered predatory has not benefited from a consistent definition that has been universally applied. However, sources studying the issue of predatory lending have focused on similar characteristics. GAO Report 04–280, *Federal and State Agencies Face Challenges in Combating Predatory Lending,* January 2004, said the following:

> While there is no uniformly accepted definition of predatory lending, a number of practices are widely acknowledged to be predatory. These include, among other things, charging excessive fees and interest rates, lending without regard to borrowers' ability to repay, refinancing borrowers' loans repeatedly over a short period of time without any economic gain for the borrower, and committing outright fraud or deception.

This definition has been reiterated in the FDIC Office of the Inspector General Audit Report 06–0111, June 2006, which stated:

> Characteristics associated with predatory lending include, but are not limited to, (1) Abusive collection actions, (2) balloon payments with unrealistic repayment terms, (3) equity-stripping associated with repeat financing and excessive fees, and (4) excessive interest rates that may involve steering a borrower to a higher-cost loan.

These same characteristics were also identified in the DoD Report to Congress on *Predatory Lending Practices Directed at Members of the Armed Forces and Their Dependents,* August 9, 2006:

> Predatory lending in the small loan market is generally considered to include one or more of the following characteristics: High interest rates and fees; little or no responsible underwriting; loan flipping or repeat renewals that ensure profit without significantly paying down principal; loan packing with high cost ancillary products whose cost is not included in computing interest rates; a loan structure or terms that transform these loans into the equivalent of highly secured transactions; fraud or deception; waiver of meaningful legal redress; or operation outside of state usury or small loan protection laws or regulations. The effect of the practices include whether the loan terms or practices listed above strip earnings or savings from the borrower; place the borrower's key assets at undue risk; do not help the borrower resolve their financial shortfall; trap the borrower in a cycle of debt; and leave the borrower in worse financial shape than when they initially contacted the lender.

While the Report to Congress provides a more expansive definition, there are several commonalities among the definitions listed above:

- Lending without regard of the borrowers ability to repay;
- Excessive fees and excessive interest rates;
- Balloon payments with unrealistic repayment terms;
- Wealth stripping associated with repeat rollovers/financing; and
- Fraud and deception.

The Department started collecting information on high cost lending in 2004 as part of the Defense Manpower and Data Center annual surveys of active duty Service members. The survey requested input on payday loans, rent-to-own, refund anticipation loans and vehicle title loans. GAO Report 05–359 focused on these four practices and obtained feedback from command leaders, Personal Financial Management (PFM) program managers, command financial counselors, legal assistance attorneys, senior noncommissioned officers (pay grades E8 to E9), chaplains, and staff from the military relief/aid societies. Data from these and others indicate that providers of such loans may be targeting Service members.

The Report to Congress reviewed five products (payday loans, vehicle-title loans, rent-to-own, refund anticipation loans, and military installment loans) identified by installation-level financial counselors (employed as PFM program managers and employed by the Military Aid Societies) and legal assistance attorneys who regularly counsel service members on indebtedness issues. When compared against the common characteristics listed above, the five products reviewed in the Report to Congress measure up somewhat differently:

Lending product	Without regard for borrowers' ability to repay	Excessive fees and interest	Unrealistic payment schedule	Repeated rollover/refinancing
Payday loan	X	X	X	X
Vehicle title loan	X	X	X	X

Lending product	Without regard for borrowers' ability to repay	Excessive fees and interest	Unrealistic payment schedule	Repeated rollover/refinancing
Military installment loan		X		
Refund anticipation loan		X		
Rent-to-own	X	X		

A major concern of the Department has been the debt trap some forms of credit can present for Service members and their families. The combination of little-to-no regard for the borrower's ability to repay the loan, unrealistic payment schedule, high fees, and interest and the opportunity to roll over the loan instead of repaying it, can create a cycle of debt for financially overburdened Service members and their families.

Consumer groups, news media, and academics have chronicled concerns about payday loans and the propensity for this lending practice to create a cycle of debt. For example, M. Flannery and K. Smolyk state the following in their June 2005 FDIC Financial Research Working Paper No. 2005–09:

> Although as economists we find it hard to define what level of use is excessive, there seems little doubt that the payday advance as presently structured is unlikely to help people regain control of their finances if they start with serious problems.

Likewise, vehicle title loans are similarly structured, with potentially similar results. According to a November 2005 report by the Consumer Federation of America, vehicle title loans are generally made for 30 days with high interest/fee structures (average of 295 Annual Percentage Rate (APR)). Limits on title loans vary by State concerning interest rates, duration, rollover allowances, and rules on repossessing the vehicle. Only four states cap interest rates at less than 100% APR. In many states these loans can be rolled over by the borrower several times if the borrower is unable to pay the principal and interest when due. If not paid or rolled over, many states allow the creditor to repossess the vehicle and in some states the borrower is not entitled to any portion of the proceeds of the vehicle sale. Loan amounts average 55 percent of the value of the vehicle.

Rent-to-own, refund anticipation loans, and some military installment loans present products with high fees and interest. Rent-to-own, which is not covered as credit under the Truth-in-Lending Act (TILA), can represent an expensive alternative to credit when used as a means of purchasing an item. Military installment loans (an installment loan marketed primarily or exclusively to the military) can represent a high cost over the duration of the loan, particularly when other charges are added to the interest rate. Tax refund anticipation loans (RALs) also cost Service members and their families high fees when they can easily obtain rapid returns through electronic filing with the assistance of their installation legal assistance office.

According to the Consumer Federation of America (report dated February 5, 2007) the advantage of RALs is minimal when comparing the speed of the refund (between 7 and 14 days faster) against the cost of the service ($30—$125). Moreover, the APR for this credit can be triple digit. A study by Gregory Elliehausen of the Credit Research Center (CRC) (Monograph #37, April 2005) showed a disproportionate percentage of individuals under 35 years old use RALs. Sixty-one percent of RAL borrowers were below 35 years old, although individuals below 35 years old represent 28.6 percent of heads of households. This is significant since 79 percent of Service members are 35 years old or below.

The reason for using RALs vary. The CRC study showed that 41 percent of borrowers obtain RALs to pay bills, 21 percent due to unexpected expenditures, 15 percent to make purchases, 15 percent because of impatience, and 7 percent for other reasons. Less than one percent said they obtained a RAL to pay for tax preparation. Through the Armed Forces Tax Council, in collaboration with the IRS, Volunteer Income Tax Assistance sites are located on most active duty military installations to assist Service members and their families with preparation and electronic filing of their tax returns.

As with other forms of short-term, high cost credit, the Department would prefer Service members and their families to consider low cost alternatives to resolve their financial crisis by establishing a more solid footing for their personal finances. The CRC study found that users of RALs and payday loans both had similar levels of debt and patterns of credit use. Additionally, through education the Department attempts to persuade Service members that planning is an important part of managing finances, and a high cost 10-day loan does not reinforce this lesson.

The five products reviewed in the Report to Congress represent two kinds of financial problems for Service members and their families: Those products that contribute to a cycle-of-debt (payday and vehicle title loans) and those products that can cost the military consumer high fees and interest costs (rent-to-own, installment loans and refund anticipation loans). Cycle of debt represents a more significant concern to the Department than the high cost of credit.

The Department considered the five products in developing the regulation. Trade associations and financial institutions expressed their concern that the regulation needed to be very clear about when the provisions of the statute applied. During our consultation with the Federal regulatory agencies, they reiterated the need for ''clear lines'' around definitions of covered consumer credit and the impacted creditors.

The regulation has focused on credit products that have, in general practice, terms that can be detrimental to military borrowers. Rent-to-own services provide rental opportunities (not covered by the Department's rule making), as well as options for ownership which are not loans under TILA. As a consequence, rent-to-own products and services were not covered. Likewise, there are installment loans with favorable terms and some with terms that can increase the interest rate well beyond the limits prescribed by 10 U.S.C. 987. Isolating detrimental credit products without impeding the availability of favorable installment loans was of central concern in developing the regulation. Consequently, installment loans that do not fit the definition of ''consumer credit'' in Section 232.3(b), including the definition of ''payday loans,'' ''vehicle loans,'' or ''tax refund anticipation loans'' are not covered by the regulation. The Department's intent is to balance protections with access to credit. The protections posed in the statute assist Service members, when applied with precision to preclude unintended barriers.

Alternatives

The Department prefers that Service members and their families who experience financial duress seek help through Military Aid Societies, military banks and defense credit unions rather than credit products that would more likely mire them in a cycle of debt. These institutions have established programs and products designed to help Service members and their families resolve their financial crises, rebuild their credit ratings and establish savings.

The Military Aid Societies are strong advocates for limiting the cost associated with credit and for creditors to develop alternative products for Service members who cannot otherwise qualify for loans. Within their own resources they provided $87.3 million in no-cost loans and grants to Service members and their families in 2005. These funds were provided for emergencies and essentials, such as rent, food, and utilities.

Financial institutions located on military installations also understand the need to provide products and services that can help those who mishandle their finances and who may need remedial assistance. A review of on-base financial institutions surfaced 24 programs on 51 military installations in the U.S. providing alternative small loan products designed to help Service members and their families to recover from their financial problems. These financial institutions supplement the emergency funding made available by the nonprofit Military Aid Societies that provide grants and no-interest loans to needy Service members and families.

