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Legislative Restriction of Creditor Powers and Remedies: A Case Study of the Negotiation and Drafting of the Wisconsin Consumer Act

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LEGISLATIVE RESTRICTION OF CREDITOR POWERS AND REMEDIES: A CASE STUDY OF THE NEGOTIATION AND DRAFTING OF THE WISCONSIN CONSUMER ACT

Jeffrey Davis

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LEGISLATIVE RESTRICTION OF CREDITOR POWERS AND REMEDIES: A CASE STUDY OF THE NEGOTIATION AND DRAFTING OF THE WISCONSIN CONSUMER ACT

Jeffrey Davis*

WITH the vast growth of consumer credit in the United States, followed by the growth of sympathy for the consumer, it became increasingly clear in the mid-1960's that the time for comprehensive consumer credit legislation was near. To encourage the passage of uniform legislation, the National Commissioners on Uniform State Laws established the Special Committee on Retail Installment Sales, Consumer Credit, Small Loans and Usury to draft the Uniform Consumer Credit Code (UCCC). Although some preliminary work had already been done, serious efforts began in 1965. The UCCC went through eight preliminary drafts, and comments were sought from all sectors of the consumer-credit community.¹ The ninth and final draft was approved in 1968 and, after minor modifications, was published in 1969.²

Although the UCCC initially met with consumer approval,³ the hoped-for general support was not to be. Criticism began to mount, and much of the initial support was withdrawn. The UCCC has been criticized for, among other things, having been funded primarily by lenders,⁴ allowing excessively high interest rates,⁵ and failing to provide effective private remedies for consumers.⁶ In general, the criticism

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1. UNIFORM CONSUMER CREDIT CODE, Prefatory Note, xxi-xxii.

2. The modifications were to conform with the provisions of the Consumer Credit Protection Act of 1968, Pub. L. No. 90-321, 82 Stat. 146, *as amended*, Fair Credit Reporting Act of 1970, Pub. L. No. 91-508, § 601, 84 Stat. 1128 (codified at 15 U.S.C. §§ 1601-81t (1970), 18 U.S.C. §§ 891-96 (1970)). See UNIFORM CONSUMER CREDIT CODE, Prefatory Note, xvii-xix.

3. Stengel, *Should States Adopt the Uniform Consumer Credit Code?*, 60 Ky. L.J. 8, 41 (1971).

4. *Id.* at 40; Murphy, *Lawyers for the Poor View the UCCC*, 44 N.Y.U. L. REV. 298, 299-300 (1969). Murphy considers these attacks to have been unfair.

5. *A Consumer Credit Code . . . for Lenders*, 34 CONSUMER REPORTS, March 1969, at 121, 121-22. The UCCC provides for maximum annual interest rates of 36 per cent on small loans and 24 per cent on revolving accounts. UNIFORM CONSUMER CREDIT CODE §§ 2.201, .207.

6. Spanogle, *Why Does the Proposed Uniform Consumer Credit Code Eschew Private Enforcement?*, 23 BUS. LAW. 1039 (1968); James & Fragomen, *Uniform Consumer Credit Code: Inadequate Remedies Under Articles V and VI*, 57 GEO. L.J. 923 (1969); Littlefield, *Preserving Consumer Defenses: Plugging the Loophole in the New UCCC*, 44 N.Y.U. L. REV. 272 (1969).

has centered around an alleged failure to restrict creditor powers and practices sufficiently.⁷

The most significant anti-UCCC action was taken by the National Consumer Law Center.⁸ Following a conference of some fifty-five consumer experts on June 20, 1969, at which the consensus was that the UCCC was inadequate and required substantial revision, the Center undertook to develop what was, in its view, an adequate code.⁹ With the aid of a grant from the Office of Economic Opportunity, it drafted the National Consumer Act (NCA), published in 1970.

Unlike the UCCC, the NCA admittedly demonstrated little concern for attracting creditor support.¹⁰ It was drafted in six months, primarily by a committee consisting solely of avowed consumer advocates,¹¹ with apparently little dispute as to what it would contain.¹² The published form of the NCA was the first draft to be generally distributed and the first draft upon which general comment was solicited. Predictably, the NCA extended well beyond the UCCC in restricting creditor powers and remedies and in creating consumer enforcement tools. It was acclaimed by some as preferable to the UCCC,¹³ but even its supporters admitted that it was often guilty of overkill.¹⁴ It was, of course, roundly criticized by others.¹⁵ Recently, the National Consumer Law Center has published the successor to the NCA—the Model Consumer Credit Act (MCCA).

7. See H. KRIPKE, *CONSUMER CREDIT: TEXT—CASES—MATERIALS* 58-62 (1970); Harper, *The Uniform Consumer Credit Code, A Critical Analysis*, 44 N.Y.U. L. REV. 53 (1969); Murphy, *supra* note 4, at 299; Turner, *The UCCC: A Credit Code for Business*, 60 Ky. L.J. 49 (1971).

8. The Center was formerly associated with Boston College Law School. Its offices are presently located at 1 Court St., Boston, Mass. 02108.

9. NATIONAL CONSUMER ACT, Prefatory Note, iii-iv.

10. In fact, one of the most significant factors contributing to the creation of the NCA was the feeling of its proponents that the UCCC draftsmen, concerned with political considerations, did little more than draft a codification of existing credit practices. NATIONAL CONSUMER ACT, Prefatory Note, iii. See also Willier, *The Uniform Consumer Credit Code: What Should Legal Services Attorneys Do?*, 3 CLEARINGHOUSE REV. 33 (1969).

11. NATIONAL CONSUMER ACT, Prefatory Note, iv. The special committee consisted of representatives of the Consumer Federation of America, Consumers Union, AFL-CIO, AFL-UAW, and various legal service organizations.

12. NATIONAL CONSUMER ACT, Prefatory Note, app. B, at vii.

13. See Turner, *supra* note 7; Comment, *Consumer Protection Under the UCCC and the NCA—A Comparison and Recommendations*, 12 ARIZ. L. REV. 572 (1970).

14. See Clark, *Default, Repossession, Foreclosure, and Deficiency: A Journey to the Underworld and a Proposed Salvation*, 51 ORE. L. REV. 302, 336 (1972); Comment, *supra* note 13, at 581.

15. See, e.g., Moo, *New Consumer Credit Legislation: Which Approach—The UCCC or NCA?*, 2 URBAN LAW. 439 (1970).

While the MCCA often departs from the NCA, its approach to consumer-credit problems is substantially the same.

The battle over consumer-credit reform is now raging in the state legislatures.¹⁶ Most states have considered or are presently considering the UCCC for possible enactment. To date, seven have adopted it in some form.¹⁷ A few legislatures will probably see some form of the MCCA in the near future. There is, however, a third consumer-credit package that deserves serious consideration—the Wisconsin Consumer Act (WCA).¹⁸

In contrast to the UCCC and the MCCA, the WCA is an actual statute, the product of six intense months of negotiation and drafting. The initial version of the WCA had been introduced in the Wisconsin Assembly in early 1971 as Assembly Bill 1057¹⁹ (Original A.B. 1057). Its provisions relating to consumer-credit transactions did not differ substantially from those of the NCA.²⁰ In its final form, the

16. The enactment of the Consumer Credit Protection Act of 1968, Pub. L. No. 90-321, 82 Stat. 146, *as amended*, Fair Credit Reporting Act of 1970, Pub. L. No. 91-508, § 601, 84 Stat. 1128 (codified at 15 U.S.C. §§ 1601-81t (1970), 18 U.S.C. §§ 891-96 (1970)), applied pressure to the states to revise their consumer credit laws. Section 123 of the Act, 15 U.S.C. § 1633 (1970), allows the Federal Reserve Board to "exempt from the requirements of this part [15 U.S.C. §§ 1631-65 (1970)] any class of credit transactions within any State if it determines that under the law of that State that class of transactions is subject to requirements substantially similar to those imposed under this part, and that there is adequate provision for enforcement." See UNIFORM CONSUMER CREDIT CODE, Prefatory Note, xxii-xxiii.

17. They are Colorado, Idaho, Indiana, Kansas, Oklahoma, Utah, and Wyoming. 1 CCH CONSUMER CREDIT GUIDE ¶ 4770 (1973).

18. Wisconsin Consumer Act, ch. 239, [1971] Wis. Laws 3688 (codified at Wis. STAT. §§ 421.101-427.105 (1971)). In this Article, these sections of the Wisconsin Statutes will be referred to as sections of the Wisconsin Consumer Act.

The WCA was based on the NCA. However, the substantive changes that resulted from negotiation and redrafting are so pervasive that its resemblance to the NCA is at best slight. I have no qualms about designating the WCA as a third package.

Strictly speaking, the WCA is not solely a consumer-credit package. Although most of its provisions apply to consumer-credit transactions, it applies as well to sales solicited and contracted away from the regular place of business of the merchant. Wisconsin Consumer Act §§ 423.201-205.

19. The bill was introduced by Representative Harout Sanasarian (D-Milwaukee), chairman of the Commerce and Consumer Affairs Committee. Sections 1 through 28 of the bill would have repealed various statutes and made other technical changes necessitated by the addition of the consumer-credit law. Section 29 contains the substantive provisions and would have created chapters 421 through 427 of the Wisconsin Statutes. In this Article citations to the original bill will be to the proposed sections contained in section 29 (*e.g.*, A.B. 1057, § 421.101).

20. Original A.B. 1057 differed significantly from the NCA in many provisions other than those dealing with consumer-credit transactions. The NCA's treatment of consumer-approval transactions was completely revamped. Compare NATIONAL CONSUMER ACT §§ 2.501-505 with A.B. 1057, §§ 423.201-212. The NCA provisions regarding a council of advisors on consumer affairs, administrative procedure, and judicial review (sections 6.301-414) and regarding credit-reporting agencies (sections 8.101-.303) were eliminated.

Regarding consumer-credit transactions, there were only two significant differences

WCA was over sixty per cent longer than Original A.B. 1057, and the majority of its provisions had been substantially redrafted.

The WCA is unique in that its provisions were arduously negotiated under political circumstances that put the consumer representatives in a strong bargaining position. In fact, the strength of the consumer position in Wisconsin may never be duplicated again. At the same time, the bargaining position of Wisconsin creditors was not weak, although it was weaker than that in which creditors usually stand. The vast financial resources of the creditor representatives, especially compared to those of the consumer representatives, their political influence, and the consequent need for their support were apparent throughout the drafting process.

Accordingly, the WCA represents a solution in which consumer-creditor interests are uniquely balanced. It goes further to protect consumer interests than any other such legislation in the country; yet it eventually won the support of the great majority of creditors within the state.²¹ Certainly, it is not without its flaws, both technical and substantive. But equally certainly, it is a significant event in the struggle to realign the relationship between creditor and consumer.

This Article discusses the background, negotiation, and drafting of selected WCA restrictions on creditor powers and remedies and compares those provisions to the analogous restrictions proposed by other reform measures. In addition to the UCCC, the MCCA and the WCA, two other major works must be considered in any discussion of consumer-credit legislation. First is Working Redraft No. 4 of the UCCC (UCCC Redraft).²² This proposed revision, published in December 1972, represents a marked change in the UCCC. Many provisions favorable to the consumer have been added, and many of the parallel provisions on sales and loans have been consolidated. Although it is not an official recommendation, it indicates the current thinking of the UCCC Special Committee. Second is the Report of the National Commission on Consumer Finance (Commission Re-

between the NCA and A.B. 1057. First, whereas the NCA regulates credit insurance (sections 4.101-.304), A.B. 1057 simply prohibited the charge of any fee or premium for such insurance (section 422.418). Second, the NCA provisions regulating liability for use of credit cards (sections 2.601-.605) were not included in A.B. 1057.

21. Among the credit groups supporting the Act in its final form were: Wisconsin Credit Union League, Wisconsin Bankers' Association, Wisconsin Retail Merchants' Association, Wisconsin Installment Bankers' Association, Wisconsin Consumer Finance Association, Wisconsin Farm Implement Dealers' Association, and Wisconsin State Chamber of Commerce. Crandall, *The Wisconsin Consumer Act: Wisconsin Consumer Credit Laws Before and After*, 1973 Wis. L. Rev. 334, 334-35 n.6 (1973).

22. UNIFORM CONSUMER CREDIT CODE (Working Redraft No. 4, 1972).

port).²³ The Commission, established by title IV of the Consumer Credit Protection Act,²⁴ submitted the report on December 31, 1972, after three years of study.

My objective in this Article is twofold. First, the discussion may enable the reader to understand the objectives of the WCA restrictions on creditors' rights and remedies and the interests that they are likely to affect. Second, by looking closely at the evolution of the WCA in the context of specific issues, it may be possible to determine whether the WCA can serve as a model for consumer-credit reform movements in other states.

I. THE SURVEY

Although the advice and recommendations of many groups were sought, the primary negotiating and nearly all of the drafting was done by representatives of banks,²⁵ retail merchants,²⁶ consumer finance companies,²⁷ and consumers.²⁸ To discover the motives behind the negotiated changes, I interviewed these key negotiators. It was necessary to focus on selected portions of the Act; because of their notoriety and likely impact on the consumer-credit industry, the Act's limitations on creditor practices and remedies were the focus of the inquiry. In each case, the negotiator was asked to describe the chronology of the change, the groups for and against the change, the alternatives considered, and the reason for the action taken. To ensure accuracy, the negotiators then reviewed and commented upon a draft of the Article. Their comments were incorporated into the final version.

II. EVENTS LEADING TO THE NEGOTIATION AND PASSAGE OF THE WCA

Until 1970, Wisconsin retail merchants assumed that a revolving credit sale was not subject to the Wisconsin twelve per cent per year usury limitation. Under the age-old time-price doctrine, if the price

23. NATIONAL COMMISSION ON CONSUMER FINANCE, CONSUMER CREDIT IN THE UNITED STATES (1972) [hereinafter COMMISSION REPORT].