These financial institutions provide low denomination loans at reasonable APRs designed to assist their members who need to get out of high cost credit and into more traditional lending products. Financial counseling and education are often prerequisites for the short term loans and some institutions have attached a requirement to develop savings as part of the loan.

Many of these military banks and credit unions use their products and services to maintain a watchful eye over their members to ensure they do not abuse services designed to assist them, such as overdraft protection, which if used on a chronic basis, can become very expensive and propel someone already overextended into a deeper spiral of debt. Representatives of the Association of Military Banks of America had an opportunity to showcase their alternative small loan products at a FDIC Conference in December of 2006. FDIC hosted this conference to spotlight the need to develop more of these types of products for Service members and their families and several financial institutions described above that currently provide such favorable credit to Service members participated in the conference.

Subsequent to the conference, FDIC issued guidelines to FDIC-supervised banks to encourage them to offer affordable small-dollar loan products. These guidelines explore a number of aspects of developing alternative small loan products, including affordability and streamlined underwriting. They also discuss tools such as financial education and savings that may address long-term financial issues that concern borrowers.

At the same time, the FDIC approved a two-year pilot project to review affordable and responsible small-dollar loan programs in financial institutions. The project is designed to assist institutions by identifying information on replicable business models for affordable small-dollar loans. FDIC expects to identify best practices resulting from the pilot that will become a resource for institutions. The Department supports the FDIC's efforts with the guidelines and the pilot project as they both will help encourage banks to meet the demand for small-dollar loans at more reasonable costs for the borrower.

Efforts To Curb the Prevalence and Impact of Predatory Loans

The Department has found that it has a small window of opportunity to convince and inform Service families about products and services beneficial to their particular situations, a job complicated by many contrary messages and enticements. Nonetheless, the Department has attempted to use the processes and resources available within the Department to curb the prevalence of high cost short term lenders, particularly those that can contribute to a spiral of debt.

Predatory lenders have seldom been placed off-limits, primarily because the process associated with placing commercial entities off-limits, through the review and recommendations of the Armed Forces Disciplinary Control Board (AFDCB), is not well suited to this purpose. The AFDCB, covered by Joint Army Regulation 190–24, is designed to make businesses outside of military installations aware that their practices raise morale and discipline concerns and to offer these businesses an opportunity to modify their practices to preclude being placed off-limits. When the commercial entity refuses to comply, the AFDCB recommends that the regional command authority place the business off-limits for all Service members within the region (regardless of Service).

Normally concerns are raised when a business has violated State or Federal laws. Remediation involves the business curtailing these illegal practices. In the case of the loan products listed above, businesses usually offer their services within the legal limits. Since the AFDCB takes on businesses one at a time, bringing a lender under scrutiny has been difficult if the lender is complying with the same rules as its competitors. Additionally, the magnitude of mediating with the number of outlets surrounding military installations has exacerbated the process. Numerous payday lenders can be found in communities around military installations (Graves and Peterson, Ohio State Law Journal, Volume 66, Number 4, 2005).

Also without clear standards and prohibitions, commanders and AFDCBs cannot easily identify what remediation lenders offering payday, auto title, and refund anticipation loans should take. In states without relevant laws, Commanders and AFDCBs must not only establish rules, but they must also educate those affected and then monitor their compliance.

As stated above, the Department will continue to provide education, awareness, and counseling programs to influence skills and attitudes towards managing personal resources wisely. There still remains a gap between the opportunity to influence a young Service member or family member concerning the best way to manage their finances, and the level of experience and capability necessary to be successful. The Department has a limited opportunity to impress upon these young people the importance of managing their resources. It does not have sufficient control over the behavior of Service members and their families to preclude them from taking on financial risks that can detract from not only their quality of life, but also military mission accomplishment.

The Department will continue to send Service members messages that they and their families need to manage their resources wisely for their own benefit and to maintain personal readiness. The Department's call for responsibility competes with market messages from the sub-prime financial industry to get cash now for purchases, vacations, and paying bills. Their marketing stresses the ease and convenience of obtaining these loans, with a virtual guarantee of approval. These messages can be particularly alluring to Service members

and families already overburdened with bills and debts. A 2006 survey accomplished by the Consumer Credit Research Foundation concluded that Service members choose payday loans primarily because they are convenient. Certainly, obtaining ''fast cash'' from a payday lender is far easier than coming to terms with delinquent debt or addressing inherent overspending that creates situations where sub-prime loans are needed.

Service members have inherently understood that limits on interest rates are appropriate, even if these limits would decrease the availability of credit. When asked in a 2006 survey conducted by the Consumer Credit Research Foundation if Service members strongly agree, somewhat agree or disagree with the statement: ''The government should limit the interest rates that lenders can charge even if it means fewer people will be able to get credit,'' over 74 percent of the Service members surveyed agreed with the statement (over 40 percent strongly agreed). Similarly when asked their position on the statement ''There is too much credit available today,'' 75 percent of Service members not using payday loans and 63 percent of Service members using payday loans agreed (51 percent of non-users strongly agreed).

''Limitations on Terms of Consumer Credit Extended to Service Members and Dependents,'' John Warner National Defense Authorization Act for Fiscal Year 2007, Section 670, Codified at 10 U.S.C. 987

10 U.S.C. 987 directs the Secretary of Defense to establish and implement regulations concerning consumer credit services for Service members. Implementing regulations must be completed and published prior to October 1, 2007, after consultation with the Department of Treasury, Office of the Comptroller of the Currency, Office of Thrift Supervision, Board of Governors of the Federal Reserve System, Federal Trade Commission, Federal Deposit Insurance Corporation, and the National Credit Union Administration. Specifically, section 987(h)(2) requires the Secretary of Defense to issue regulations establishing the following:

(A) Disclosures required of any creditor that extends consumer credit to a covered member or dependent of such a member.

(B) The method for calculating the applicable annual percentage rate of interest on such obligations, in accordance with the limit established under this section.

(C) A maximum allowable amount of all fees, and the types of fees, associated with any such extension of credit, to be expressed and disclosed to the borrower as a total amount and as a percentage of the principal amount of the obligation, at the time at which the transaction is entered into.

(D) Definitions of ''creditor'' under paragraph (5) and ''consumer credit'' under paragraph (6) of subsection (i), consistent with the provisions of this section.

(E) Such other criteria or limitations as the Secretary of Defense determines appropriate, consistent with the provisions of this section.

This broad latitude allows the Department to determine the scope and impact of the regulation, consistent with the provisions of the statute. These provisions have been established to protect Service members and their families from potentially abusive lending practices and products. The statute provides several limitations on credit transactions, and allows the Department to focus these limitations on areas of greatest concern.

As noted in the preamble to the proposed rule, the Department has learned of the potential for unintended consequences that could adversely affect credit availability if it were to adopt a broadly applicable regulation. Some comments received suggested that one way to limit the potential adverse and unintended consequences of the statute would be to adopt a regulation that provided for a general or conditional exception for credit products offered by insured depository institutions and their subsidiaries. While the proposed rule did not include any exceptions for insured depositories or their subsidiaries, the Department explicitly asked for comment on the issue.

Most respondents to the request for comments addressed the question of whether the final rule should exclude insured depository institutions from coverage generally or in limited circumstances. Almost all representatives of insured depository institutions strongly supported the Department exempting lenders that are subject to supervision by a Federal banking agency. They noted that these institutions have not been identified as engaging in predatory lending practices. Consumer representatives, on the other hand, as well as the FTC staff who provided comment on this issue, did not favor making distinctions in the ''creditor'' definition based on whether or not the lender was subject to supervision by Federal banking agencies.

Comments from lending institutions about the need for a general or limited exemption of Federally-insured depository institutions and their subsidiaries from this regulation were tempered in part by their support of the proposed definition of ''consumer credit,'' which is limited to potentially abusive credit products identified by the Department in its report to Congress. Specifically, they noted that if the regulations were expanded to cover a wider range of financial products, the need for an exemption of insured depository institutions from this regulation would be increased to ensure that Service members and their dependents have access to affordable credit by responsible lenders.

The intent of the statute is clearly to restrict or limit credit practices that have a negative impact on Service members without impeding the availability of credit that is benign or beneficial to Service members and their families. The Department has determined that given the limited types of credit products covered by the rule, an exemption for depository institutions is not needed to ensure access to beneficial credit by Service members and their dependents. Accordingly, the final rule does not provide exemptions for insured depository institutions or their subsidiaries. As noted above, Federally-supervised financial institutions that commented appeared to be concerned about future iterations of the regulation and the potential for the regulation to impact their ability to provide beneficial credit to Service members and their families. If the Department considers it necessary to reconsider the products included as covered consumer credit, the issue of such exemptions would also be reconsidered.

II. Description of the Regulation, by Section

232.1 and 232.2, Authority, purpose and coverage, and Applicability: No comments were received on these provisions. The provisions in the proposed rule are being adopted without substantive change.