24. Pub. L. No. 90-321, tit. IV, 82 Stat. 164, *as amended*, Act of July 20, 1970, Pub. L. No. 91-344, 84 Stat. 440.

25. The primary bank negotiator was Lawrence J. Bugge of Milwaukee.

26. Retail merchants were chiefly represented by John S. Holbrook, Jr., and Boris Auerbach.

27. Consumer finance companies were primarily represented by Edward J. Heiser, Jr. For Heiser's analysis of the WCA and a discussion of some of the problems that may arise, see Heiser, *The Wisconsin Consumer Act: A Critical Analysis*, — MARQ. L. REV. — (1973).

28. The unquestioned consumer leader and, for much of the time, the sole consumer negotiator was Thomas D. Crandall of Milwaukee Legal Services.

of goods was not to be paid at the time of the purchase, any increase in the amount due when paid was not considered a finance charge. Rather, it was simply considered to be a natural increase in the purchase price resulting from the delayed payment.²⁹ In October 1970, this house of cards collapsed for Wisconsin merchants who offered goods for sale on revolving credit. In *State v. J.C. Penney Co.*,³⁰ the Wisconsin supreme court, looking behind the form of revolving charge accounts to their substance, found that such accounts do indeed amount to a forbearance of money and not a time sale.³¹

The decision had a severe impact on all Wisconsin retailers who offered open-end credit plans; these were principally the large retailers.³² The impact was twofold. First, the retailers were forced to limit finance charges on open-end accounts to one per cent per month. This substantial reduction in income, not coupled with a reduction in overhead, was a severe blow, which put the profitability of open-end plans in serious doubt. The second and perhaps more significant result was that the retailers immediately became potentially subject to great liability for past violations of the usury limita-

29. See, e.g., *Hogg v. Ruffner*, 66 U.S. (1 Black) 115, 118-19 (1861).

30. 48 Wis. 2d 125, 179 N.W.2d 641 (1970), noted in 71 COLUM. L. REV. 905 (1971); 2 CUMB.-SAM. L. REV. 234 (1971); 54 MARQ. L. REV. 223 (1971); 69 MICH. L. REV. 1368 (1971); 55 MINN. L. REV. 1244 (1971).

31. Quoting at length from the trial court opinion analyzing the Penney revolving charge contract, the court listed the following factors as among those tending to show that the agreement is not a traditional time-price sale: (1) The customer may elect to pay cash and lower the cost even after service charges have begun; (2) the contract is not entered into in connection with a specific sale; (3) the extension of credit is based on the purchaser's ability to pay; (4) the sale of goods is absolute, with creation of a debt as consideration therefor; (5) there may be multiple sales with debt to the account and also credit for payments; (6) the "service charge" is not fixed and independent of the amount owed; (7) the customer is not quoted a time sale price as well as a cash price; (8) the "service charge" is not a penalty intended to induce prompt payment; and (9) the sales tax is computed on the cash price. 48 Wis. 2d at 144-50, 179 N.W.2d at 651-54.

The South Dakota supreme court came to the same conclusion in *Rollinger v. J.C. Penney Co.*, — S.D. —, 192 N.W.2d 699 (1971). See Note, *Interest Incognito—Usury Statute Applied to Revolving Charge Account Agreement*, 34 U. PITT. L. REV. 54 (1972) (discussing both *Penney* cases). A recent Iowa supreme court decision followed the Wisconsin court. See *State ex rel. Turner v. Younger Bros.*, 210 N.W.2d 550 (1973). However, no other state has followed the Wisconsin decision. See *Sliger v. R.H. Macy & Co.*, 59 N.J. 465, 283 A.2d 904 (1971); *Maine Merchants Assn. v. Campbell*, 287 A.2d 430 (Me. 1972); *Standard Oil Co. (Indiana) v. Williams*, — Ind. App. —, 288 N.E.2d 170 (1972); *Kass v. Garfinckel, Brooks Bros., Miller & Rhoads, Inc.*, 299 A.2d 542 (D.C. Ct. App. 1973). See also *Zachary v. R.H. Macy & Co.*, 31 N.Y.2d 443, 457, 293 N.E.2d 80, 88, 340 N.Y.S.2d 908, 918-19 (1972).

32. The decision had little impact on small retailers. Those who carried their own credit normally made only closed-end credit sales, which were apparently still outside the operation of the usury statute. Any open-end credit available from these merchants was normally offered through bank credit cards, which had always been subject to usury restrictions.

tions.³³ Litigation under the usury statutes, in addition to being a nuisance, would involve large legal costs and, more significantly, could produce a continuous stream of unfavorable publicity. One solution to these problems lay in the legislature. As of October 1970, the large retailers were primarily interested in obtaining passage of legislation that would eliminate the retroactive application of usury penalties to revolving sales accounts.

At the same time, Wisconsin banks hoped to obtain an exemption from the usury laws for their open-end credit plans. Apparently, because of the high cost of handling thousands of small drafts, growth of bank credit cards in Wisconsin would have been considerably inhibited if there had been no increase in the permissible finance charge.³⁴

In early 1971, through the efforts of the large retailers, S.B. 277, a bill prohibiting retroactive application of the usury penalties, was introduced into the Wisconsin legislature. Similarly, through the efforts of the Wisconsin Installment Bankers Association, A.B. 492, a bill increasing allowable finance charges on revolving accounts, was also introduced.

Meanwhile, consumer finance companies, long dissatisfied with the Wisconsin rate restrictions on licensed loans,³⁵ succeeded, in June 1971, in obtaining passage of a bill that relaxed these restrictions temporarily.³⁶ The increased rates were to remain in effect until July 1973, by which time the legislature would presumably have considered the matter more thoroughly.³⁷

The next significant event in the pre-WCA maneuvering occurred in October 1971. Nearly two years before, the Wisconsin legislature had established an advisory committee to examine the UCCC and recommend the changes, if any, that should be made prior to enactment. The committee initially set out to strengthen the UCCC consumer protections; however, a severe split of opinion developed over

33. WIS. STAT. § 138.06 (1971) provides various remedies and penalties for loans in violation of the usury limitations. These may amount to as much as the total principal, interest, and charges paid during the two years prior to suit. WIS. STAT. § 138.06(3) (1971).

34. Conversation with Bill Dixon, Vice-President of First Wisconsin National Bank, head of the Credit Card Division, February 28, 1973.

35. Since consumer finance companies borrow most of the money they lend, the increases in the prime rate during the 1960's had significantly reduced profit margins. Hence, they sought similar increases in the rates chargeable to consumers.

36. See *Capital Times* (Madison, Wis.), Nov. 8, 1971, at 36, col. 1.

37. *Id.* Originally, the finance companies succeeded in obtaining passage of a permanent rate increase bill in both houses. However, Governor Lucey vetoed the bill, and the finance companies were forced to settle for a temporary increase.

how much strengthening was needed. On October 4, 1971, two consumer representatives on the committee walked out in protest over the apparent acceptance of the UCCC. They reportedly charged that the UCCC was "nearly worthless" from the standpoint of consumer protection and that the other committee members were committed to "recommending legislation favorable only to creditors."³⁸ The nine remaining representatives continued putting the final touches on their recommendation.

Later in October, Governor Patrick J. Lucey, referring specifically to A.B. 492 and S.B. 277, officially informed the legislature that he was opposed to piecemeal consumer legislation and that he did not think legislation beneficial to lenders appropriate without added statutory protection for the consumer.³⁹ He further advised the legislature to take up A.B. 1057. On October 26, the assembly began to work on A.B. 1057, but, due to a flood of proposed amendments, consideration of the bill was postponed until the January session.

Thus, at the end of 1971, the retail merchants sought protection from retroactive application of the usury penalties, the banks sought rate increases for their revolving charge plans and for their small loans, and the consumer finance companies hoped to make the rate increases they had obtained in July permanent. However, the Governor's position made it clear that special interest legislation would be unavailable outside the framework of a comprehensive consumer-credit package. In addition, consumer advocates recognized that the passage of protective legislation would require substantial creditor support. But the complete breakdown between the consumer representatives and other members of the UCCC advisory committee showed that the UCCC could not serve as the catalyst. For these reasons, a consumer-creditor coalition, which had begun to materialize as early as the summer of 1971, slowly took shape in the hope that, through negotiation, A.B. 1057 could be molded into a form that could be supported by all.

The negotiations took place in two clearly discernible stages. Well before Governor Lucey's official communication to the legislature, the banks had known of his desire for comprehensive legislation, his support of A.B. 1057, and his confidence in its proponents. Hence, in August 1971, the bank representatives began conferring

38. Wis. St. J., Oct. 5, 1971, § 2, at 3, col. 1. One of the creditor negotiators told me that he thinks this was simply a grandstand play intended to generate support for A.B. 1057. He also thinks it worked.

39. Capital Times (Madison, Wis.), Nov. 8, 1971, at 36, col. 4.

with the proponents of A.B. 1057 to see if a compromise was possible. With the mutual discovery that they could work together, serious negotiations began in September; representatives of retail merchants joined the discussions a few weeks later. The issue of third-party creditor immunity became the testing ground for the fragile coalition, so the successful resolution of this problem set the tone for subsequent negotiations. The first round of negotiations ended in December.⁴⁰ The fruits of the negotiators' labor were assembled, and A.B. 1057, as modified, was distributed throughout the credit community.

The second stage of the negotiations took place in January 1972. Although suggestions and arguments were put forth by numerous credit groups—credit unions, farm implement dealers, and savings and loan associations—and the banks and retailers continued their involvement, the primary input at this stage came from consumer finance company representatives.

Notably absent from the negotiations, although their participation was solicited, were representatives of the large manufacturer-affiliated automobile finance companies and the Wisconsin automobile dealers. Their unwillingness to join the coalition is easily understood. Since the prevailing interest rates in the Wisconsin automobile credit market were substantially below the statutory limits, the automobile interests needed no rate relief. In addition, they were unaffected by the *Penney* case. They made their opposition to the WCA clear throughout the negotiations, apparently assuming they could prevent its passage. This assumption was, of course, incorrect. Although the automobile finance companies and the dealers worked hard to defeat the bill⁴¹ and did succeed in getting one amendment passed,⁴² the WCA was adopted substantially as submitted.

The effect of this group's failure to participate in the negotiations is quite a speculative matter. On many critical issues they were represented only to the extent that the banks, which also finance automobile sales, shared their interests. The banks, however, sought gains in other areas and were willing to compromise the interests shared with the automobile finance group for the sake of other concerns. Throughout the negotiations and the battle in the legislature,

40. As of December, the bank-retailer-consumer combination was beginning to bog down. Having made a number of substantial concessions and having obtained substantial concessions in return, individual negotiators began to lose their ability to persuade. Although all issues had not been resolved, it was time to get some new blood into the negotiations.

41. Crandall, *supra* note 21, at 334-35 n.6.

42. See text accompanying notes 250-51 *infra*.

passage of the bill was in doubt. The automobile finance companies and the automobile dealers could certainly have exacted substantial consumer concessions in exchange for their support. What those concessions might have been cannot be known.⁴³

On the whole, however, the Act represents an extraordinary individual and collective effort, put forth by people searching for common ground, while diligently representing often quite divergent interests. In its final form, the WCA had the support of most credit organizations and nearly all consumer groups.⁴⁴ After a difficult battle in the legislature⁴⁵ that resulted in only a few substantive changes, the Wisconsin Consumer Act was passed and signed into law on March 29, 1972. It went into effect on March 1, 1973.

III. NEGOTIATING THE WCA

A. *The Elimination of Third-Party Creditor Immunity*

The negotiations began with one of the most notorious consumer-credit issues: the immunity of the third-party creditor from consumer claims or defenses arising out of failures on the part of the retail merchant.⁴⁶ Often the credit purchase of goods or services is financed by an independent creditor rather than by the seller. In such instances, if the goods prove to be defective or if the merchant fails to honor his warranty, the customer normally remains obligated on the debt; the third-party creditor is immune from any claims or defenses that the customer may have against the merchant. The consumer's frustration at being forced to make payments on defective goods is not difficult to appreciate.

43. For some guesses as to what some of these concessions might have been, see text following note 198 *infra*.

44. For a list of the creditors who supported the WCA, see note 21 *supra*. Consumer groups in support of the Act included Wisconsin Consumers' League; Greater Milwaukee Consumers' League; U.A.W., Region 10; Wisconsin State AFL-CIO; National Farmers' Organization; Allied Council of Senior Citizens; Milwaukee County Labor Council (AFL-CIO); and Madison Federation of Labor (AFL-CIO). Crandall, *supra* note 21, at 334-35 n.6.

45. The Act was passed overwhelmingly in the Democrat-controlled Assembly but was initially defeated in the Republican-controlled Senate. Capital Times (Madison, Wis.), March 3, 1972, at 36, col. 1. The defeat was attributed primarily to the efforts of Household Finance Corporation. *Id.* However, the Senate moved to reconsider the bill, and, after a few minor changes, it was passed a week later. *Id.*, March 9, 1972, at 1, col. 7.

46. The elimination of this immunity is often referred to as the abolition of the holder in due course doctrine, but the doctrine is only partly responsible for the immunity. See Jordan & Warren, *The Uniform Consumer Credit Code*, 68 COLUM. L. REV. 387, 433-38 (1968); Kripke, *Consumer Credit Regulation: A Creditor-Oriented Viewpoint*, 68 COLUM. L. REV. 445, 469-73 (1968); Littlefield, *supra* note 6; Murphy, *supra* note 4, at 315-20.

Immunity is achieved in various ways, depending on the type of transaction involved. If the lender makes a direct loan to the consumer, there is no contractual tie-up to the merchant from whom the goods are eventually purchased. In the absence of a special statutory provision immunity is automatic, regardless of the relationship that the lender may have with the merchant.⁴⁷ Where the loan is indirect—that is, where the seller initially extends the credit and then sells the paper to the creditor—immunity may result in one of two ways. If the customer has signed a negotiable note, the creditor simply takes the note as a holder in due course. If there is no negotiable note, the customer's contract is assigned to the creditor. The contract invariably contains a clause wherein the customer waives all defenses against an assignee. Although their enforceability has been successfully attacked in a number of states,⁴⁸ these waiver-of-defense clauses are usually enforced, and immunity is achieved.⁴⁹

Basically, the argument for restricting the third-party creditor's immunity is that the creditor normally has a continuing relationship with the merchant and, by buying the merchant's paper, is helping

47. Widely variant relationships between merchants and direct lenders abound. For example, it is quite common for lender and merchant to enter into a mutually beneficial referral agreement wherein the merchant suggests to the customer that the particular lender would be likely to finance the purchase. The creditor, of course, would prefer to be the only source of credit suggested. However, it is not uncommon for a merchant to recommend more than one possible lender. The customer of a highly reputable merchant will have no trouble obtaining credit, provided the customer is creditworthy. Hence, unless he receives some kind of a commission, the merchant has no reason to agree to limit his referrals to one lender. See Kripke, *supra* note 46, at 471. On the other hand, even if a customer is a good credit risk, many lenders are leery of making loans for the purchase of goods from a less reputable merchant, because, even if there is no legal liability, a dissatisfied customer is troublesome and the lender would prefer to avoid such problems. Hence, the less reputable merchant is delighted to find a lender who will accept his referrals, and no further consideration is needed to induce exclusive referrals.

There exist, of course, many other kinds of creditor-merchant relationships, among them captive finance companies, familial relationships within lender-merchant management, and interlocking directorships. Moreover, regardless of any such relationship, it is common practice for the lender to make out the loan check directly to the merchant, particularly where the lender retains a security interest in the goods purchased.

Classically, the immunity of direct lenders is not affected by the existence of such relationships, regardless of the intimacy of the relationship. As long as the lender is not a party to the sale contract, the customer has no claim or defense against him. Littlefield, *supra* note 6, at 292-93 n.76.

48. See, e.g., *Fairfield Credit Corp. v. Donnelly*, 158 Conn. 543, 264 A.2d 547 (1969); *Quality Fin. Co. v. Hurley*, 337 Mass. 150, 148 N.E.2d 385 (1958); *Unico v. Owen*, 50 N.J. 101, 232 A.2d 405 (1967).

49. The cases in this area are far from unanimous in either theory or result. In 1954, the weight of authority favored immunity. Gilmore, *The Commercial Doctrine of Good Faith Purchase*, 63 YALE L.J. 1057, 1096 (1954). At that time Professor Gilmore saw a trend toward elimination of immunity. However, this trend was not so apparent to Professor Kripke, writing more recently. See Kripke, *supra* note 46, at 469.

the merchant to stay in business.⁵⁰ When the merchant sells defective goods or fails to perform his contractual obligations, the creditor is, in a sense, an accomplice and should share the responsibility.

There was apparently never any question among the first-stage negotiators of the WCA that the completed bill would provide for some third-party liability. All parties agreed that consumers had been unfairly treated in some cases. Moreover, creditors had agreed to limited liability in the legislative advisory committee negotiations over the UCCC,⁵¹ and the banks did not intend to try to regain what they had given up there. Indeed, all parties agreed to some extent that the doctrine's time had run out. The problem was to define mutually satisfactory limits to the newly created liability.

Original A.B. 1057 sought to eliminate creditor immunity in consumer transactions through three separate provisions, which (1) prohibited the taking of a negotiable instrument and subjected any holder of a negotiable instrument to the claims and defenses of the debtor to the extent of the transaction total;⁵² (2) subjected an assignee, any waiver clause notwithstanding, to customer claims and defenses to the extent of the transaction total;⁵³ and (3) subjected the direct lender, to the extent of the amount financed, to all customer claims and defenses arising out of an "interlocking loan."⁵⁴

The banks' position on immunity was complex. Regulation of the financing of retail purchases necessarily affects the retailer, as well as the creditor. Often the retailer from whom the bank buys consumer paper is also the bank's commercial customer. Thus, in order to maintain amiable relationships in the business community, the banks were forced to represent the interests of those retail con-

50. Where the creditor buys the paper free of consumer defenses, the creditor helps the disreputable merchant avoid his responsibilities to customers. The nonjudgment-proof customer is forced to pay, and his only recourse as to the merchant is to bring a civil suit—an alternative that rarely appears inviting to consumers. Clearly, it would be more difficult for such merchants to stay in business without this assistance. Moreover, this type of financier is justifiably singled out because other types of financing (for example, inventory or accounts receivable financing, or sale of stock) do not offer this particular benefit.

51. The advisory committee had adopted alternative A of UCCC section 2.404, wherein an assignee is subject to customer claims and defenses to the extent of the amount owing when the claim is raised. However, in addition to the UCCC exception of agricultural-purpose transactions from operation of the section, the committee had also excepted motor vehicle purchases. Regarding negotiable instruments, the committee had adopted UCCC section 2.403, which provides that, except in sales or leases for agricultural purposes, the seller or lessor may not take a negotiable instrument other than a check as evidence of the obligation of the consumer.

52. A.B. 1057, § 422.405. See NATIONAL CONSUMER ACT § 2.405.

53. A.B. 1057, § 422.406. See NATIONAL CONSUMER ACT § 2.406.

54. A.B. 1057, § 422.407. See NATIONAL CONSUMER ACT § 2.407.

cerns that were absent from the negotiations, as well as their own interests.

Initially, the banks thought three changes were essential. First, the complete nullification of waiver-of-defense clauses in credit sales was unacceptable.⁵⁵ The banks were willing, however, to accept a delay period during which the assignee-creditor would be subject to customer claims and defenses against the merchant, but after which waiver clauses would be enforceable. Second, the banks sought a narrower definition of interlocking loans, especially with regard to credit card transactions. Third, they sought to decrease the amount for which a third-party creditor may be liable on an individual claim.

1. *Delay Period on Waiver-of-Defense Clauses*

While in some states waiver-of-defense clauses are completely unenforceable in certain kinds of contracts,⁵⁶ a number of states make them unenforceable only for a limited time after the customer has been notified of the assignment of his contract.⁵⁷ Once the delay period has passed without the customer having asserted any claim or defense, the waiver is enforceable, and creditor immunity results.

Original A.B. 1057 subjected an assignee to customer claims and defenses without a time limit;⁵⁸ the assignee-creditor's liability was coextensive with the liability of the merchant. As long as the merchant was legally obligated to the customer, either contractually or otherwise, the creditor was potentially liable for any failure to perform on the part of the merchant.

The prospect of indefinite potential liability was very trouble-

55. No Wisconsin creditor was concerned about the prohibition of the use of negotiable instruments in credit sales. While such notes were not completely obsolete in Wisconsin, no large national or local retailer used them.

56. See, e.g., NEV. REV. STAT. § 97.275 (1967) (retail installment sales contracts); N.M. STAT. ANN. § 50-16-5 (Supp. 1971) (retail installment sales contracts); PA. STAT. ANN. tit. 69, §§ 615(f)-(g) (1947) (retail installment sales of motor vehicles); WASH. REV. CODE ANN. § 63.14.150 (1968) (retail installment sales contracts).

57. Typically, this delay period is fairly short. See, e.g., DEL. CODE ANN. tit. 6, § 4312 (Supp. 1970) (15-day notification period for all retail sales); ILL. ANN. STAT. ch. 121-1/2, § 262D (Supp. 1972) (five-day notification period for all installment sales except motor vehicles); MICH. COMP. LAWS ANN. § 445.865(d) (1967) (15-day notification period for all retail installment sales except motor vehicles); PA. STAT. ANN. tit. 73, § 50-207 to -208 (Supp. 1972) (15-day notification period for home improvement retail installment sales); PA. STAT. ANN. tit. 69, § 1402 (Supp. 1972) (45-day notification period for all retail installment sales except home improvements and motor vehicles); TEX. REV. CIV. STAT. ANN. art. 5069-6.07 to -7.08 (1970) (30-day notification period for all retail installment sales).

58. A.B. 1057, § 422.406. This provision was identical to NATIONAL CONSUMER ACT § 2.406. The MCCA made no change in this policy. See MODEL CONSUMER CREDIT ACT §§ 2.601-.602.

some to the banks. Although they admitted that the thirty to forty-five days usually provided by statute⁵⁹ is too short to protect the customer adequately, the banks argued that the economics of financing credit sales require some cutoff point beyond which the creditor's potential liability is extinguished. It is a common practice among indirect lenders to hold a portion of the contract price in a reserve account as protection against nonpayment. The size of the account is normally determined to be a percentage of the total outstanding accounts purchased from the particular dealer. Money is released from the account to the dealer periodically, depending on the status of the portfolio. It was argued that the increased potential creditor liability would require increases in reserves and that the absence of a time limit on potential liability would make it impossible to determine how to manage these accounts. The result, it was suggested, would be increased dealer costs, which would be passed on to the customer.

Consumer representatives were willing to compromise. However, since the banks were not really arguing their own case,⁶⁰ the consumer representatives drove a hard bargain. Believing that the vast majority of legitimate complaints arise within the first year of the contract, consumer representatives agreed to delay the effectiveness of waiver-of-defense clauses for twelve months after notice to the customer of the assignment.⁶¹ They insisted, however, that the delay period be so terminated only if the assignee is not "related to"⁶² the

59. See note 57 *supra*.

60. It was clear that the banks could protect themselves through holdback accounts and recourse agreements. Generally, throughout the negotiations, consumer representatives were not very receptive to arguments made by proxy. Hence, since the primary bank concern was protection of the retailer's interest, bank representatives were at something of a disadvantage.

In addition, the validity of the creditors' argument is questionable. If the merchant is highly reputable, the number of valid claims wherein the merchant refuses to satisfy the customer will be minute, and the impact of liability on the lender will be correspondingly light. See Kripke, *Chattel Paper as a Negotiable Specialty Under the Uniform Commercial Code*, 59 YALE L.J. 1209, 1215-16 (1950).

Moreover, the release of funds from a holdback account is actually a matter of estimating the probability that an unsatisfied valid claim will arise. Certainly there is a point at which this probability with respect to an individual account is sufficiently low to permit release of the reserve (for example, when any express warranty runs out). Granted, the certainty of a statutory time limit is lacking. But where the creditor carries hundreds (or thousands) of accounts with a merchant, the occasional late-arising claim is not likely to have a serious economic impact. In my opinion, the banks, rather than seeking relief from a severe problem, simply sought the peace of mind that comes of certainty.

61. Wisconsin Consumer Act § 422.407 (2).

62. Wisconsin Consumer Act §§ 421.301(32)-(33) define "person related to" as follows:

(32) "Person related to" with respect to a natural person means:

- (a) The spouse of the natural person;
- (b) A brother, brother-in-law, sister, sister-in-law of the natural person;
- (c) An ancestor or lineal descendent of the natural person or his spouse; and

assignor and the assignee acquires the contract in good faith and for value.⁶³ For the purposes of this section an extremely stringent definition of good faith, which conceivably could require that the creditor be certain of the merchant's good repute if he is to rely on a waiver clause, was included.⁶⁴ Moreover, while the creditor will not be subject to the debtor's claim unless he receives notice of it within the twelve-month period, the WCA contains no restrictions as to what types of notice will be effective.⁶⁵ Presumably, any notice of the customer's claim, regardless of its source or form, will be effective against the creditor if received in time. This could include information received from the merchant, other customers, newspapers, or perhaps even the grapevine. It remains for litigation to establish any limits.

With regard to the immunity of the third-party creditor the UCCC provides two alternatives.⁶⁶ Alternative A invalidates waiver-of-defense clauses entirely, while Alternative B provides for a three-month delay period. Hence, the UCCC essentially takes no position on this issue. The UCCC Redraft, however, discards Alternative B.⁶⁷ Similarly, the National Commission on Consumer Finance recommends indeterminate lender responsibility. Stating that most delaying statutes provide an "unrealistically short" period within which to assert a defense, the Commission concludes that they afford the consumer "no real protection."⁶⁸

(d) Any other relative, by blood or marriage, of the natural person or his spouse who shares the same home with the natural person.

(33) "Person related to" with respect to an organization means:

(a) A person directly or indirectly controlling the organization, controlled by the organization or, who together with the organization, is under common control;

(b) An officer or director of the organization or a person performing similar functions with respect to the organization or to a person related to the organization;

(c) The spouse of a natural person related to the organization; and

(d) A relative by blood or marriage of a person related to the organization who shares the same home with him.

Section 421.301(31) defines "person" to include both natural persons and organizations.

A very similar definition of "person related to" is found in MODEL CONSUMER CREDIT ACT § 1.433.

63. Wisconsin Consumer Act § 422.407(2).

64. The assignee does not acquire the contract in good faith if he has knowledge or written notice of violations of the Act, unconscionable conduct by the assignor, or substantial complaints against the assignor involving such contracts. Wisconsin Consumer Act § 422.407(3).

65. Wisconsin Consumer Act § 422.407(2) simply states that a waiver-of-defense clause is enforceable only by an assignee who "has not received notice of the customer's claim or defense" within 12 months of giving notice of the assignment to the customer.

66. UNIFORM CONSUMER CREDIT CODE § 2.404.

67. UNIFORM CONSUMER CREDIT CODE § 3.404 (Working Redraft No. 4, 1972).

68. COMMISSION REPORT, *supra* note 23, at 35. See also Jordan & Warren, *supra* note 46, at 434-35 (discussing the New York ten-day delay statute).