232.3, Definitions: In implementing the statute, the Department has defined the terms ''creditor'' and ''consumer credit'' judiciously, having heard from numerous groups through comments received in response to **Federal Register** notice DoD–2006–OS–0216, solicited and unsolicited comments, and through meetings requested of the Department that applying the provision broadly would create numerous unintended consequences. These unintended consequences would have a ''chilling effect'' on the availability of consumer credit for Service members and their dependents in circumstances that are not necessarily predatory.

In defining the term ''creditor,'' the statute provides the following:

(5) CREDITOR.—The term ''creditor'' means a person—

(A) Who—

(i) Is engaged in the business of extending consumer credit; and

(ii) Meets such additional criteria as are specified for such purpose in regulations prescribed under this section; or

(B) Who is an assignee of a person described in subparagraph (A) with respect to any consumer credit extended.

Consistent with the statute, the final rule defines ''creditor'' as any person who extends consumer credit covered by part 232. For this purpose a ''person'' includes both natural persons as well as business entities, but would exclude governmental entities. Pursuant to the Department's authority to specify additional criteria, a person would be a creditor only if the person is also a ''creditor'' for purposes of the Truth in Lending Act (TILA). Section 987(c) of 10 U.S.C. provides that the disclosures required by that section be presented along with the disclosures required under TILA, and in accordance with the terms prescribed by the regulations implementing TILA. Thus, it does not appear that section 987 was intended to apply to persons or transactions that are not covered by TILA.

For clarity, the Department has implemented the provision covering assignees by including a specific reference to assignees in each section of the regulation that would apply to an assignee, in lieu of including assignees in the definition of ''creditor.'' See sections 232.4, 232.8 and 232.9.

The definition of consumer credit provided in the statute is as follows:

(6) CONSUMER CREDIT.—The term ''consumer credit'' has the meaning provided for such term in regulations prescribed under this section, except that such term does not include (A) A residential mortgage, or (B) a loan procured in the course of purchasing a car or other personal property, when that loan is offered for the express purpose of financing the purchase and is secured by the car or personal property procured.

It is clearly the intent of the statute that the Department define which types of consumer credit transactions shall be covered by the law, provided that they do not include the two listed exemptions. This is because the statute authorizes the Department to specify additional criteria for an entity to be considered a creditor that is engaged in the business of extending consumer credit. The Department has exercised this authority by limiting the rule's applicability to creditors that engage in certain types of consumer credit transactions. Accordingly, the final rule focuses on three problematic credit products that the Department identified in its August 2006 *Report to Congress on the Impact of Predatory Lending Practices on Members of the Armed Forces and Their Dependents:* payday loans, vehicle title loans, and refund anticipation loans. The Department's definition of the term ''consumer credit'' in the proposed rule was intended to narrow the regulation's impact to consumer credit products and services that are potentially detrimental and for which there are DoD-recommended, alternative products or services available to Service members and their dependents. DoD believes that a narrow definition will prevent unintended consequences while affording the protections granted by the statute.

After review of comments received through the **Federal Register** publication of the proposed rule, the Department believes that the scope of the regulation as proposed is appropriate to address the concerns that formed the basis of its report to the Congress. Comments received from consumer advocates and some others expressed the view that the Department's proposed definition of ''consumer credit'' was too narrow and that creditors could restructure their loan products to make high-cost extensions of credit while avoiding coverage under Part 232. Comments received from representatives of federally-insured depository institutions generally supported the consumer credit definition in the proposed rule.

The Department continues to believe that the scope of the proposed rule and the definition of consumer credit are appropriate. The Department maintains the ability to issue additional rules in the future and the Department plans to continue surveying Service members and their dependents to collect data on their use of credit products. The Department will also monitor market developments that affect Service members and will obtain a variety of inputs from regulatory agencies, consumer protection groups and the credit industry to assess the level of protection provided by the final rule. The Department will review this data to determine if further revisions are needed. Accordingly, the proposed definition of ''consumer credit'' is being adopted without substantive change. The Department has made technical changes to the regulation to clarify that the consumer credit defined in the regulation is closed-end credit and not open-end credit.

With respect to exclusion of ''residential mortgages'' the final rule adopts the proposed rule's exclusion which applies to any credit transaction secured by an interest in the borrower's dwelling. Thus, home-purchase transactions, refinancings, home-equity loans, and reverse mortgages would be excluded. Home equity lines of credit are also excluded. In addition, the property need not be the consumer's primary dwelling to qualify for the exclusion. A ''dwelling'' includes any residential structure containing one to four units, whether or not the structure is attached to real property, and would also include an individual condominium unit, cooperative unit, mobile home, or manufactured home.

Payday Loans

Payday loans have common characteristics that make them detrimental to a Service member's financial well being and inferior to alternative sources of emergency support. These characteristics can exacerbate a cycle of debt, particularly if the borrower is already over-extended through the use of other forms of credit. The final rule defines ''payday loans'' based on certain characteristics, in order to distinguish them from other financial products. A payday loan is defined as *a closed-end credit transaction having a term of 91 days or fewer, where the amount financed does not exceed $2,000.* The ''amount financed'' is not defined in this regulation, but must be determined based on the definition of that term in the Federal Reserve Board's Regulation Z, which implements the TILA. In addition, the definition of ''payday loan'' is limited to transactions where the borrower contemporaneously provides a check or other payment instrument that the creditor agrees to hold, or where the borrower contemporaneously authorizes the creditor to initiate a debit or debits to the covered borrower's deposit account.

Payday loans, otherwise known as deferred presentment loans, are allowed in 39 States as a separate credit product from other forms of credit regulated by Federal or State statute. States authorizing these types of loans require payday lenders to obtain a license to operate within the State. States have defined these products and services, primarily through the basic process used to secure a payday loan, either through holding a check or by obtaining access to a bank account through electronic means. These basic processes have been included as part of the definition of payday loans in the regulation (Section 232.3(c)). Many States have also established limits to the amount that can be borrowed and the duration of the loan as part of the authorized activities of lenders licensed to offer these products and services. A review of State limits for payday loans

establishes a foundation for the definition used in this regulation.

The majority of States have a maximum dollar amount, maximum time limits and maximum fees that trigger regulation. Six States (New Mexico, Oregon, Texas, Utah, Wisconsin and Wyoming) have no dollar limit on the amount that can be loaned, and nine States (Alaska, Arizona, Idaho, New Mexico, Rhode Island, South Dakota, Virginia, Wisconsin and Wyoming) have no maximum limit established for the duration of a payday loan. Of the States that impose limits on the loan amount or loan duration, the highest dollar limit is $1,000 (Idaho and Illinois) and the longest permissible loan term is 180 days (Ohio). The average dollar limit is $519 and the average limit on loan term is 46 days.

Payday loans offered over the internet often originate in States with no limits on fees or maximum loan amounts. A survey of websites offering payday loans indicates $1,500 as generally the maximum amount loaned. A review of sites marketing ''Military Payday Loans'' refer to loans of up to 40 percent of a Service member's take home pay. This amount can vary considerably based on rank, other entitlements, tax withheld and military allotments. For married enlisted Service members in the grade of E–6 and below (no deductions for taxes or other allotments), the $2,000 limit in the final rule would cover a loan made for 40 percent of take-home pay. The limits established in the definition for payday loans reflect the maximum duration and amount anticipated for loans based on current State practices, to include internet payday loans originating from locations without limits.

Many respondents expressed some concern that the four-part definition of payday loans may allow creditors to change one aspect of their product to evade the regulation, such as extending the length of the loan or extending open-end credit. The Department's intent is to balance these concerns against the concerns expressed by other respondents that the definition should remain as narrow as proposed to preclude unintended consequences regarding short-term, small-dollar credit availability for covered borrowers. Most financial institutions requested that the definitions of consumer credit clearly specify that they apply to closed-end loans to preclude misinterpretations.

Industry and consumer group respondents requested clarification of the payday loan definition. Specifically, they sought to clarify that borrowers must provide a check to the creditor or authorize a debit to the borrower's deposit account contemporaneously with the borrower's receipt of funds, and not contemporaneously with the payment of interest or fees. Section 232.3(b)(1)(i) of the final rule has been modified to make this clarification.

The definition of ''payday loans'' includes transactions where the covered borrower receives funds and contemporaneously authorizes the creditor to initiate a debit or debits to the borrower's deposit account. However, there is an exclusion to this definition in 232.3(b)(1)(i)(A): ''*This provision does not apply to any right of a depository institution under statute or common law to offset indebtedness against funds on deposit in the event of the covered borrower's delinquency or default.*'' This exclusion only applies to a depository institution's right of offset under State or other applicable law.

Vehicle Title Loans

The Department believes that vehicle title loans should be included within the definition of consumer credit, and that covering such transactions is consistent with the law's purpose. The definition for ''vehicle title loans'' limits the rule's coverage to loans of 181 days or fewer. Many States have not established statutes overseeing these loans. A 2005 survey of States conducted by the Consumer Federation of America found that, of the 16 States authorizing vehicle-title lending, 10 require 30-day or one-month term limits (with authorized renewals or extensions), and one State allows up to 60 days (with 6 renewals). Four States do not establish term limits.

Some consumer groups remarked that the scope of the definition for vehicle title loans may not encompass all practices used by creditors to provide high-cost, short-term vehicle title loans. Some industry respondents said the restrictions in the regulation may make some creditors reluctant to offer beneficial loans to covered borrowers with poor or no credit history. However, the majority of federally-insured depository institution respondents said that their loans that use vehicles as collateral would be unaffected since they are made for longer than 181 days.

As with payday loans, the Department has sought to balance the definition of vehicle title loans to reflect the countervailing concerns of respondents. The Department does not want protections from high-cost, short-term vehicle title loans to unnecessarily inhibit covered borrowers from accessing beneficial loans for which a vehicle is used as collateral.

Comments received from a group of bank trade associations asked that the rule clarify that ''motor vehicle'' only includes vehicles which must be registered pursuant to state law. The final rule has been modified to make this clarification.

Refund Anticipation Loans

The Department believes that covering RALs is consistent with the intent of the statute. They have been included because survey data has shown RALs to be the second most prevalent high cost loan used by Service members, and because alternatives that can expedite their tax returns are available, generally at no cost. Some states have also addressed concerns with RALs. Connecticut has established a rate cap for RALs, prohibiting transactions where the APR exceeds 60 percent. Other states, such as California, Washington, Oregon, and Nevada, have established statutes specifying disclosure requirements for RALs. Respondents representing tax preparers and financial institutions providing RALs objected to being included in the definitions of covered consumer credit products, stating their product does not contribute to a cycle of debt or place a critical family asset at risk.

Credit union trade association respondents and bank trade association respondents said the inclusion of RALs in the rule would have little impact on their members because so few of them make these loans, and the few that do make them will likely cease doing so because of the rule's requirements. The Department believes that its definition of RALs limits unintended consequences and allows for refunds to be provided expeditiously.

One commenter expressed concern that the rule could be construed to apply when a borrower notes that the source of repayment is the tax refund. The intent of the regulation is to cover credit products that are designed expressly to use tax refunds as the collateral for the loan. The rule does not cover loans where borrowers merely note that a tax refund may be used to repay the advance. To ensure the Department's intent is clear, the word ''expressly'' has been repeated in the RAL definition to modify the statement concerning repayment of the loan.

Loans Where the MAPR Is Less Than 24%

In its proposal the Department solicited comments on other approaches that would encourage lenders to offer responsible, small-dollar, short-term loans that meet the credit needs of Service members and their dependents. For example, comment was solicited on whether loans should be exempt from

coverage under Part 232 if the MAPR were less than 24%.

Industry respondents generally said that such an exemption would have little impact on credit products defined in the regulation because the credit product definitions are already narrow enough in scope to leave institutions room to provide affordable small-dollar loans to Service members and their dependents. Some consumer groups favored such an exemption only if it were part of a ''safe harbor'' accompanied by significantly broader definitions of covered credit products. The Department has not adopted an MAPR-based exemption from the definition of consumer credit in the final rule to include this recommendation. To accommodate current and potential small-dollar, short-term loan programs, the Department has already made allowances in the regulation for credit products that are within the MAPR limit of section 232.4(b) and believes these are sufficient to support lower cost alternatives.

Definition of MAPR

The definition of MAPR creates a distinctive percentage rate that reflects the provisions of the statute. The MAPR does not include fees imposed on the borrower for unanticipated late payments, default, delinquency or a similar occurrence, because such fees are imposed as a result of contingent events that may occur after the loan is consummated. Thus, such fees are not included in the computation of the maximum 36% MAPR cap imposed by these rules.

Many respondents expressed concern that disclosing both an MAPR and an APR to Service members and their dependents would cause confusion. The statute requires that the MAPR be presented to the covered borrower. The Department will take steps to educate Service members and their dependents on the MAPR.

While acknowledging that the narrow scope of the rule will ease the potential for confusion, comments from industry representatives sought to modify the MAPR definition to make it as close as possible to the APR disclosed under TILA. By contrast, consumer groups contended that the MAPR definition should include all cost elements, and should not contain exclusions in the proposed rule, such as for actual unanticipated late payments.

The Department has designed the definition of MAPR within the context of the consumer credit covered by the regulation. The Department's intent is to ensure that the credit products covered by the regulation cannot evade the 36 percent limit by including low interest rates with high fees associated with origination, membership, administration, or other cost that may not be captured in the TILA definition of APR.

Some industry respondents were concerned about including costs in the MAPR that are ''associated with the extension of consumer credit'' because this may include costs for products or services that are purchased in connection with a loan, but are not required. For example, industry respondents argue that ancillary products (such as voluntary credit insurance and debt cancellation coverage) should not be included in the MAPR calculation because these products may protect borrowers against being burdened with debt if a covered event occurs.

The Department believes the definition is consistent with the statute and is appropriate in the context of the consumer credit covered by the rule. The Department is concerned that Service members are sold products such as voluntary insurance without having these credit insurance products placed in the context of the Service member's employment status or his or her current level of insurance coverage. Additionally, the Department is concerned about small loans that are associated with sales of products or services not related to the loans, such as credit offered as part of Internet access or catalog sales. The definition has been designed to cover sales such as these or sales similar to those mentioned in this paragraph and considers them ''associated with the extension of consumer credit.''

One commenter expressed concern that only fees for ''actual unanticipated'' late payments would be excluded from the MAPR, because some borrowers might notify the lender if they know their payment will be late. The language in the proposed rule tracks the language in section 226.4(c)(2) of Regulation Z, which excludes such fees from the APR disclosed under TILA. The intent is to exclude charges from the MAPR that the lender does not anticipate under the terms of the agreement. The language in the final rule is being adopted as proposed, so that creditors determinations under Part 232 will be consistent with their existing practice under TILA.

The final rule also has been revised to clarify that the MAPR does not include certain taxes or fees prescribed by law, such as fees paid to public officials in connection with perfecting a security interest. See § 232.3(h)(2)(i) and (ii). The revision is being made for consistency with the Federal Reserve Board's Regulation Z, which does not require such charges to be included in the APR disclosed under TILA.

Industry respondents also requested that the final rule clarify that the definition of ''consumer credit'' be limited to closed-end transactions so that the rules are not unintentionally interpreted to include credit cards. Many respondents stated it was not clear whether the rule included open-end credit and that it is important that the final rule explicitly state it is limited to the three listed closed-end credit products. In order to clarify that the regulation covers only closed-end credit, the definition in 232.3(b) has been modified to include the words ''closed-end'' as part of the definition of covered consumer credit.

232.4, Terms of consumer credit extended to covered borrowers: This section implements the statutory prohibition limiting the amount that creditors may charge for extensions of consumer credit to covered borrowers. The proposed rule mirrors the statutory language. This section also applies to ''assignees'' consistent with the statutory definition of ''creditor.''

232.5, Identification of covered borrower: The Department has received several comments expressing concern over the potential difficulty in identifying a covered borrower, particularly in light of the penalties for failing to provide the statutory protections to a covered borrower. While the Department recognizes this concern, the Department would emphasize that identifying the covered borrower is only relevant in the context of transactions defined by the regulation as consumer credit (for payday loans, vehicle title loans and refund anticipation loans).

Some respondents expressed concern that imposing a duty on creditors to identify dependents of active duty Service members in order to comply with Part 232 would conflict with the Equal Credit Opportunity Act, which is implemented by the Federal Reserve Board's Regulation B. These respondents noted that under Regulation B, a creditor may not inquire about a credit applicant's marital status. The Department notes, however, that the final rule does not require creditors to inquire about marital status. The ''covered borrower identification statement'' contained in § 232.5(a) of the final rule requests credit applicants to identify if they are a dependent based on any of the listed criteria (spouse, child or individual for whom the member provides financial support), but

does not require an applicant to specify which one of these applies in their specific case. Accordingly, the ''covered borrower identification statement'' does not inquire about an applicant's marital status. The Department also notes that § 202.5(a)(2) of the Federal Reserve's Regulation B states that creditors may obtain information required by federal statutes or regulations. The Department has consulted with staff of the Federal Reserve Board, and they agreed with the Department's analysis.

The Department's intent is to balance protections for covered borrowers (according to the statute) while also addressing creditors' need to have some degree of certainty in determining that the loans they make are in compliance with the statute as implemented by Part 232. The Department understands creditors may otherwise decline offering beneficial credit products to covered borrowers as a result of concerns over potential violations. To achieve an appropriate balance, the Department has proposed a safe harbor, under which the creditor may require the applicant to sign a statement declaring whether or not he or she is a covered borrower (using the definition from the statute). If required by the creditor, this declaration provides a ''safe harbor'' for the creditor to prevent inadvertently violating the statute by failing to recognize a covered borrower. For creditors who provide consumer credit, as defined by the regulation, by means of the Internet, the applicant can provide an electronic signature that fulfills the requirements of the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. § 7001 et seq.