Since most defects in consumer goods should become apparent within a year, it cannot be said that the WCA offers "no real protection." On the other hand, the benefit of the clause to the creditor after the delay period seems only marginal.⁶⁹ In that light it seems harsh to leave the rare customer whose claim arises after the delay period without recourse.

2. *Interlocking Loans*

The primary objective of interlocking loan provisions is to prevent creditors from avoiding the restriction of creditor immunity in credit sales simply by changing the form of the transaction. For example, in the normal third-party-financed credit sale, the merchant "supplies" the financing and then immediately sells the paper or assigns the contract to the creditor. Under the WCA, the creditor would be subject to the claims of the customer against the merchant for at least twelve months after notice of the assignment. On the other hand, if the customer had obtained a direct loan from the same creditor and used the proceeds to purchase goods from the merchant, the WCA would not subject the creditor to customer claims against the merchant. Given this dichotomy, it would seem simple enough for the lender to retain his immunity by extending the credit directly to the customer. Presumably, the creditor could accomplish this merely by supplying the merchant with the proper forms.⁷⁰ But such meaningless changes of form should not allow the creditor to escape the operation of the statute.

On the other hand, in some circumstances the direct lender has no tie to the merchant, and it cannot be said that he has simply made the same loan directly that he would have made indirectly. In such a case, there is no justification for saddling the creditor with responsibility resulting from the consumer's choice of merchants.⁷¹ The concept of the interlocking loan is intended to draw the line between those direct lenders who should share the responsibility for merchant failures and those who should not.

Draftsmen of consumer-credit legislation now generally seem to agree that the direct lender should bear some responsibility when

69. See note 60 *supra*.

70. Quite often the indirect lender approves the loan before the merchant closes the deal. The actual assignment of the contract is merely a formality, and the distinction between direct and indirect lending is meaningless.

71. The MCCA would impose liability in many cases in which the lender has neither this connection with the merchant nor knowledge of which merchant the consumer will patronize. See note 74 *infra*. However, this view has not received general support. See Kripke, *supra* note 46, at 470-71 n.66; Littlefield, *supra* note 6, at 292-93 n.76.

the loan is closely related to the sale. While the UCCC is silent on this point, the UCCC Redraft adds provisions imposing such responsibility.⁷² Similarly, the National Commission recommends lender liability in "connected loans."⁷³

Original A.B. 1057 defined interlocking loans as those wherein the lender "participated in or was connected with the consumer transaction" in which the proceeds of the loan were used.⁷⁴ The definition of "participated or connected"⁷⁵ included, but was not limited to, all credit card transactions,⁷⁶ loans wherein the seller referred the customer to the creditor,⁷⁷ and the circumstance where "[t]he creditor makes 20 or more loans in any calendar year, the proceeds of which are used in transactions with the same seller"⁷⁸ Not only would a vast number of loans interlock under these provisions,⁷⁹ but the open-ended definition of "participated or connected" would also make it impossible to evaluate prospectively whether a loan would interlock.⁸⁰ This vagueness was anathema to creditors. Arguing that

72. A lender who makes a consumer loan to enable the borrower to purchase or lease goods or services from a particular merchant may be subject to the consumer's claims or defenses against the merchant if

(a) the lender knows that the seller or lessor arranged, for a . . . fee, for the extension of credit by the lender; (b) the lender is a person related to the seller or lessor unless the relationship is remote or is not a factor in the transaction; (c) the seller or lessor guarantees the loan or otherwise assumes the risk of loss by the lender upon the loan; (d) the lender directly supplies the seller or lessor with the contract document used by the consumer to evidence the loan, and the seller or lessor significantly participates in the preparation of the document; or (e) the loan is conditioned upon the consumer's purchase or lease of the goods or services from the particular seller or lender, but the lender's payment of proceeds of the loan to the seller or lessor does not in itself establish that the loan was [s]o conditioned.

UNIFORM CONSUMER CREDIT CODE § 3.405 (Working Redraft No. 4, 1972).

73. COMMISSION REPORT, *supra* note 23, at 37-38.

74. A.B. 1057, § 422.407(1). See NATIONAL CONSUMER ACT § 2.407(1).

The MCCA changes this formulation. It makes the direct lender subject to consumer claims and defenses unless he can show that he had no reason to know that the proceeds of the loan would be used in a consumer transaction. MODEL CONSUMER CREDIT ACT § 2.603(3). While perhaps less vague, this provision is at least as broad as its NCA counterpart.

75. A.B. 1057, § 422.407(2). This provision is very similar to NCA section 2.407(2); however, the Wisconsin bill included one additional type of participation—when "[t]he creditor knows that the seller arranged the extension of credit by the creditor." A.B. 1057, § 422.407(2)(c).

76. A.B. 1057, § 422.407(2)(h). See NATIONAL CONSUMER ACT § 2.407(2)(g).

77. A.B. 1057, § 422.407(2)(f). See NATIONAL CONSUMER ACT § 2.407(2)(e).

78. A.B. 1057, § 422.407(2)(e). See NATIONAL CONSUMER ACT § 2.407(d).

79. The coincidence of a large-volume automobile or appliance dealer and a large lender in the same geographic area would undoubtedly result in satisfaction of the "20 or more loans" requirement in a very short time. In addition, the very common practice of referring a customer to a creditor would presumably result in interlock even though the referral may not have been exclusive and even though there may have been no referral agreement.

80. Arguably, any time the proceeds of a loan are used to purchase goods, the

such a broad definition of interlocking loans would severely restrict the availability of direct credit, bank representatives quickly convinced consumer representatives that these provisions operated far beyond their intended sphere. They suggested that it made more sense to define interlocking loans in terms of a finite number of specific activities and relationships. To that end, the section was entirely redrafted.

It was agreed, fairly uneventfully, that a lender must know or have reason to know that the "proceeds of the loan are used to pay all or a part of the customer's obligation to the [merchant] . . ." if a loan is to interlock.⁸¹ Once this precondition is met, there are six circumstances, any of which gives rise to an interlocking loan under the WCA.

There was substantial agreement on the first four circumstances: (1) where the lender is "related to" the seller,⁸² (2) where the lender supplies the loan forms to the seller,⁸³ (3) where the lender pays a commission to the seller,⁸⁴ and (4) where the lender has a recourse or guarantee arrangement with the seller.⁸⁵ These four circumstances substantially coincide with provisions of the UCCC Redraft⁸⁶ and the Commission Report.⁸⁷ There is no such general agreement among the proposed consumer-credit legislation on the last two interlocking relationships enumerated in the WCA—credit-card sales and consumer-credit transactions with known disreputable merchants.

Intensive negotiations were necessary to determine the extent to which credit-card transactions would be subject to the interlocking loan provisions. As mentioned above, Original A.B. 1057 included

creditor has "participated in" or was "connected with" the sale. Presumably, the NCA draftsmen did not intend the application of section 2.407 to go this far, but it would be impossible to predict where its application might stop short of this.

The MCCA draws this line more clearly. The lender is subject to consumer defenses unless he can show that he had no reason to believe that the loaned funds would be used in a consumer transaction, MODEL CONSUMER CREDIT ACT § 2.603(3).

81. Wisconsin Consumer Act § 422.408(3).

82. Wisconsin Consumer Act § 422.408(3)(a). The definition of "related to" is set out in note 62 *supra*.

83. Wisconsin Consumer Act § 422.408(3)(b).

84. Wisconsin Consumer Act § 422.408(3)(c).

85. Wisconsin Consumer Act § 422.408(3)(d).

86. Uniform Consumer Credit Code §§ 3.405(1)(a)-(d) (Working Redraft No. 4, 1972).

87. COMMISSION REPORT, *supra* note 23, at 37-38. Oddly, the Commission Report does not include the fourth factor (recourse agreement) among those to be considered in evaluating closeness, even though an express agreement between merchant and creditor would be required. However, where such an agreement exists, the parties will probably fall within the Commission's sixth factor—repeated and regular loans resulting from merchant referrals. *Id.* at 38.

all credit-card purchases within this definition.⁸⁸ This was totally unacceptable to the banks, which believed that an insurmountable accounting problem would be created if the majority of charge-card purchases were not exempted from the interlocking loan provisions. That is, if the customer could raise complaints as to small purchases—even if only a few customers exercised this option—it would take a tremendous amount of manpower to track down the individual transactions and charge them back to the merchant. To a business whose profitability depends on the minimization of human processing time, this was a horrifying prospect. Consumer representatives, however, were not willing simply to exclude credit cards from the interlocking loan provisions. Banks that issue credit cards are certainly closely related to the merchants who honor their cards.⁸⁹ The fact that credit is extended through the device of a credit card, rather than through a loan, does not alter the rationale for imposing creditor responsibility. The banks, however, were able to convince the consumer representatives that, to a certain extent, credit cards are not truly a credit device but are merely a substitute for cash. That is, but for the card, the consumer would use cash to make smaller purchases rather than borrow money. Consumer representatives agreed that, in so far as the card is a cash substitute, the creditor is not really helping to keep the merchant in business and should not be subject to the customer's claims against the merchant. Lacking any empirical guidelines, the negotiators settled somewhat arbitrarily on one hundred dollars as the point at which a credit-card purchase becomes a loan rather than a mere expenditure of plastic money. Hence, the fifth circumstance in which interlock is found under the WCA is a credit-card purchase in excess of one hundred dollars.⁹⁰ On such purchases the bank is subject to customer defenses against the merchant; for smaller charges, the customer cannot use such defenses.⁹¹

88. A.B. 1057, § 422.407(2)(h). See NATIONAL CONSUMER ACT § 2.407(2)(g).

The MCCA makes no change in this policy. Although there is no explicit reference to credit-card transactions, they are undoubtedly covered by the broad MCCA language. See MODEL CONSUMER CREDIT ACT §§ 2.603(3)-(4). Certainly, the bank knows that the customer will use the credit card in consumer transactions. See note 74 *supra*.

89. Typically, the bank and the merchant enter into a complex agreement that gives the bank the right to charge back to the merchant any purchase for which the customer refuses to pay and calls for the merchant to pay a percentage of the purchase price to the bank. See, e.g., New England Bankcard Assn., Operating Rules, arts. 7, 9.

90. Wisconsin Consumer Act § 422.408(3)(f). Of course, it was also necessary to except credit cards from the section creating interlock where there exists a recourse or guarantee agreement with the merchant. See Wisconsin Consumer Act § 422.408(3)(d).

91. The section is worded in terms of *loans* in excess of one hundred dollars. Presumably, this refers to each discrete transaction. Hence, if a number of items are pur-

In retrospect, all negotiators seemed quite content with this result. The banks succeeded in escaping responsibility for merchant failures in the great majority of credit-card purchases. Further, the banks can protect themselves against the failures of a specific merchant by establishing a limit of one hundred dollars for purchases from that merchant. Consumer representatives never considered this an area of particular abuse, since the bank credit card is primarily a middle class device; yet, the bank is subject to consumer claims and defenses in the case of large purchases, where the greatest possibility of abuse lies.

The Commission Report recommends the same approach. However, it suggests a purchase price of fifty dollars as the point below which a credit-card purchase does not interlock.⁹² Of course, a fifty-dollar cutoff point is as arbitrary as one of one hundred dollars. If the policy behind the limitation is that at some point credit cards are cash substitutes rather than credit devices, then the true cutoff point would depend on the buying habits of the individual customer. I therefore submit that the talk about "cash substitutes" simply provides a convenient rationale for performing a very practical task—setting a cutoff point high enough that the bank's clerical operations are not severely encumbered, yet low enough to minimize the likelihood of abuse.

The UCCC Redraft also provides for a fifty-dollar purchase price minimum before subjecting the issuer of a bank credit card to the claims and defenses that the cardholder has against the merchant.⁹³ However, it adds a second limitation—that the lender is not so subject unless the cardholder's residence and the place where the purchase was made are within the same state or within one hundred miles of each other. Apparently this limitation is based on the presumption that the lender is unlikely to have a significant connection with a more distant merchant. By comparison, the WCA provision applies only to credit-card purchases made within Wisconsin but contains no such distance limitation.⁹⁴ Also, the UCCC Redraft adds the limitation that the cardholder may assert his claim or defense

chased at one time for a total exceeding 100 dollars, the transaction would interlock. The fact that more than one voucher may have been filled out should be irrelevant. However, this could yield the odd result that the purchase of a 25-dollar appliance interlocks because other goods were purchased at the same time. Of course, if the appliance turns out to be defective, the customer would have a defense only to the extent of 25 dollars. See note 110 *infra* and accompanying text.

92. COMMISSION REPORT, *supra* note 23, at 38.

93. UNIFORM CONSUMER CREDIT CODE § 3.403(2) (Working Redraft No. 4, 1972).

94. Wisconsin Consumer Act § 422.408(3)(f).

against the lender only after having attempted, in good faith, to obtain satisfaction from the merchant.⁹⁵

The objective of the definition of interlocking loans, in so far as the five circumstances discussed above are concerned, is to delineate those situations in which the creditor and the merchant are so closely related that the creditor should not be allowed to escape responsibility for the merchant's conduct. There is, however, a second, and much more controversial, objective of the WCA interlocking loan provisions—to force the credit community to police retail merchants. Basically, the rationale is: Some policing is needed, neither the state nor the merchant community has performed the task satisfactorily, the creditor is better able to assume the function than the borrower, and the result of forcing creditors to police merchants will be a more equitable distribution of the costs of policing throughout the community.⁹⁶ In theory, if the creditor is saddled with responsibility for merchant failures, creditors will refrain from financing purchases from the less reputable merchants in the community.⁹⁷ Creditors, of course, do not feel that this burden should be theirs.