There is one caveat to this ''safe harbor'' provision. If the loan applicant signs a declaration that denies being a covered borrower, but the creditor obtains documentation as part of the credit transaction reflecting that the applicant is a covered borrower (such as, a current military leave and earning statement as proof of employment), the applicant's declaration would not create a safe harbor for the creditor. In such cases, creditors should seek to resolve the inconsistency, but if they are unable to do so, they may avoid any risk of noncompliance by treating the applicant as a covered borrower based on the documentation or by declining to extend credit due to the inability to verify information provided in the borrower's signed declaration.

This caveat prevents creditors from using the declaration to allow covered borrowers to waive their right to the protections provided by the regulation. This may occur when the creditor recognizes the applicant is a covered borrower as a result of the documents presented as part of the credit transaction. The intent of this caveat is not to hold the creditor accountable for false statements made by an applicant when there is no indication through the credit transaction that the applicant is a covered borrower.

In contrast, when an applicant claims to be a covered borrower without presenting proof of status, further validation by the creditor is not required. However, creditors have the option of verifying the applicant's status as a covered borrower using several sources of information, but they are not required to do so. Thus, creditors may request applicants to provide proof of their current employment and income, for example by requesting from service members a copy of the most recent month's military leave and earning statement. Creditors may also request Service members or dependents to provide a copy of their military identification card.

These sources, however, might not always be determinative. For example, in some cases a leave and earnings statement might not reflect a recent change in the applicant's active duty status. Military identification cards, which are the same as identification cards carried by members of the active component, are issued to members of the National Guard and the Reserve regardless of their duty status. Hence, the final rule states ''*[u]pon such request, activated members of the National Guard or Reserves shall also provide a copy of the military orders calling the covered member to military service and any orders further extending military service.*'' This would also be the case for their dependents. The final rule does not provide a safe harbor to creditors in the situation described in this paragraph.

It is the Department's understanding that providing proof of employment is a prerequisite to receiving a payday loan or a vehicle title loan. The military leave and earning statement is the document that provides validation of employment.

The Department will provide access to a database to creditors to validate the status of an applicant. This arrangement is currently available to creditors to validate the active duty status of Service members as part of implementation of benefits authorized by the Servicemembers Civil Relief Act (*https://www.dmdc.osd.mil/scra/owa/home*). The proposed database (available at *http://www.dmdc.osd.mil/mla/owa/home*), will include the status of covered borrowers and can be used to resolve questions creditors may have about the status of an applicant who denies being a covered member and yet presents information during the credit transaction that is contrary to this declaration. In these situations, the database would provide the most accurate verification of the status of the applicant, to include activated members of the National Guard and Reserve and their dependents.

232.6, Mandatory disclosures: Section 232.6 describes the disclosures that must be provided to covered borrowers before they become obligated on a consumer credit transaction. This includes the new disclosures established under 10 U.S.C. 987 and also includes disclosures that creditors are already required to provide pursuant to the Federal Reserve Board's Regulation Z, which implements the TILA. Regulation Z contains certain requirements pertaining to the format of the TILA disclosures for closed-end credit transactions, including a requirement that they ''shall be grouped together, shall be segregated from everything else, and shall not contain any information not directly related'' to the disclosures required under Regulation Z. The Department intends that the disclosures required under this proposal be provided consistent with the format requirements of Regulation Z. Accordingly, the covered borrower identification statement described in § 232.5 and the disclosures provided pursuant to § 232.6(a)(1), (3), and (4) should not be interspersed with the TILA disclosures.

The general rule is that disclosures required by § 232.6(a) (1), (3), and (4) must be provided orally as well as in writing. However, in credit transactions entered into by mail or on the Internet, a creditor complies with this requirement if the creditor provides covered borrowers with a toll-free telephone number on or with the written disclosures and the creditor provides oral disclosures when the covered borrower contacts the creditor for this purpose. Consumer groups that commented stated that providing borrowers with a toll-free telephone number would not be sufficient because it places the burden on the borrower instead of the lender. Many industry respondents expressed concern about the costs of providing the disclosures, to include developing software, training employees about the new rules, and updating all their forms. The Department believes providing consumers with a toll-free telephone number to access oral disclosures fulfills the intent of the statute and balances overall considerations for protection with access to credit.

The Department has received several comments about potential disparities in disclosures required by this part as opposed to TILA. Many respondents felt that the current APR disclosures are barely understood by consumers and that adding a new MAPR disclosure to the mix will only serve to create more confusion. As with other aspects of the statute, the Department's intention has been to develop a regulation that is consistent with the statutory intent. The Department recognizes the potential confusion inherent in mandating the disclosure of two differing annual percentage rates (the MAPR required by this regulation and the APR required by TILA). As previously stated, the Department is responsible for training Service members and making similar education available for spouses. The differences between APR and MAPR will be added to their training, along with explaining their rights as a covered borrower. Some respondents sought clarification on whether MAPR disclosures would be required in advertising. These same respondents suggest that including MAPRs and APRs in marketing initiatives would be confusing to consumers. Under section 232.6 of the final rule, creditors must provide the required disclosures in writing before consummation of the transaction. Disclosure of the MAPR in advertisements is not required.

232.7, Preemption: The final rule implements the statute. Although, revisions have been made, this section has been drafted to clarify the statutory language, no substantive change is intended.

Some respondents expressed concern about the adequacy of enforcement for lenders that are not subject to enforcement by the federal depository institution supervisory agencies. The Department does not view the regulation as having substantial direct effects on States, or distribution of power and authority. States determine whether they will enforce the regulation or not for creditors under their jurisdiction. Associations of state supervisors recommended the Department seek written agreements between the Department and state regulatory agencies about enforcement, supervision, and information sharing to help state authorities enforce those areas that will normally fall under their jurisdiction. The Department intends to rely on federal and state regulators to oversee or enforce compliance with the final rule, to the extent possible under their statutory authority, for their respective creditors.

232.8, Limitations: Section 232.8(a) implements the statutory provision in 10 U.S.C. 987(e)(1), which prohibits a creditor from extending consumer credit to a covered borrower in order to roll over, renew, or refinance consumer credit that was previously extended by the same creditor to the same covered borrower.

The proposed regulation includes a limited exception to this prohibition, however, to permit workout loans and other refinancings that result in more favorable terms to the covered borrower, such as a lower MAPR. Most respondents agree that workout loans and other refinancings that are on ''more favorable terms'' for the borrower should be allowed. However, many respondents thought the standard for applying the exception was too subjective and would create uncertainty about what terms are considered ''more beneficial.'' Respondents suggested that financial institutions might err on the side of caution and forego entering transactions that could benefit the borrower in order to avoid any potential liability. Some respondents proposed specific ways to give creditors more certainty, such as by permitting creditors to show how the refinancing benefits the borrower or by allowing any refinancing initiated by the covered borrower.

The final rule does not identify additional examples of ''more favorable terms,'' because the Department has determined the definition currently included in the regulation is sufficient to allow creditors to provide workout loans on the basis of factors other than a lower MAPR that result in more favorable terms. By not limiting the phrase ''more favorable terms'' to a limited set of circumstances, covered borrowers will be protected without constraining creditors' ability to refinance loans on more favorable terms.

In the proposal, the Department solicited comment on whether it should adopt a rule clarifying that the refinancing or renewal of a covered loan requires new disclosures under § 232.6 only when the transaction would be considered a new transaction that requires TILA disclosures. Respondents' opinions differed, but most respondents stated that consistency between the Department's rules and Regulation Z would be less confusing and easier to implement. To maintain consistency between Part 232 and Regulation Z, the Department is adopting such a rule. See § 232.6(c). Whether or not new disclosures are required in a particular transaction, when a creditor refinances or renews an extension of consumer credit to a covered borrower, the limitations on rates and terms apply in the same manner as they would for the original transaction.

In some cases, a consumer might become a covered borrower after obtaining consumer credit. When consumers request to refinance or renew a short-term loan, creditors are likely to rely on their original determination that the consumer is not a covered borrower. Most respondents agreed that creditors should be able to rely on the original determination that the consumer is not a covered borrower for renewals and refinancings although a few argued for limiting the number of refinancings allowed before new disclosures and borrower identification were required. The Department believes that it would be unnecessarily burdensome to impose a duty on creditors to make a new determination in each transaction given that a change in the borrower's status will infrequently occur with short-term transactions. Accordingly, the final rule does not apply when the same creditor extends consumer credit to a covered borrower to refinance or renew an extension of credit that was not covered by Part 232 because the consumer was not a covered borrower at the time of the original transaction. See § 232.5(d).

Subparagraph (a)(3), in accordance with 10 U.S.C. 987(e)(3), makes it unlawful for any creditor to extend consumer credit to a covered borrower if the ''creditor requires the covered borrower to submit to arbitration *or imposes other onerous legal notice provisions*.'' Many respondents felt that a ban on ''onerous'' legal notice provisions was vague. Some offered examples of what should be considered onerous legal notice provisions, such as threats to use or using criminal process to collect a debt, making a misleading or deceptive statement, and requiring court or hearing costs to be borne by the borrower. Similarly, subparagraph (a)(4), in accordance with 10 U.S.C. 987(e)(4), makes it unlawful for any creditor to extend consumer credit to a covered borrower if the ''creditor demands *unreasonable notice* from the covered borrower as a condition for legal action.'' Industry respondents also requested the rule provide a list of what would be considered an ''unreasonable notice.'' In general, the comments with this provision address a fear it is not clear enough. The Department has determined that the provisions provide adequate explanation of ''unreasonable notice'' and thus has not included specific examples in the final rule of what constitutes ''onerous legal notice'' or ''unreasonable notice.'' It has concluded, that in so far as necessary, the scope of the provision is more

appropriately determined on a case-by-case basis.

Under § 232.8(a)(5) creditors are generally prohibited from extending consumer credit to a covered borrower if the creditor uses a check or other method of access to the covered borrower's deposit account. Section 232.8(a)(5) also lists certain exceptions to the general prohibition. Accordingly, for credit transactions with an MAPR of 36% or less, the creditor may require the borrower to use an electronic fund transfer to repay a consumer credit transaction, require direct deposit of the consumer's salary as a condition of eligibility for consumer credit, or take a security interest in funds deposited after the extension of credit in an account established in connection with the consumer credit transactions. Creditors must also comply with any other applicable statutes governing the use of electronic fund transfers, savings and direct deposit of consumer's salary. Respondents were generally supportive of allowing borrowers to use electronic fund transfers to pay debt if the MAPR is below 36% as conducive to creating flexible alternatives to lower cost consumer credit and helping stop the cycle of debt exacerbated by payday lending. The Department believes the flexibility that 10 U.S.C. 987(h)(2)(E) provides will encourage beneficial alternative loans designed to assist covered borrowers with financial recovery.

As proposed, § 232.8(a)(5) would have prohibited covered borrowers from using a vehicle title as security for any loan, even if the loan complied with the restrictions, limits and disclosure requirements of Part 232. Industry respondents pointed out this was inconsistent with other provisions treating vehicle-secured loans as covered transactions under these rules. The reference to vehicle secured loans in the proposed § 232.8(a)(5) was inadvertent, and has been corrected in the final rule.

Section 8(a)(7) prohibits creditors from charging a prepayment penalty to covered borrowers. The final regulation does not define what constitutes a prepayment penalty, and the Department expects creditors to rely on existing State and Federal laws for guidance.

232.9, Penalties and remedies: This provision incorporates the penalties and enforcement provisions contained in the statute. Section 9 provides, among other things, that any credit agreement subject to the regulation that fails to comply with this regulation is void from inception. It further provides that a creditor or assignee who knowingly violates the regulation shall be subject to certain criminal penalties. No comments were received, and the final rule incorporates the statutory provisions without change.

The statute, however, does not provide explicitly for enforcement of these rules beyond the provisions described above. The Department understands that the federal bank, thrift and credit union regulatory agencies have authority—derived from federal law unique to federally-regulated depository institutions—to enforce these rules with respect to the institutions that they supervise. However, the Department notes that this authority extends to a narrow category of depository institutions that it proposes to cover as ''creditors,'' but it does not extend to other creditors, such as nonbank lenders, that would also be covered creditors and that may be most likely to provide the types of consumer credit restricted by these rules. The Department is concerned that reliance solely on private litigation or criminal prosecution with respect to these other creditors may be insufficient to ensure uniform compliance with these rules with respect to all creditors. The Department understands that the consumer credit covered in the regulation is primarily overseen by state regulatory agencies. Consequently, the Department has made contact with the state regulatory agencies to determine which states plan to enforce the regulation and to determine how best to work with all 50 states on enforcement.

232.10, Servicemembers Civil Relief Act protections unaffected: Section 232.10 incorporates the statutory language, no comments were received on this provision and the final rule is unchanged from the proposal.

232.11, Effective date and transition: Virtually all respondents who would be subject to the rule requested a delayed effective date so that they would have more time to comply with the rules than the proposed 30-day period. Many respondents suggested six months to a year after publication of the final rule would be more reasonable for making the necessary systems changes. Two industry trade associations commented that it will be easier for creditors to comply by the effective date if the final rule remains as narrow in scope as the proposed rule. A consumer group and state regulators that commented believe that 30 days was sufficient.

The Department recognizes the limited time provided to creditors to react to implement the rules. However, the statute does not provide the Department any flexibility in determining the effective date of the statute, which is October 1, 2007. The Department believes this situation is ameliorated somewhat by the fact that the scope of the proposed rule is narrow and the policy decisions embedded in the final rule mirror to a great extent the provisions contained in the proposed rule. This should have afforded applicable creditors ample time to begin preparing for the requirements under the rule.

B. Statutory Certification

Executive Order 12866, ''Regulatory Planning and Review''

It has been determined that 32 CFR part 232 is not an economically significant regulatory action. The rule does not:

(1) Have an annual effect to the economy of $100 million or more or adversely and materially affect the economy; a section of the economy; productivity; competition; jobs; the environment; public health or safety; or State, local, or tribal governments or communities;

(2) Create a serious inconsistency or otherwise interfere with an action taken or planned by another Agency;

(3) Materially alter the budgetary impact of entitlements, grants, user fees, or loan programs, or the rights and obligations of recipients thereof; or

(4) Raise novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in this Executive Order.

Nevertheless, the proposed regulation was submitted to the Office of Management and Budget for review under other provisions of Executive Order 12866 as a significant regulatory action.

Unfunded Mandates Reform Act (Sec. 202, Pub. Law. 104–4)

It has been certified that this rule does not contain a Federal mandate that may result in the expenditure by State, local and tribal governments, in aggregate, or by the private sector, of $100 million or more in any one year.

Public Law 96–354, ''Regulatory Flexibility Act'' (5 U.S.C. 601)

It has been certified that this rule is not subject to the Regulatory Flexibility Act (5 U.S.C. 601) because it would not, if promulgated, have a significant economic impact on a substantial number of small entities. The North American Industrial Classification (NAIC) for the impacted businesses is 522390—''other financial activities related to credit intermediation.'' According to the 2002 Economic Census, there are approximately 5,205

small businesses related to this classification, with 3,000 of these small businesses having fewer than 5 employees. These 5,205 businesses represent a portion of the 51,725 potential respondents cited in the Paperwork Reduction Act evaluation.

The limitations and disclosures posed by this part impact only a small percentage of the market served by the industries covered by this part. For example according to the payday lending trade association, Service members and their dependents represent approximately one-to-two percent of the payday lending market. Thus there is not a significant economic impact on a substantial number of small entities.

Public Law 96–511, ''Paperwork Reduction Act'' (44 U.S.C. Chapter 35)

Section 232.6 of this rule contains information collection requirements. As required by the Paperwork Reduction Act (44 U.S.C. Chapter 35), DoD has submitted an information clearance package to the Office of Management and Budget for review. In response to DoD's invitation in the Proposed Rule to comment on any potential paperwork burden associated with this rule, the following comments were received.

232.6 Mandatory disclosures: Section 232.6 describes the disclosures that must be provided to covered borrowers before they become obligated on a consumer credit transaction. This includes the new disclosures established under 10 U.S.C. 987 and also includes disclosures that creditors are already required to provide pursuant to the Federal Reserve Board's Regulation Z, which implements the TILA. Regulation Z contains certain requirements pertaining to the format of the TILA disclosures for closed-end credit transactions, including a requirement that they ''shall be grouped together, shall be segregated from everything else, and shall not contain any information not directly related'' to the disclosures required under Regulation Z. The Department intends that the disclosures required under this proposal be provided consistent with the format requirements of Regulation Z. Accordingly, the covered borrower identification statement described in § 232.5 and the disclosures provided pursuant to § 232.6(a)(1), (3), and (4) should not be interspersed with the TILA disclosures.

The general rule is that disclosures required by § 232.6(a) (1), (3), and (4) must be provided orally as well as in writing. However, in credit transactions entered into by mail or on the internet, a creditor complies with this requirement if the creditor provides covered borrowers with a toll-free telephone number on or with the written disclosures and the creditor provides oral disclosures when the covered borrower contacts the creditor for this purpose. Consumer groups that commented stated that providing borrowers with a toll-free telephone number would not be sufficient because it places the burden on the borrower instead of the lender. Many industry respondents expressed concern about the costs of providing the disclosures, to include developing software, training employees about the new rules, and updating all their forms. The Department believes providing consumers with a toll-free telephone number to access oral disclosures fulfills the intent of the statute and balances overall considerations for protection with access to credit.

The Department has received several comments about potential disparities in disclosures required by this regulation as opposed to TILA. Many respondents felt that the current APR disclosures are barely understood by consumers and that adding a new MAPR disclosure to the mix will only serve to create more confusion. As with other aspects of the statute, the Department's intention has been to develop a regulation that is consistent with the statutory intent. The Department recognizes the potential confusion inherent in mandating the disclosure of two differing annual percentage rates (the MAPR required by this regulation and the APR required by TILA). As previously stated, the Department is responsible for training Service members and making similar education available for spouses. The differences between APR and MAPR will be added to their training, along with explaining their rights as a covered borrower. Some respondents sought clarification on whether MAPR disclosures would be required in advertising. These same respondents suggest that including MAPRs and APRs in marketing initiatives would be confusing to consumers. Under section 232.6 of the final rule, creditors must provide the required disclosures in writing before consummation of the transaction. Disclosure of the MAPR in advertisements is not required.