In order to coerce creditor policing the definition of interlocking loans must be broad. If a loan interlocks only where the creditor and merchant have a manifest working agreement, no significant policing will result, for creditors will surely refrain from entering into such agreements with disreputable merchants. As long as the danger of interlocking is so easily avoided, there will be no impetus to refuse a loan to a customer who intends to apply the proceeds to the purchase of goods or services from such a merchant.

Original A.B. 1057 contained no specific provision aimed to this end; however, its definition of interlock⁹⁸ was so pervasive that no specifically directed provision was needed.⁹⁹ When the section was

95. UNIFORM CONSUMER CREDIT CODE § 3.403(3)(a) (Working Redraft No. 4, 1972). Certainly this makes good sense, but the provision's impact is likely to be minimal. The vast majority of customers will probably look first to the merchant as a matter of common sense. Moreover, since the banks are concerned about maintaining affable relationships with customers, they are not likely to ignore a complaint simply because the customer brought it to the bank first. Rather, the bank is more likely to contact the merchant and to act as a mediator in the dispute.

96. This view is not unique. For a thorough discussion of the competing policies and the suggestion that the UCCG deal with this problem, see Littlefield, *supra* note 6, at 280-97.

97. By "less reputable" or "disreputable" merchants, I mean merchants who, with some regularity, fail to perform their agreements with customers or who fail to remedy valid complaints.

98. See text accompanying notes 74-80 *supra*.

99. Surely this result was intended by the draftsmen of the NCA. See NATIONAL CONSUMER ACT § 2.407, Comment 2.

The MCCA goes still further. The nonexclusive list of circumstances for which a

redrafted to define interlocking loans in terms of specific, identifiable relationships, consumer representatives insisted that a section coercing creditor policing be included. They would have liked every loan that found its way into the hands of a disreputable merchant to interlock. Banks insisted that, at most, a loan should interlock only if it is made by a creditor who knows that the merchant is disreputable. The issue for negotiation was thus narrowed to what kinds of lender knowledge of merchant reputations would give rise to interlock. The final formulation includes "knowledge from [the lender's] course of dealing with other customers of the [merchant] or from the lender's records, or written notice of substantial complaints by such other customers, that [the merchant] fails or refuses to perform his contracts with them and . . . fails to remedy such complaints within a reasonable time."¹⁰⁰ Bank representatives now fear that this provision will have a more pervasive impact than they initially intended. Consumer representatives, content with this result, suggest that knowledge of a merchant derived from other customers could reasonably include grapevine information and that written notice should include such sources as newspaper and better business bureau reports. It remains for the courts to establish the ultimate reach of the provision.

Neither the UCCC nor the UCCC Redraft contains a knowledge-of-disreputable-merchant provision. Apparently, the UCCC Special Committee agrees with creditors that the burden of policing retail merchants belongs elsewhere. The National Commission, however, includes among the factors and incidents that it considers relevant to a determination of close connection, a provision nearly identical to that of the WCA.¹⁰¹

The first-stage redrafting of the interlocking loan provisions was nearly totally acceptable to all creditors participating in the second-stage negotiations. However, the consumer finance company representatives did insist on one change: A prerequisite that "all or a meaningful part" of the proceeds of the loan be used in the purchase¹⁰² was added to the definition of interlocking loans. Consumer

lender will be "deemed to have knowledge" that the loan proceeds will be used in a consumer transaction is even more extensive than the NCA list of circumstances giving rise to participation or connection. Compare MODEL CONSUMER CREDIT ACT § 2.603(4) with NATIONAL CONSUMER ACT § 2.407(2).

100. Wisconsin Consumer Act § 422.408(3)(e).

101. COMMISSION REPORT, *supra* note 23, at 38. The Commission's terminology is somewhat illogical, since a creditor's knowledge of a merchant's reputation hardly establishes a close connection.

102. Wisconsin Consumer Act § 422.408(3).

finance companies often make multipurpose loans, the proceeds of which might be used to consolidate existing loans or to purchase goods from more than one merchant. They argued that it was anomalous that an entire loan should interlock where only a small portion of its proceeds were applied to purchases from the merchant with whom the lender is said to have an interlocking relationship.¹⁰³

3. The Financial Liability Limit

The final bank objective concerning the liability of third-party creditors was to reduce the extent to which a creditor might be liable on an individual claim. Original A.B. 1057 provided for creditor liability up to the amount of the total transaction in credit sales and up to the amount financed in the case of interlocking loans.¹⁰⁴ The banks believed that since the creditor is not directly responsible for the merchant's failure, its liability should not in any event exceed the amount due on the obligation at the time the defense is raised.

As suggested above,¹⁰⁵ the Wisconsin consumer representatives felt that creditors kept many merchants in business by financing their sales,¹⁰⁶ whether by purchasing the merchants' paper or by making interlocking loans.¹⁰⁷ They felt that creditor liability should

103. But note, where only a portion of an interlocking loan is used in the purchase on which the customer's claim is based, lender liability is limited to that amount. See note 110 *infra*. Why, then, should a small loan that would otherwise interlock not do so simply because it was not "a meaningful part" of a large multipurpose loan?

104. A.B. 1057, § 422.406 (credit sales). See NATIONAL CONSUMER ACT § 2.406. A.B. 1057, § 422.407(1) (connected loans). See NATIONAL CONSUMER ACT § 2.407(1).

The MCCA extends the potential liability of the creditor beyond the transaction total. Credit-sale financiers and lenders are both subject to all of the claims and defenses of the consumer arising out of the transaction financed. MODEL CONSUMER CREDIT ACT §§ 2.602(2) (credit sales), 2.603(2) (loans). The creditor can limit his potential liability if he acquires the obligation of the consumer "in good faith, for value, without notice of any claims, defenses or equities and continues to act in good faith" thereafter. MODEL CONSUMER CREDIT ACT § 2.603(2) (lenders). See also MODEL CONSUMER CREDIT ACT § 2.602(2) (credit sales). If these requirements are met the liability of a sales financier is limited to the transaction total, MODEL CONSUMER CREDIT ACT § 2.602(2), and that of a lender is limited to the amount of the loan plus the finance charges. MODEL CONSUMER CREDIT ACT § 2.603(2). However, for the purposes of these provisions, a creditor is not in good faith if, having reason to know of a claim, he attempts to collect the obligation. MODEL CONSUMER CREDIT ACT § 2.601(3)(a).

105. See note 50 *supra* and accompanying text.

106. While there are, of course, many substantial retailers who carry their own credit, or at least a great deal of it, most merchants depend heavily on the availability of outside financing. The Wisconsin consumer representatives believed that much of the consumer abuse occurs at the hands of insubstantial, inefficient, and often undercapitalized merchants who, but for creditor support, would not be in business.

107. While the interlocking lender does not supply the merchant's working capital as clearly as does the purchaser of the merchant's paper, the circumstances giving rise to interlock certainly call for some creditor responsibility. The NCA and A.B. 1057 dichotomy in potential liability between "transaction total" in sales and "amount financed" on loans is apparently based on the presumption that the interlocking lender

extend to the amount of the entire transaction. Consumer representatives realized, however, that primary responsibility should lie with the merchant. Hence, their objectives concerning creditor responsibility were twofold: First, where a valid consumer claim or defense arises, the consumer should be able to stop making payments and set off the value of any claim against the amount due; and, second, if the consumer has a claim in excess of the amount due and is unable to obtain redress against the merchant (for example, where the merchant is insolvent or unavailable), the customer should be able to look to the creditor.

Once the objectives of the consumer representatives were clear, the negotiators were able to arrive at a mutually satisfactory compromise. They devised the following two-stage formula: First, the creditor is subject to customer claims and defenses to the extent of the amount owed at the time the defense is raised. Second, if judgment against the merchant has been obtained and execution returned unsatisfied,¹⁰⁸ the creditor is additionally liable up to the total amount financed (including finance charges). On the theory that the creditor is actually involved in the transaction only to the extent of the amount financed, the customer may look solely to the merchant for his down payment. This formula applies to both credit sales¹⁰⁹ and interlocking loans.¹¹⁰

In sharp contrast to the WCA, the unwavering position of the UCCC Special Committee is that creditor liability should never extend beyond the amount due at the time that notice of the claim is received.¹¹¹ The National Commission, on the other hand, recom-

is somehow not as deeply involved in the transaction; that is, the interlocking lender is involved only to the extent of the amount of the loan, whereas the credit-sales financier is more like the merchant's partner. To the extent that the financing is essential to the merchant's operation, the distinction seems specious—a conclusion that the Wisconsin negotiators reached without difficulty.

108. Until this event has occurred, except where the merchant is in bankruptcy, receivership, or other insolvency proceedings, the debtor may assert any claims against the creditor only by way of counterclaim, defense to or set-off against claims brought by the creditor. Wisconsin Consumer Act § 422.407(5). This protects the creditor against being automatically joined in every action against the merchant; where the merchant is solvent, the creditor retains the prerogative to avoid involvement. Since the normal credit-sale financier is bound by the litigation, see note 114 and text accompanying notes 113-14 *infra*, the customer is not prejudiced by his inability to join the creditor. The provision was added late in the negotiations, chiefly at the insistence of the consumer finance companies.

109. See Wisconsin Consumer Act §§ 422.406(4) (regarding holders of negotiable instruments), 422.407(2) (regarding assignees of consumer contracts).

110. Wisconsin Consumer Act § 422.408(4). Of course, this liability is limited to the portion of the loan used in the purchase on which the claim is based.

111. UNIFORM CONSUMER CREDIT CODE §§ 2.404A, .404B. The UCCC Redraft suggests no change in this policy. UNIFORM CONSUMER CREDIT CODE §§ 3.403(3)(b), .404(2), .405(2) (Working Redraft No. 4, 1972).

mends substantially the same outside limits on creditor liability as those adopted by the WCA,¹¹² but does not recommend that the customer be required to look first to the merchant for recovery of any claim in excess of the amount due on the account. I submit that, although it is more complex, the Wisconsin approach is preferable to those of the UCCC and the National Commission. Since the amount that is due when the claim is raised depends entirely on the time that the merchant's failure becomes apparent, the UCCC approach seems quite arbitrary. If the creditor is to be subject to customer claims against the merchant, I see no reason why his liability should be less if a defect in the goods or services appears six months after the sale than if the defect appears immediately. Also, where the customer's claim exceeds the amount due, requiring the customer to obtain judgment against the merchant is preferable for two reasons. First, it ensures that the party truly responsible for the claim will pay if possible. Creditor liability will exceed the amount due on the account only in the unusual case where execution against the merchant is returned unsatisfied. Second, it reduces the cost to the creditor that would arise if he were unnecessarily joined in customer-merchant litigation.

At first blush, these requirements seem to be an added burden for the consumer. However, the burden has been minimized in the WCA. If judgment against the merchant is obtained by default, the customer will not have been put to a great deal of trouble. If, in the case of credit sales, the issue of the merchant's failure to perform has been litigated the creditor is bound by the judgment.¹¹³ The situation is somewhat different in the case of interlocking loans, since the lender is not bound by any judgment that the customer may obtain against the merchant.¹¹⁴ However, once the customer establishes that the loan interlocks, the creditor is likely to concede the issue of

112. COMMISSION REPORT, *supra* note 23, at 35-36. The Commission recommends that under negotiable instruments and contracts, liability should not exceed the original amount financed, whereas in the case of loans, liability should not exceed the lesser of the amount financed or the amount of the purchase made with the loan proceeds. Although not entirely clear, the "amount financed" presumably does not include finance charges.

113. Wisconsin Consumer Act §§ 422.406(4)(b), .407(2)(b).

114. There is a sensible explanation for this different treatment of sales and loans. Presuming merchant liability, there is never any question as to the creditor's secondary liability in the case of sales. In the case of loans, however, the customer must first establish the existence of an interlocking loan as a condition precedent to lender liability. Hence, in the case of sales the creditor has clear impetus and opportunity to aid the merchant in his defense. The direct lender, on the other hand, might reasonably believe himself immune and thus ignore the merchant's handling of the case. If execution is then returned unsatisfied and the customer can establish interlock, the lender should have the opportunity to relitigate the issue of the merchant's liability.

the merchant's liability. Even if the interlocking lender chooses to relitigate this issue, the customer is unlikely to be severely prejudiced since the WCA provides that the prevailing customer be awarded attorney's fees.¹¹⁵

B. *Delays in the Enforcement of Creditor Remedies: Default, Unilateral Deferral, Cure of Default, and Repossession*

The UCCC does not upset the common law policy that the definition of default be left a matter of contract between the parties. Many consumer advocates see this continuation of common law policy as one of the UCCC's major failings.¹¹⁶ In the consumer setting, the common law presumption of bargaining between the parties is a myth.¹¹⁷ The definition of default, as well as nearly all other contract provisions, is in the hands of the creditor. Unsurprisingly, some of the events of default found in consumer contracts bear only scant relation to the likelihood that the creditor will be paid.¹¹⁸ For example, payment of an installment even one day late is invariably a default. Further, the contract usually contains an acceleration clause that gives the creditor the option, on default, of declaring the entire balance of the obligation immediately due and payable.¹¹⁹ Of course, where the debt is secured, default gives rise to the creditor's Uniform Commercial Code rights to repossess and dispose of collateral.¹²⁰

115. Wisconsin Consumer Act § 425.308.

116. See NATIONAL CONSUMER ACT § 5.103, Comment 1; Clark, *supra* note 14, at 308.

117. See Shuchman, *Consumer Credit by Adhesion Contracts*, 35 TEMP. L.Q. 125 (1962).

118. For example, the pre-WCA motor vehicle security agreement form approved by the Wisconsin Banker's Association and the Wisconsin Installment Banker's Association included the following among the events of default: death of the debtor or surety, failure to perform any obligation under the agreement, and "any other event which causes Secured Party, in good faith, to deem itself insecure." Regarding the likelihood of being paid, the death of a surety could certainly be meaningless, and relevance of the death of the debtor depends on the condition of his estate. Moreover, many of the debtor's obligations under the agreement, if not performed, might well bear no relation to the creditor's likelihood of receiving payment. For example, the debtor is obligated not to permit the value of the collateral to be impaired, regardless of the size of the impairment or the amount due on the obligation. Surely, a 200-dollar dent in the fender of a 3,000-dollar car is irrelevant to the bank if the outstanding balance is 1,000 dollars. Finally, the creditor could in good faith deem itself insecure on the basis of an erroneous tip that the debtor is about to abscond.