Executive Order 13132 Federalism

Executive Order 13132 requires that Executive departments and agencies identify regulatory actions that have significant federalism implications. A regulation has federalism implications if it has substantial direct effects on the States, on the relationship or distribution of power between the Federal Government and the States, or on the distribution of power and responsibilities among various levels of government.

The provisions of this part, as required by 10 U.S.C. 987, override State statutes inconsistent with this part to the extent that state statutes provide lesser protections for covered borrowers than those provided to residents of that State. In this respect, this proposed part, if adopted, would not affect in any manner the powers and authorities that any State may have or affect the distribution of power and responsibilities between Federal and State levels of government. Therefore, the Department has determined that the proposed part has no federalism implications that warrant the preparation of a Federalism Assessment in accordance with Executive Order 13132.

List of Subjects in 32 CFR Part 232

Loan programs, Reporting and recordkeeping requirements, Service members.

■ For the reasons set forth in the preamble, Title 32, Code of Federal Regulations is amended by adding part 232 to read as follows:

PART 232—LIMITATIONS ON TERMS OF CONSUMER CREDIT EXTENDED TO SERVICE MEMBERS AND DEPENDENTS

Sec

Authority: 10 U.S.C. 987.

§ 232.1 Authority, purpose, and coverage.

(a) *Authority.* This part is issued by the Department of Defense to implement 10 U.S.C. 987.

(b) *Purpose.* The purpose of this part is to impose limitations on the cost and terms of certain defined extensions of consumer credit to Service members and their dependents, and to provide additional consumer disclosures for such transactions.

(c) *Coverage.* This part defines the types of consumer credit transactions, creditors, and borrowers covered by the regulation, consistent with the

provisions of 10 U.S.C. 987. In addition, the regulation:

(1) Provides the maximum allowable amount of all charges, and the types of charges, that may be associated with a covered extension of consumer credit;

(2) Requires creditors to disclose to covered borrowers the cost of the transaction as a total dollar amount and as an annualized percentage rate referred to as the Military Annual Percentage Rate or MAPR, which must be disclosed before the borrower becomes obligated on the transaction. The disclosures required by this regulation differ from and are in addition to the disclosures that must be provided to consumers under the Federal Truth in Lending Act;

(3) Provides for the method creditors shall use in calculating the MAPR, and;

(4) Contains such other criteria and limitations as the Secretary of Defense has determined appropriate, consistent with the provisions of 10 U.S.C. 987.

§ 232.2 Applicability.

This part applies to consumer credit extended by creditors to a covered borrower, as those terms are defined in this part.

§ 232.3 Definitions.

Terms used in this part are defined as follows:

(a) *Closed-end credit* means consumer credit other than ''open-end credit'' as that term is defined in Regulation Z (Truth in Lending), 12 CFR part 226.

(b) *Consumer credit* means closed-end credit offered or extended to a covered borrower primarily for personal, family or household purposes, as described in paragraph (b)(1) of this section.

(1) Except as provided in paragraph (b)(2) of this section, consumer credit means the following transactions:

(i) *Payday loans.* Closed-end credit with a term of 91 days or fewer in which the amount financed does not exceed $2,000 and the covered borrower:

(A) Receives funds from and incurs interest and/or is charged a fee by a creditor, and contemporaneously with the receipt of funds, provides a check or other payment instrument to the creditor who agrees with the covered borrower not to deposit or present the check or payment instrument for more than one day, or;

(B) Receives funds from and incurs interest and/or is charged a fee by a creditor, and contemporaneously with the receipt of funds, authorizes the creditor to initiate a debit or debits to the covered borrower's deposit account (by electronic fund transfer or remotely created check) after one or more days. This provision does not apply to any right of a depository institution under statute or common law to offset indebtedness against funds on deposit in the event of the covered borrower's delinquency or default.

(ii) *Vehicle title loans.* Closed-end credit with a term of 181 days or fewer that is secured by the title to a motor vehicle, that has been registered for use on public roads and owned by a covered borrower, other than a purchase money transaction described in paragraph (b)(2)(ii) of this section.

(iii) *Tax refund anticipation loans.* Closed-end credit in which the covered borrower expressly grants the creditor the right to receive all or part of the borrower's income tax refund or expressly agrees to repay the loan with the proceeds of the borrower's refund.

(2) For purposes of this part, consumer credit does not mean:

(i) Residential mortgages, which are any credit transactions secured by an interest in the covered borrower's dwelling, including transactions to finance the purchase or initial construction of a dwelling, refinance transactions, home equity loans or lines of credit, and reverse mortgages;

(ii) Any credit transaction to finance the purchase or lease of a motor vehicle when the credit is secured by the vehicle being purchased or leased;

(iii) Any credit transaction to finance the purchase of personal property when the credit is secured by the property being purchased;

(iv) Credit secured by a qualified retirement account as defined in the Internal Revenue Code; and

(v) Any other credit transaction that is not consumer credit extended by a creditor, is an exempt transaction, or is not otherwise subject to disclosure requirements for purposes of Regulation Z (Truth in Lending), 12 CFR part 226.

(c) *Covered borrower* means a person with the following status at the time he or she becomes obligated on a consumer credit transaction covered by this part:

(1) A regular or reserve member of the Army, Navy, Marine Corps, Air Force, or Coast Guard, serving on active duty under a call or order that does not specify a period of 30 days or fewer, or such a member serving on Active Guard and Reserve duty as that term is defined in 10 U.S.C. 101(d)(6), or

(2) The member's spouse, the member's child defined in 38 U.S.C. 101(4), or an individual for whom the member provided more than one-half of the individual's support for 180 days immediately preceding an extension of consumer credit covered by this part.

(d) *Credit* means the right granted by a creditor to a debtor to defer payment of debt or to incur debt and defer its payment.

(e) *Creditor* means a person who is engaged in the business of extending consumer credit with respect to a consumer credit transaction covered by this part. For the purposes of this section, ''person'' includes a natural person, organization, corporation, partnership, proprietorship, association, cooperation, estate, trust, and any other business entity and who otherwise meets the definition of ''creditor'' for purposes of Regulation Z.

(f) *Dwelling* means a residential structure that contains one to four units, whether or not the structure is attached to real property. The term includes an individual condominium unit, cooperative unit, mobile home, and manufactured home.

(g) *Electronic fund transfer* (EFT) has the same meaning for purposes of this part as in Regulation E (Electronic Fund Transfers) issued by the Board of Governors of the Federal Reserve System, 12 CFR part 205.

(h) *Military annual percentage rate* (MAPR). The MAPR is the cost of the consumer credit transaction expressed as an annual rate. The MAPR shall be calculated based on the costs in this definition but in all other respects it shall be calculated and disclosed following the rules used for calculating the Annual Percentage Rate (APR) for closed-end credit transactions under Regulation Z (Truth in Lending), 12 CFR part 226.

(1) The MAPR includes the following cost elements associated with the extension of consumer credit to a covered borrower if they are financed, deducted from the proceeds of the consumer credit, or otherwise required to be paid as a condition of the credit:

(i) Interest, fees, credit service charges, credit renewal charges;

(ii) Credit insurance premiums including charges for single premium credit insurance, fees for debt cancellation or debt suspension agreements; and

(iii) Fees for credit-related ancillary products sold in connection with and either at or before consummation of the credit transaction.

(2) The MAPR does not include:

(i) Fees or charges imposed for actual unanticipated late payments, default, delinquency, or similar occurrence;

(ii) Taxes or fees prescribed by law that actually are or will be paid to public officials for determining the existence of, or for perfecting, releasing, or satisfying a security interest;

(iii) Any tax levied on security instruments or documents evidencing indebtedness if the payment of such

taxes is a requirement for recording the instrument securing the evidence of indebtedness; and

(iv) Tax return preparation fees associated with a tax refund anticipation loan, whether or not the fees are deducted from the loan proceeds.

(i) *Regulation Z* means any of the rules, regulations, or interpretations thereof, issued by the Board of Governors of the Federal Reserve System to implement the Truth in Lending Act, as amended, from time to time, including any interpretation or approval issued by an official or employee duly authorized by the Board of Governors of the Federal Reserve System to issue such interpretations or approvals. Words that are not defined in this regulation have the meanings given to them in Regulation Z (12 CFR part 226) issued by the Board of Governors of the Federal Reserve System (the ''Board''), as amended from time to time, including any interpretation thereof by the Board or an official or employee of the Federal Reserve System duly authorized by the Board to issue such interpretations. Words that are not defined in this regulation or Regulation Z, or any interpretation thereof, have the meanings given to them by State or Federal law, or contract.

§ 232.4 Terms of consumer credit extended to covered borrowers.

(a) Neither a creditor who extends consumer credit to a covered borrower nor an assignee of the creditor shall require the member or dependent to pay a military annual percentage rate (MAPR) with respect to such extension of credit, except as—

(1) Agreed to under the terms of the credit agreement or promissory note;

(2) Authorized by applicable State or Federal law; and

(3) Not specifically prohibited by this part.