To be sure, all the events of default defined in this security agreement could be relevant to the creditor's likelihood of being paid. However, nothing in the security agreement guarantees it.

119. 2 G. GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY 1195 (1965): "For a hundred years, it may be, no security agreement has failed to include an acceleration clause." See also J. WHITE & R. SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE § 26-3, at 958 (1972).

120. UNIFORM COMMERCIAL CODE §§ 9-501, -503 to -504.

Although the Wisconsin consumer representatives recognized that creditors rarely take advantage of these default provisions, they felt that the common law policy gives creditors the power to discriminate in the individual case. Although such power might be justifiable in the commercial setting, where it has been bargained and paid for, the consumer representatives felt it has no legitimate place in the consumer-credit world. They believed that no creditor should be allowed to take affirmative action against a consumer unless the contract breach has a material impact on the creditor's likelihood of receiving payment and that mere delinquency on a single installment has no such impact.¹²¹ They further believed that even where a debtor has committed a material breach he should be given a reasonable opportunity to reinstate the contract. Thus, in Original A.B. 1057 they severely restricted the definition of default and further regulated the circumstances under which the creditor could accelerate the obligation or take any other action.

The negotiations concerning these provisions were extremely arduous. Though all creditor groups were concerned, some were much more intensely concerned than others. Many creditors rarely resort to repossession; they rely on security interests, if at all, as a psychological tool to help induce payment. Therefore, they were willing to accept any scheme that would not severely disrupt their normal collection activities. However, many other creditors, chiefly automobile financiers, rely heavily on collateral in extending credit. Repossession and disposal of collateral is an essential part of their business operation. Any delay in the accrual of their right to repossess or dispose of collateral may result in losses.¹²² Since the potential impact of these restrictions on their interests was considerable, their negotiating position was intractable.

1. *Default and Unilateral Deferral*

Original A.B. 1057 defined default as (a) failure to pay three successive installments when due, (b) failure to pay the balance due

121. See Crandall, *supra* note 21, at 357-58. Crandall, the key Wisconsin consumer negotiator, emphasizes the need to reinstate the doctrine of material breach in consumer contracts and that at common law missed payments alone were not considered material enough to justify acceleration of the entire obligation.

122. Johnson, Denial of Self-Help Repossession: An Economic Analysis, in Brief for the Permanent Editorial Board for the Uniform Commercial Code as Amicus Curiae, app. A., at 26-34, *Adams v. Southern Cal. First Natl. Bank*, 42 U.S.L.W. 2230 (9th Cir., Oct. 4, 1973). A version of Professor Johnson's paper can be found in 47 S. CAL. L. REV. 82 (1973).

within three months of the date for final payment, or (c) delinquency on installments totaling thirty per cent of the amount financed.¹²³ It also provided that if the customer were ten days delinquent on any installment, he had the unlimited right to (1) defer the payment, (2) refinance the unpaid balance, or (3) consolidate the unpaid balance with that of another transaction.¹²⁴ Since the effect of each provision is to delay accrual of the creditor's right to take action against the debtor, the definition of default and the unilateral deferral-refinance-consolidation right became a single package in negotiations.

At first-stage negotiations, bank representatives were initially concerned that default was defined only in terms of nonpayment.¹²⁵ They argued that credit is often extended in genuine reliance on collateral and that in such cases, if the actions of the debtor jeopardize the value of the collateral or the creditor's ability to realize on it, the creditor ought to be able to protect his interest. The banks did not have much difficulty convincing consumer representatives that if the vendor were powerless to protect his security interest, collateral-based credit would be severely restricted and low-income consumers would find it difficult to buy cars. Hence, consumer representatives agreed to include in the definition of default the customer's failure to observe a covenant in the contract, "breach of which materially impairs the condition, value or protection of or the creditor's right in" the collateral.¹²⁶ On the theory that the unsecured creditor needs similar protection, a breach that "materially impairs the customer's ability to pay" was also included.¹²⁷

123. A.B. 1057, § 425.103(1). See NATIONAL CONSUMER ACT § 5.103(1). The "amount financed" does not include the finance charge. A.B. 1057, § 421.301(5); NATIONAL CONSUMER ACT § 1.301(5). The MCCA discards this formula. The primary thrust of its approach is that the debtor is in default when he is delinquent on installments amounting to more than fifteen per cent of the transaction total. See MODEL CONSUMER CREDIT ACT § 7.102. There is no provision for default arising from debtor conduct other than nonpayment.

124. A.B. 1057, § 422.203(1). See NATIONAL CONSUMER ACT § 2.203(1).

125. For reasons unclear to me, draftsmen of the NCA considered this a fundamental principle. See NATIONAL CONSUMER ACT § 2.203, Comment 1.

126. Wisconsin Consumer Act § 425.103(2)(c).

127. Wisconsin Consumer Act § 425.103(2)(c). This phrase came in on the heels of the collateral-jeopardy provision. Consequently, and unfortunately, it did not receive much attention. The result is far too broad a grant of power to the creditor, power the creditor does not need. To be sure, there are circumstances in which the unsecured creditor needs to act quickly to protect his interests, such as when the debtor makes a fraudulent conveyance or begins to move his personalty out of the state. Indeed, these are the sort of circumstances that the WCA draftsmen had in mind. But the broad material-impairment-of-ability-to-pay provision extends far beyond such extreme circumstances. Presumably, events such as loss of job, illness, and divorce can amount to a default under this provision—even before the debtor's next payment is due. Conceivably, the creditor whose forms contain the right debtor covenants will hold the

Creditor representatives at the second stage had no objections, and the section was adopted as revised.

The definition of default as three *successive* installments outstanding was totally unacceptable to all creditors, so it was discussed early in the first stage of negotiations. The possibility that a debtor could, without default, miss two installments, pay one, and then miss two more was mind-boggling. Although creditor representatives were willing to agree that default based on a one-day delinquency may be too severe, they were quite concerned about the potential losses that result from any significant delay in the accrual of repossession rights. Therefore, they argued that default should occur within a reasonably short time after a payment is missed.

Consumer representatives never truly expected the original definition to remain. Yet they staunchly opposed the accrual of creditor remedies as a result of a single late payment.¹²⁸ They were willing to discuss such a definition of default, however, since under Original A.B. 1057, the debtor who was having difficulty meeting his payment schedule could elect to modify the contract terms.¹²⁹ The creditors, of course, were hardly pleased with the prospect of unilateral modification.

It took creditor representatives little time to convince consumer representatives that unilateral refinance and consolidation were simply unworkable. The exercise of such rights would have required the complete rewriting of the contract with new terms, payment schedules, and other arrangements, which would simply not be pos-

same power he once held under the now infamous insecurity clause. Surely, such creditor latitude is unjustifiable. Any impaired-ability-to-pay test should be limited to those cases where the creditor has a legitimate need to act quickly to protect his interests. Otherwise, where collateral is not jeopardized, the creditor should be required to wait until a default in payment has occurred.

Of course, this result could be achieved through a very strict construction of "material impairment," either by administrative rule or by the Wisconsin courts. It is to be hoped that such a construction will be adopted.

128. The materiality of a single delinquent payment is not susceptible to easy analysis—especially in a vacuum. The true significance of a delinquency is not the injury to the creditor. Rather, a delinquency is significant because it is an indication that later payments might not be made. If a customer has consistently paid prior installments within ten days of the date due, a five-day delinquency indicates nothing. On the other hand, if a debtor has a poor payment record and if his contract has just been renegotiated, a five-day delinquency might be a strong indication that more trouble is in the offing. To repossess the first debtor's car after a five-day delinquency hardly seems justifiable. In the second instance, however, the equities seem to have changed—the delinquency seems more material. In both cases, we know more than the mere fact that there was a single delinquency. The surrounding facts were critical to the evaluation of materiality; they were critical to the "indication value" of the delinquency. Hence, consumer representatives were probably correct in asserting that a single delinquency, of itself, should not be a default.

129. A.B. 1057, § 422.203(1). See NATIONAL CONSUMER ACT § 2.203(1).

sible in a unilateral sense; to set down statutory guidelines for such contracts would also have been impossible. Consumer representatives readily agreed to eliminate these provisions. Their primary concern was really the right to defer payments. Yet, without limitations this provision would also be unworkable, for it would allow the debtor to defer all installments indefinitely. Thus, the problem at the first stage was narrowed to finding a mutually satisfactory combination of a strict default definition plus a restricted unilateral deferral right. The result was that a complex list of limitations accompanied the unilateral deferral right,¹³⁰ while default was defined as a single delinquency of more than ten days or a material breach of some other covenant.

This agreement, however, proved to be short-lived, as second-stage creditor representatives were far from satisfied. Even as limited, the concept of unilateral deferral was disconcerting, especially to consumer finance companies. It was seen as a source of accounting problems, especially for computerized credit operations, and as a paperwork burden since every delinquent debtor would have to be notified of his deferral right. Moreover, and one of the most significant creditor objections, contract adjustments have always been seen as an accommodation to the customer, and creditors thought that they should be able to choose those customers to whom such favors should be extended. Where the customer has a legitimate reason (such as illness or layoff) for his inability to make a payment, creditors may normally be willing to make adjustment. But the thought of a deadbeat being able to defer payments at will was a particularly bitter pill.

Due largely to the efforts of consumer finance company representatives, an uneasy compromise was eventually reached. The unilateral deferral right was thrown out entirely, and the definition of default for nonpayment became concurrent delinquency of more than ten days on *any two* installments.¹³¹ The rationale was that giving the debtor one "free" missed payment is tantamount to an automatic deferral. The creditor cannot take action against the debtor for one delinquent payment. However, the creditor knows when default occurs, accounting problems are minimized, and the

130. Among the limitations were: (1) No payment could be deferred for more than 180 days; (2) no right of deferral would exist for any of the first six installments; and (3) no more than two installments could be deferred in any twelve-month period.

131. Wisconsin Consumer Act § 425.103(2)(a). If the interval between payments is more than two months, default is defined as a delinquency of more than 60 days. On open-end plans, default is failure to make payment when due on two occasions within a 12-month period, Wisconsin Consumer Act § 425.103(2)(b).

choice as to who obtains a further deferral remains with the creditor.¹³² Of course, a special provision was needed where the debtor failed to pay the final installment. Creditors also convinced consumer representatives that special treatment should be given to failure to pay the first installment.¹³³ It was agreed that the definition of default in either case would be failure to make such payment within forty days of the date due.¹³⁴

The National Commission takes a somewhat puzzling position on this point. It suggests that default should not be defined by statute, but should be left to the determination of the contracting parties. It adds, however, that default should result only from the breach of "major contract provisions" and that it should not result solely because the creditor believes the prospect of payment has been impaired.¹³⁵ Apparently, the Commission simply hopes that creditors will follow these guidelines, but it suggests no reason for its objection to statutory enforcement of this hoped-for result. Another decided difference between the Commission point of view and the WCA is that the Commission considers failure to make timely payments to be a breach of a major contract provision¹³⁶ and believes that affording the debtor a right to cure offers sufficient protection from improvident creditor action.¹³⁷

Notably, the UCCC Special Committee has changed its position and now suggests regulation of the definition of default to an extent nearly identical to the recommendation of the National Commission.¹³⁸

132. Of course, the WCA allows deferral by agreement (section 422.204(1)), and also allows agreements permitting unilateral deferral at the election of the creditor (section 422.204(8)). Since the debtor may prepay all or part of the obligation at any time without penalty (section 422.208), the creditor's unilateral deferral right will not work to the detriment of the debtor except to the extent of the deferral charge.

133. Many creditors seem to attach special importance to the first installment, interpreting failure to pay it promptly as an indication of bad faith on the part of the debtor. Arguably, failure to make this payment is a more material breach than failure to pay some other installment. In addition, the first installment is occasionally larger than the remaining scheduled installments, for it is more like a part of the down-payment than of the amount financed. At any rate, consumer representatives did not see this as a common area of abuse or an unreasonable creditor desire.

134. Wisconsin Consumer Act § 425.103(2)(a). Initially, as a result of a clerical error, the WCA did not reflect the agreement reached on this point. Rather, a default as to the first or last installment was defined as mere failure to pay when due. This error has now been corrected by administrative rule. See Wis. ADMIN. CODE, BANKING § 80.60 (1973).

135. COMMISSION REPORT, *supra* note 23, at 25.

136. *Id.*

137. *Id.* See discussion in text accompanying notes 139-58 *infra*.

138. The UCCC Redraft makes enforceable an agreement defining default "only to the extent that (1) the consumer fails to make a payment as required by agreement;

2. Cure of Default

A statutory right to cure default requires that before the creditor is entitled to take any action he notify the debtor of the default and give him a certain amount of time within which to pay the amount of any delinquent installments, without acceleration, or to tender whatever performance is necessary to cure any default other than nonpayment. Having cured, the debtor is reinstated, without penalty, to the position he would have been in had no default occurred. The National Commission found in its survey of creditor practices that before declaring an account delinquent, banks allow an average of 12.2 days and finance companies an average of 16.5 days.¹³⁹ It recommends a statutory 14-day cure period, which would merely be the adoption of current industry practice.¹⁴⁰

Because of this industry practice, and because they had previously agreed to accept a cure provision in the UCCC negotiations,¹⁴¹ Wisconsin creditors were not adverse to the concept of a right to cure. In fact, some of them were staunchly in favor of it.¹⁴² Rather, the debate centered upon questions of (1) the procedure to be followed in effecting notice and cure, (2) whether the right should be forfeitable, and (3) exceptions to the right (that is, when, if at all, the creditor should be able to take action without affording the debtor notice and opportunity to cure).

First-stage negotiators eventually agreed that the procedure for notice and cure set out in Original A.B. 1057 should be scrapped. It had provided that notice of the right and initiation of the running of the cure period could be effected only by service of a complaint in an action brought by the creditor for possession of collateral.¹⁴³ If the debtor cured within fifteen days after service, the action would be dismissed.¹⁴⁴ Negotiators saw no virtue in requiring the creditor

or (2) the prospect of payment, performance, or realization of collateral is significantly impaired" UNIFORM CONSUMER CREDIT CODE § 5.109 (Working Redraft No. 4, 1972). The UCCC contains no provision restricting events constituting default.

139. COMMISSION REPORT, *supra* note 23, at 25, 43.

140. *Id.* at 25.

141. Although the UCCC contains no right to cure, the Wisconsin UCCC legislative advisory committee had included in its recommendation a one-time-per-transaction twenty-day cure period.

142. The collection practice of sending simulated legal process to delinquent debtors has recently come under attack as being unconscionable. Since this practice had been effective in inducing payment, and since affording the debtor a right to cure entails sending him an official notice of the right, many creditors welcomed the change.

143. The only way to obtain possession under the WCA is by filing suit. *See* text accompanying notes 167-76 *infra*.

144. A.B. 1057, §§ 425.206-207. *See* NATIONAL CONSUMER ACT §§ 5.206-207. The

to file suit in order to bring his default rights to fruition.¹⁴⁵ Moreover, this procedure seems particularly frivolous when the creditor does not want possession of the collateral or when there is no security interest at all. Therefore, first-stage negotiators settled, without serious difficulty, on a simplified procedure. Upon default, a fifteen-day cure period begins to run from written notice by the creditor of the customer's right to cure. The passage of this period is a prerequisite to the creditor's exercise of any other rights or remedies.¹⁴⁶ In keeping with the new definition of default, cure is effected by tender of any balance due or by "tendering performance necessary to cure any default other than nonpayment of amounts due."¹⁴⁷ In retrospect, all negotiators seem quite content with this much more workable procedure.

The second right-to-cure issue during negotiation was whether a recalcitrant debtor should ever lose the right to cure, and, if so, when. Suppose, for example, that a debtor buys a new car on credit, the contract to be paid off in three years, with payments to be due on the first of the month. For the first six months of the contract, the debtor consistently makes his payment twenty to twenty-five days late. Each month he receives at least two late notices and, occasionally, a phone call from the bank's collection department. In the seventh month, the debtor makes no payment, and on the eleventh day of the eighth month the bank, having received no payment,

MCCA retains the basic scheme, which requires that the creditor file suit in order to initiate the running of the cure period. MODEL CONSUMER CREDIT ACT § 7.108(1). The basic changes are that under the MCCA the debtor may cure at any time prior to judgment and that the creditor may require the debtor to pay court costs and a performance deposit in addition to making up back payments. MODEL CONSUMER CREDIT ACT § 7.108(2). There are no exceptions to the MCCA right to cure, nor is there any limit to the number of times a debtor may cure during the course of a transaction. MODEL CONSUMER CREDIT ACT § 7.108(5).

145. Arguably, the only reason the creditor would want the cure period to run is so that he can accelerate the loan and sue for possession. However, where the debtor would cure, putting the creditor to the expense of filing suit seems unnecessary. Moreover, even where the debtor does not cure, the expense is unjustifiable unless the creditor actually wants possession of the collateral. It might be argued that the creditor who does not want the collateral has no need for the cure period to run, since he can always try to induce payment through normal collection methods. However, the ability to accelerate the obligation is of value to the creditor even though he does not seek possession of collateral. It allows him to write off the debt and attempt to collect it or assign it to a collector as a lump sum. This saves him the trouble of keeping track of how many payments have gone unpaid. Perhaps the draftsmen of the NCA intended to inhibit acceleration to as great an extent as possible regardless of impact on creditor operations. The Wisconsin consumer representatives, however, sought only to provide the debtor with an opportunity to cure while minimizing the impact on creditor practices.

146. Wisconsin Consumer Act §§ 425.104-.105.

147. Wisconsin Consumer Act § 425.105(2).

sends the debtor notice of his right to cure. Within fifteen days the debtor makes the two back payments plus delinquency fees, and the contract is reinstated. The debtor then misses the ninth payment. When the tenth payment is ten days past due, notice of right to cure is again sent, and the debtor cures within the fifteen-day period. When the eleventh installment is not received, the bank contacts the debtor in hope of helping him solve his apparent financial woes—perhaps to extend the contract and reduce the monthly payments, perhaps to consolidate other obligations into a single lower monthly payment. The debtor is not cooperative; he may even be surly.

At this point, the bank has invested substantial effort in the account, with no let-up in sight. The cost of collecting the debt is beginning to approach the profit on the loan. Some banks, especially those that prefer not to deal with higher risk borrowers, quickly become fed up with troublesome debtors and make a point of getting them off the books as soon as possible. In negotiations, creditor representatives argued that at some point a recalcitrant debtor ought to lose his right to cure; an unlimited right to cure could cause creditors a great deal of trouble and possibly some untoward expense. At the bottom of their argument may have been the feeling that the debtor does not *deserve* an unlimited right to cure.¹⁴⁸

Consumer representatives saw no reason why the debtor should ever lose the right to cure, for if the debtor cures, the creditor receives full interest on the late installments plus a delinquency fee that should at least help to cover the cost of collection. However, consumer representatives were willing to limit the right to cure since, at the end of first-stage negotiations, the debtor still had a unilateral deferral right. Thus, even if the debtor were to lose his right to cure, he could still eliminate any nonpayment default by electing to defer the delinquent payment. Consequently, at the end of first-stage negotiations, the debtor was allowed only one cure opportunity in any twelve-month period.

As discussed above, the unilateral debtor deferral right, even as limited in first-stage negotiations, was distressing to many second-stage creditors. They were intent on eliminating the right, but its

148. Although it was only articulated tangentially, I received the impression from interviewing creditors and creditor representatives that the specter of the deadbeat loomed over the negotiations. The true deadbeat, a debtor who has the ability to pay but does not, is probably quite rare. COMMISSION REPORT, *supra* note 23, at 43. The Commission's survey showed deadbeathood to be among the least common reasons for failure to meet contractual terms. Nevertheless, when a creditor encounters the real thing, it makes his blood boil.

existence had played a key role in the consumer agreement to limit the right to cure. Hence, second-stage creditor insistence on the elimination of unilateral deferral necessarily undermined the first-stage agreement reached on cure—just as it undermined the first-stage agreement on default. Finally, as part of the decision to eliminate the unilateral deferral right, the negotiators agreed to provide the debtor with a right to cure default *twice* within any twelve-month period.¹⁴⁹ Thus, our hypothetical debtor, having cured default for the second time within twelve months, would lose his right to cure until one year after the first cure. If, at some time prior to that date, he is in default, the creditor's right to seek possession of the collateral accrues immediately. The right to cure itself never changes; that is, where the right to cure exists, the respective rights and obligations of the debtor and the creditor are unaffected by the number of times the debtor has previously cured.

In retrospect, the Wisconsin consumer representatives are unhappy with the result reached. They are consoled, however, by their belief that because the right to cure is difficult to lose, such an event should be rare.¹⁵⁰

The final cure-related issue, that of exceptions to the right, was resolved at second-stage negotiations.¹⁵¹ Creditors argued that special circumstances, such as where a creditor has a possessory security interest in securities that threaten to decline rapidly in value or where he believes that the debtor intends to conceal or remove collateral from the jurisdiction, may require a secured creditor to act quickly. They argued that prohibiting action that could prevent such losses was not in the interest of the paying consumer, who would ultimately shoulder the burden of the loss.

Consumer representatives were easily convinced that, when collateral in the hands of the debtor threatens to decline severely in value, it is in the interest of all parties to liquidate it. Consequently, an exception was created for this situation.¹⁵² For a number of reasons, however, consumer representatives were not willing to

149. Wisconsin Consumer Act § 425.105(3).

150. Since the great majority of defaults are due to events beyond the debtor's control, *see* COMMISSION REPORT, *supra* note 23, at 43, the number of defaulting debtors who get more than ten days behind on two payments and are then able to cure should be few. The number who do so repeatedly, yet in good faith, should be extraordinarily rare.

151. First-stage negotiations had not produced agreement, and A.B. 1057 as modified in December contained no exceptions to the right to cure, although a restraining order to protect collateral had been created. The banks continued to be involved in the negotiations, however, and played an important role in the resolution of this issue.

152. Wisconsin Consumer Act § 425.105(4).

create any further exceptions. First, they believed that creditors sometimes rely on the possibility of concealment or removal of collateral as an excuse for an otherwise unjustifiably quick repossession. They also believed that actual preventive repossessions were quite rare and that the over-all economic impact of prohibiting such repossessions would not be great. In addition, they had serious doubts about the reliability of most reports concerning removal in that these are normally received from neighbors, estranged spouses, and relatives, many of whom have axes to grind or are merely repeating gossip. Finally, consumer representatives had agreed at first-stage negotiations to allow a creditor to obtain a court order restraining a debtor from jeopardizing collateral. They believed that such an order, backed by the court's contempt power, would effectively stifle most potential skips and adequately protect creditors. As a result of these views, consumer representatives took a firm stand against any additional exceptions to the right to cure. Creditor representatives were unable to soften this position.¹⁵³

The ability of consumer representatives to withstand political pressure to limit drastically the right to cure is extremely significant, in my view, because this is the only point at which the WCA cure provisions force any substantial change in normal creditor operations. In general, a creditor will not repossess collateral soon after default unless there is some special reason for believing that he will not ultimately receive full payment. However, in these unusual circumstances the fifteen-day delay will force creditors to alter definitively their normal patterns. The impact of this change remains to be seen.¹⁵⁴

The cure procedure recommended by the National Commission is essentially the same as that in the WCA. The Commission also recommends that the repeatedly recalcitrant debtor lose his right to cure and suggests that he be allowed to cure only three times during the term of the contract.¹⁵⁵ Although it is not clear whether

153. See Wisconsin Consumer Act § 425.207.

154. One automobile finance company spokesman told me that quick repossession occurs most commonly after the creditor has spent a lot of time with the debtor trying to iron out the debtor's credit difficulties. If the creditor is skeptical about the debtor's good faith, any delinquency immediately after the discussions is likely to be met with immediate repossession. Consequently, the knowledge that quick action is prohibited might decrease the willingness of some creditors to work with a debtor whose credibility is marginal.

155. COMMISSION REPORT, *supra* note 23, at 25. The objective of any loss-of-cure formula is apparently to draw the line between the good faith debtor, who should be allowed to cure whenever he can, and the deadbeat, with whom the creditor should presumably be allowed to deal more harshly. No rationale is given for the Commission's choice of formulation, just as there really is none for the WCA choice, the latter

the Commission considered exceptions to the right, it recommends none.

Making nearly unanimous the view that *some* right to cure ought to be afforded to the consumer, the UCCC Redraft has added cure provisions.¹⁵⁶ However, the proposed consumer protection falls far short of that in either the WCA or the Commission Report. The UCCC Redraft provides a *once-per-transaction*, twenty-day cure period where the debtor is ten days delinquent on a scheduled payment.¹⁵⁷ Further, there is no right to cure defaults other than non-payment. The utility of such a limited right seems questionable.¹⁵⁸

3. Recovery of Collateral

Upon default the UCC allows the secured creditor to, among other things, take possession of the collateral without judicial process,¹⁵⁹ sell it, and apply the proceeds of the sale to the outstanding debt.¹⁶⁰ This ability to act quickly upon default assures the creditor that the collateral will have maximum value when repossessed and that his potential loss will be minimized. The efficient limitation of creditor losses clearly benefits the paying customer by increasing the availability of secured loans and reducing creditor overhead, which would otherwise be passed on to the consumer. In spite of these benefits, however, this summary procedure has come under serious constitutional attack. The attack, which stems from the landmark Supreme Court decision in *Sniadach v. Family Finance*

having been simply a matter of compromise. I doubt, however, if it really makes much difference, as long as more than one or two opportunities to cure during the contract are provided. See note 150 *supra*.

156. UNIFORM CONSUMER CREDIT CODE §§ 5.110, .111 (Working Redraft No. 4, 1972).

157. This, in effect, slightly modifies the definition of default. Until the debtor has once been afforded his right to cure the creditor may not take action prior to the tenth day of delinquency.

158. Its utility seems particularly questionable in light of the UCCC Redraft definition of default. When a single ten-day delinquency can result in loss of the right, there has hardly been a distinction drawn between the good faith debtor and the deadbeat. If the rationale is that the creditor is in a better position to draw this line than the legislature, why provide a right to cure at all?

The limitation of the right to nonpayment defaults also seems unjustified. If the default is failure to procure insurance or failure to assist in perfecting the security interest, especially if the default arises out of ignorance, why should the debtor not be given the opportunity to cure? Are these defaults somehow more material than non-payment? Perhaps certain kinds of nonmonetary defaults are more dangerous to the creditor's interests than delinquency in payment. If so, perhaps exceptions from the right to cure are justified in those circumstances. But the broad exclusion of all non-monetary defaults seems contrary to the objective of a right to cure.