(b) A creditor described in paragraph (a) of this section or an assignee may not impose an MAPR greater than 36 percent in connection with an extension of consumer credit to a covered borrower.

§ 232.5 Identification of covered borrower.

(a) This part shall not apply to a consumer credit transaction if the conditions described in paragraphs (a)(1) and (a)(2) of this section are met:

(1) Prior to becoming obligated on the transaction, each applicant is provided with a clear and conspicuous ''covered borrower identification statement'' substantially similar to the following statement and each applicant signs the statement indicating that he or she is or is not a covered borrower:

Federal law provides important protections to active duty members of the Armed Forces and their dependents. To ensure that these protections are provided to eligible applicants, we require you to sign one of the following statements as applicable:

I AM a regular or reserve member of the Army, Navy, Marine Corps, Air Force, or Coast Guard, serving on active duty under a call or order that does not specify a period of 30 days or fewer.

_____

I AM a dependent of a member of the Armed Forces on active duty as described above, because I am the member's spouse, the member's child under the age of eighteen years old, or I am an individual for whom the member provided more than one-half of my financial support for 180 days immediately preceding today's date.

_____

—OR—

I AM NOT a regular or reserve member of the Army, Navy, Marine Corps, Air Force, or Coast Guard, serving on active duty under a call or order that does not specify a period of 30 days or fewer (or a dependent of such a member).

_____

Warning: It is important to fill out this form accurately. Knowingly making a false statement on a credit application is a crime

(2) The creditor has not determined, pursuant to the optional verification procedures in paragraphs (b) or (c) of this section, that any such applicant is a covered borrower.

(b) The creditor may, but is not required to, verify the status of an applicant as a covered borrower by requesting the applicant to provide a current (previous month) military leave and earning statement, or a military identification card (DD Form 2 for members, DD Form 1173 for dependents), as described in DoD Instruction 1003.1, *Identification (ID) Cards for Members of the Uniformed Services, Their Dependents, and Other Eligible Individuals*, December 5, 1997. Upon such request, activated members of the National Guard or Reserves shall also provide a copy of the military orders calling the covered member to military service and any orders further extending military service.

(c) The creditor may, but is not required to, verify the status of an applicant as a covered borrower by accessing the information available at *http://www.dmdc.osd.mil/mla/owa/home*. Searches require the service member's full name, Social Security number, and date of birth.

(d) This part shall not apply to a consumer credit transaction in which the creditor rolls over, renews, repays, refinances, or consolidates consumer credit in accordance with § 232.8(a)(1) if § 232.5(a)(1) and § 232.5(a)(2) applied to the previous transaction.

§ 232.6 Mandatory loan disclosures.

(a) *Required information.* With respect to any extension of consumer credit (including any consumer credit originated or extended through the internet) to a covered borrower, a creditor shall provide to the member or dependent the following information clearly and conspicuously before consummation of the consumer credit transaction:

(1) The MAPR applicable to the extension of consumer credit, and the total dollar amount of all charges included in the MAPR.

(2) Any disclosures required by Regulation Z (Truth in Lending), 12 CFR part 226.

(3) A clear description of the payment obligation of the covered borrower, as applicable. A payment schedule provided pursuant to paragraph (a)(2) of this section satisfies this requirement.

(4) A statement that ''Federal law provides important protections to regular or reserve members of the Army, Navy, Marine Corps, Air Force, or Coast Guard, serving on active duty under a call or order that does not specify a period of 30 days or fewer, and their dependents. Members of the Armed Forces and their dependents may be able to obtain financial assistance from Army Emergency Relief, Navy and Marine Corps Relief Society, the Air Force Aid Society, or Coast Guard Mutual Aid. Members of the Armed Forces and their dependents may request free legal advice regarding an application for credit from a service legal assistance office or financial counseling from a consumer credit counselor.''

(b) *Method of disclosure.* (1) *Written disclosures.* The creditor shall provide the disclosures required by paragraph (a) in writing in a form the covered borrower can keep.

(2) *Oral disclosures.* The creditor also shall provide the disclosures required by paragraphs (a)(1), (a)(3) and (a)(4) of this section orally before consummation. In mail and internet transactions, the creditor satisfies this requirement if it provides a toll-free telephone number on or with the written disclosures that consumers may use to obtain oral disclosures and the creditor provides oral disclosures when the covered borrower contacts the creditor for this purpose.

(c) *When disclosures are required for refinancing or renewal of covered loan.* The refinancing or renewal of a covered loan requires new disclosures under § 232.6 only when the transaction

would be considered a new transaction that requires disclosures under the Truth in Lending Act, as implemented by the Federal Reserve Board's Regulation Z, 12 CFR part 226.

§ 232.7 Preemption.

(a) *Inconsistent laws.* 10 U.S.C. 987 as implemented by this part preempts any State or Federal law, rule or regulation, including any State usury law, to the extent such law, rule or regulation is inconsistent with this part, except that any such law, rule or regulation is not preempted by this part to the extent that it provides protection to a covered borrower greater than those protections provided by 10 U.S.C. 987 and this part.

(b) Different treatment under State law of covered borrowers is prohibited. States may not:

(1) Authorize creditors to charge covered borrowers rates of interest that are higher than the legal limit for residents of the State, or

(2) Permit the violation or waiver of any State consumer lending protection that is for the benefit of residents of the State on the basis of the covered borrower's nonresident or military status, regardless of the covered borrower's domicile or permanent home of record, provided that the protection would otherwise apply to the covered borrower.

§ 232.8 Limitations.

(a) 10 U.S.C. 987 makes it unlawful for any creditor to extend consumer credit to a covered borrower with respect to which:

(1) The creditor rolls over, renews, repays, refinances, or consolidates any consumer credit extended to the covered borrower by the same creditor with the proceeds of other consumer credit extended by that creditor to the same covered borrower, unless the new transaction results in more favorable terms to the covered borrower, such as a lower MAPR. This part shall not apply to a transaction permitted by this paragraph when the same creditor extends consumer credit to a covered borrower to refinance or renew an extension of credit that was not covered by this part because the consumer was not a covered borrower at the time of the original transaction.

(2) The covered borrower is required to waive the covered borrower's right to legal recourse under any otherwise applicable provision of State or Federal law, including any provision of the Servicemembers Civil Relief Act (50 U.S.C. App. 10 U.S.C. 527 *et seq.*).

(3) The creditor requires the covered borrower to submit to arbitration or imposes other onerous legal notice provisions in the case of a dispute.

(4) The creditor demands unreasonable notice from the covered borrower as a condition for legal action.

(5) The creditor uses a check or other method of access to a deposit, savings, or other financial account maintained by the covered borrower, except that, in connection with a consumer credit transaction with an MAPR consistent with § 232.4(b):

(i) The creditor may require an electronic fund transfer to repay a consumer credit transaction, unless otherwise prohibited by Regulation E (Electronic Fund Transfers) 12 CFR part 205;

(ii) The creditor may require direct deposit of the consumer's salary as a condition of eligibility for consumer credit, unless otherwise prohibited by law; or

(iii) The creditor may, if not otherwise prohibited by applicable law, take a security interest in funds deposited after the extension of credit in an account established in connection with the consumer credit transaction.

(6) The creditor requires as a condition for the extension of consumer credit that the covered borrower establish an allotment to repay the obligation.

(7) The covered borrower is prohibited from prepaying the consumer credit or is charged a penalty fee for prepaying all or part of the consumer credit.

(b) For purposes of this section, an assignee may not engage in any transaction or take any action that would be prohibited for the creditor.

§ 232.9 Penalties and remedies.

(a) *Misdemeanor.* A creditor or assignee who knowingly violates 10 U.S.C. 987 as implemented by this part shall be fined as provided in title 18, United States Code, or imprisoned for not more than one year, or both.

(b) *Preservation of other remedies.* The remedies and rights provided under 10 U.S.C. 987 as implemented by this part are in addition to and do not preclude any remedy otherwise available under State or Federal law or regulation to the person claiming relief under the statute, including any award for consequential damages and punitive damages.

(c) *Contract void.* Any credit agreement, promissory note, or other contract with a covered borrower that fails to comply with 10 U.S.C. 987 as implemented by this regulation or which contains one or more provisions prohibited under 10 U.S.C. 987 as implemented by this regulation is void from the inception of the contract.

(d) *Arbitration.* Notwithstanding 9 U.S.C. 2, or any other Federal or State law, rule, or regulation, no agreement to arbitrate any dispute involving the extension of consumer credit to a covered borrower pursuant to this part shall be enforceable against any covered borrower, or any person who was a covered borrower when the agreement was made.

§ 232.10 Servicemembers Civil Relief Act protections unaffected.

Nothing in this part may be construed to limit or otherwise affect the applicability of Section 207 and any other provisions of the Servicemembers Civil Relief Act (50 U.S.C. App. 527).

§ 232.11 Effective date and transition.

Applicable consumer credit—This part shall only apply to consumer credit that is extended to a covered borrower and consummated on or after October 1, 2007.

Dated: August 27, 2007.

L.M. Bynum,

Alternate OSD Federal Register Liaison Officer, DoD.

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