159. UNIFORM COMMERCIAL CODE § 9-503.

160. UNIFORM COMMERCIAL CODE § 9-504.

*Corp.*¹⁶¹ and the more recent decision in *Fuentes v. Shevin*,¹⁶² centers upon the theory that the defaulting debtor, in being dispossessed of the collateral without notice or opportunity to object, is deprived of his property without the due process of the law guaranteed by the fourteenth amendment. The issue is now being litigated,¹⁶³ and its ultimate resolution is, as of this writing, uncertain.¹⁶⁴

A legislative dilemma, however, exists quite apart from the constitutional one.¹⁶⁵ Even if self-help repossession is constitutionally permissible, the legislature must still decide whether the admitted unfairness to at least the occasional debtor¹⁶⁶ can be significantly reduced through procedural safeguards, whether such safeguards can be constructed so as to have a minimal impact on creditor costs, and whether the increase in costs, to the extent it is inescapable, is justified by the amount of protection afforded the debtor.

The question of whether prejudgment self-help repossession would be available in Wisconsin was never really in issue during the WCA negotiations. In the eyes of consumer representatives, this was not a negotiable matter. They believed that, regardless of increased creditor costs, no debtor should be deprived of his property without having an opportunity to object. First-stage creditor representatives were particularly concerned about preventing the complete loss of self-help repossession. Therefore, they did not press

161. 395 U.S. 337 (1969).

162. 407 U.S. 67 (1972).

163. A number of courts have considered this question. White, *The Abolition of Self-Help Repossession: The Poor Pay Even More*, 1973 Wis. L. Rev. 503, 503 & n.1. In the one case in which the trial court found self-help repossession to be a denial of due process, the Court of Appeals for the Ninth Circuit reversed on the ground that there was no state action involved. *Adams v. Southern Cal. First Natl. Bank*, 42 U.S.L.W. 2230 (Oct. 4, 1973), *rev'd*, *Adams v. Egle*, 338 F. Supp. 614 (S.D. Cal. 1972). For discussions of the state action aspects of such cases, see Martin, *Secured Transactions*, 19 WAYNE L. REV. 593, 638-41 (1973); White, *supra*, at 504-10.

164. See generally Regenfass, *Self-Help Remedies After Fuentes v. Shevin*, 47 FLA. B.J. 155 (1973); White, *supra* note 163; Casenote, 8 LAND & WATER L. REV. 315 (1973).

165. Even if the Court balances the various interests and costs and decides, as suggested by Professor White, that there is no due process violation, see White, *supra* note 163, at 510-30, such a holding is not binding on state legislatures, which remain free to provide their citizens with more protection than is required by the federal Constitution.

166. Surely, the repossession of collateral where the debtor has a valid defense but no opportunity to assert it is an unfortunate occurrence. Not only is the individual injured, but general confidence in the law is undermined. One consumer representative told me that his legal aid clients invariably felt left out and that they perceived some form of conspiracy between the courts and the car dealers. He felt that the social cost of permitting prejudgment self-help repossession far exceeds the pecuniary cost of denying it.

for a prejudgment self-help remedy, but argued vigorously for the availability of self-help execution.¹⁶⁷

Original A.B. 1057 required the creditor who sought to repossess to file suit for possession. If the customer wished to object, he would have five days to file a demand for a hearing, which would be scheduled as soon as possible. If a "substantial question" as to the creditor's rights should appear, a final hearing would be held.¹⁶⁸ At no time, *either before or after* judgment for possession, was self-help repossession permitted.¹⁶⁹

At the outset, however, consumer representatives recognized that the elimination of postjudgment self-help repossession was an extension well beyond the limited requirements of *Sniadach*¹⁷⁰ and that employment of the sheriff to repossess collateral is slow and expensive. They were willing to permit self-help repossession after judgment if provisions that adequately inhibited violence could be drafted.¹⁷¹ At their urging, the WCA, by the end of first-stage negotiations, provided that, in self-help repossessions, the creditor could neither commit a breach of the peace nor enter a dwelling used by the customer as his residence.

The negotiators chose not to force the Wisconsin courts to devise strikingly new procedures, but rather decided to use the Wisconsin small claims courts as the forum¹⁷² for obtaining judgment for possession. Since the return date in small claims courts can be as early as eight days after mailing of process,¹⁷³ this forum provides a speedy resolution of the possession issue. The requirement that the debtor request a hearing was eliminated, so that the WCA simply

167. The banks presumed that a very small portion of defaulting debtors would actually appear and raise valid defenses. Thus, they assumed that once the return date passed, they would be in substantially the same position as under pre-WCA law.

168. A.B. 1057, § 425.208. See NATIONAL CONSUMER ACT § 5.208.

169. A.B. 1057, § 425.204. See NATIONAL CONSUMER ACT § 5.204. The MCCA contains a similar provision requiring judicial process in the repossession of collateral. MODEL CONSUMER CREDIT ACT § 7.202. However, the MCCA provides for the issuance of such process before judgment where necessary to obtain jurisdiction over the debtor or where the debtor "is about to remove the property from the state with the intent to defraud the creditor." MODEL CONSUMER CREDIT ACT § 7.205(3).

170. Cf. NATIONAL CONSUMER ACT § 5.208, Comment 1 (indicating that *Sniadach* supplies the primary rationale for the NCA approach).

171. Presumably, although there is no comment to this effect, the NCA rationale underlying the complete elimination of self-help repossession is that the likelihood of violence is decreased if the sheriff is always present.

172. Wisconsin Consumer Act § 425.205(1). Of course, the small claims court jurisdictional limit on amount in issue, WIS. STAT. § 299.01(3) (1971), was made inapplicable.

173. WIS. STAT. § 299.05(3) (1971).

provides that the debtor may appear on the return date and plead orally to the complaint.¹⁷⁴ The issue of possession is then decided; the two-stage hearing procedure set out in Original A.B. 1057 is eliminated.¹⁷⁵ The right to possession, however, is the only issue to be resolved;¹⁷⁶ if the creditor wishes a money judgment, for either damages or deficiency, a second action must be brought. Of course, once judgment is entered, the creditor may always choose to enlist the sheriff's aid in taking possession of the collateral.¹⁷⁷ The negotiators also recognized that unless the prejudgment repossession provisions and the right to cure provisions were related, an additional eight-day delay would be encountered while the creditor waited for the debtor's right to cure to expire. Since they saw no purpose in such a delay, the negotiators provided that the creditor may bring his action for possession at any time after default, but that the return day may not be set prior to the expiration of the cure period.¹⁷⁸

Once bank representatives accepted the abolition of prejudgment repossession, the negotiators worked together with very little conflict in the development of this procedure. Their mutual satisfaction with the result was undoubtedly the key to the fact that second-stage negotiators never seriously objected to the over-all scheme. Only two notable changes were made at the second stage, neither of which affected the general approach to repossession.

First, nearly all creditors were dissatisfied with the inability of the repossessing party to enter a dwelling. This requirement, they felt, would lead to the absurd result that household goods would have to be left out on the lawn before they could be repossessed. They argued that the UCC breach-of-the-peace restriction¹⁷⁹ effectively prevents violence, and that, even if it is not sufficient, the creditor should at least be able to enter a residence with the consent of the debtor. Consumer representatives, however, feared that the consent of the debtor might often be less than voluntary.¹⁸⁰ They were willing

174. Wisconsin Consumer Act § 425.205(1)(d).

175. See text accompanying note 168 *supra*. If at this hearing neither party is able to establish a right to possession, which is possible since neither party is likely to be prepared to discuss sophisticated legal or factual questions, the matter would undoubtedly be continued. In this instance, the WCA procedure would approximate that of Original A.B. 1057.

176. Wisconsin Consumer Act § 425.205(1)(e). For a severe criticism of this policy, see Heiser, *supra* note 27, at —.

177. Wisconsin Consumer Act § 425.205(5)(a).

178. Wisconsin Consumer Act § 425.205(6).

179. UNIFORM COMMERCIAL CODE § 9-503.

180. Consumer representatives believed that repossessors are often quite incon-

to back down only to the extent that the reposessor be allowed to enter a residence at the "voluntary request" of the customer.¹⁸¹ This solution did not truly satisfy many creditors, but consumer representatives were quite firm. They felt that once judgment is entered, most customers will peacefully give up the collateral.¹⁸² However, even if problems are created for creditors, consumer representatives felt that a reposessor should not be allowed to enter a dwelling under less than amicable circumstances unless a sheriff is present.

The second change was made primarily at the suggestion of consumer finance representatives and without much conflict. In the interest of reducing costs, a provision was added permitting the action for possession to be commenced by an officer or agent of the creditor even though such person may not be an attorney.¹⁸³

Barring unforeseen difficulties, the scheme worked out in Wisconsin should not have disastrous cost consequences.¹⁸⁴ First, obtaining judgment for possession need not, of itself, cause delay. Judgment may be obtained on the fifteenth day following notice of the right to cure, and collateral may be repossessed within the hour. Second, the costs of obtaining judgment, although hardly negligible, have been minimized, primarily by eliminating the need for an attorney. If the issue of possession can be settled at the hearing, as should normally be the case, the only cost increase will be that due to the added time spent by the employee in presenting the creditor's case. However, if the creditor has not received notice of the customer's defense,

siderate of the interests of the debtor. For a collection of repossession cases, see Hogan, *The Secured Party and Default Proceedings Under the UCC*, 47 MINN. L. REV. 205, 212 n.30 (1962).

181. Wisconsin Consumer Act § 425.206(2).

182. Where the customer has appeared to defend the action for possession and lost, this assumption is probably valid. However, having received notice of cure plus process regarding the action for possession will probably not soften very many debtors who would have otherwise objected to the reposessor's efforts. If these documents induce neither cure nor appearance at the hearing, they will probably just be added to the already large pile of notices the average debtor receives prior to repossession. Certainly, these documents should reduce the number of debtors who are surprised by repossession. However, I suspect that many uncooperative debtors are not at all surprised when the reposessor knocks at the door.

183. Wisconsin Consumer Act § 425.205(1)(a). Unfortunately, since this section provides only that the action "may be commenced by" such a person, it is not clear whether the person is authorized to take a default or, when the debtor disputes the issue, to argue the creditor's case. This uncertainty remains to be settled through litigation or regulation. Presumably, the section was intended to make creditor attorneys entirely optional in such proceedings, and I assume that that will be its effect.

184. Professor Johnson, in his extensive analysis of self-help automobile repossession in California, suggests that the costs of eliminating self-help repossession could be as much as 381 dollars per repossession. Johnson, *supra* note 122, at 34. However, his assumptions differ considerably from the circumstances under the WCA. See *id.* at 22.

he will most likely be unprepared to meet any claims beyond questions regarding default and cure. In this instance, the matter is likely to be continued and will probably necessitate the employment of an attorney. Costs are then likely to be considerable, but they are certainly justified.

The soundness of the legislative decision to eliminate prejudgment repossession turns on whether the increased costs are balanced by the societal benefit received. The benefit is simply a function of the number of debtors that will raise valid claims at the hearing on possession. If, for example, the cost of the average repossession is increased by thirty dollars and only one debtor in five hundred raises a valid claim, the decision made in the WCA will have been wrong. While it is, of course, impossible to place a dollar value on the prevention of an improper repossession, fifteen thousand dollars seems too high a price. On the other hand, if fifty valid defenses are raised in five hundred actions for possession, the choice made by the negotiators was probably correct. Not only will a substantial number of improper repossessions have been prevented, but the industry practices giving rise to valid defenses should begin to change as well.

There is a second, less significant factor to be considered in evaluating the legislative decision. If a substantial number of invalid defenses are raised, a possibility which has been suggested elsewhere,¹⁸⁵ perhaps the system should be altered. The societal benefit received when an invalid defense is raised is minimal. Yet, a substantial number of such claims could severely increase costs, particularly if the majority of these claims cannot be disposed of at the initial hearing. In my opinion, the probability that a meaningful number of debtors will raise valid defenses is not so small that reform should not be attempted. However, the longevity of these reforms should rest in the hands of consumers. If a miniscule proportion of valid defenses are raised, either creditor conduct is largely proper or the notice-and-opportunity protections are not working. In either case, consumer advocates should be open to revision of the procedures.

In contrast to the WCA, the UCCC suggests no limitations on the UCC repossession provisions. The Special Committee is apparently considering a change, although it has made no recommendation as yet. The UCCC Redraft states that sufficient time was not

185. See *id.* at 33. See also R. DOLPHIN, AN ANALYSIS OF ECONOMIC AND PERSONAL FACTORS LEADING TO CONSUMER BANKRUPTCY 90-92 (1965); Kripke, *supra* note 46, at 480-81 (discussing the story, "not often publicized by legal aid bureaus," of the existence of "real deadbeats").

available to attempt to resolve the adjustments that may be required by the evolving law following *Sniadach*.¹⁸⁶

The National Commission, on the other hand, suggests a procedure nearly identical to that found in the WCA.¹⁸⁷ With "full understanding" that substantial rate increases and severely curtailed credit availability are likely to occur, the Commission bases its recommendation on the concept "that an individual has the right to continued 'use and possession of property (free) from arbitrary encroachment.'" ¹⁸⁸ It suggests that "the right . . . to an opportunity to be heard must apply across the board, irrespective of the type of repossession—'self-help,' replevin, or whatever."¹⁸⁹

Although I may be guilty of oversimplification, the Commission does not appear to be concerned with the possibility of increased rates or decreased credit availability, nor with the proportion of debtors who would actually benefit from notice and an opportunity to be heard. Certainly *Fuentes* does not suggest that due process requires such absolute disregard for the interests of the typical, paying consumer.¹⁹⁰ Perhaps a presumption that the cost increase will not be unduly burdensome is implicit in the Commission's recommendation.

4. Some Reflections

The delay in the accrual of repossession rights and the requirement that a judgment be obtained before repossession may well be among the greatest cost-impact areas of the WCA. The National

186. UNIFORM CONSUMER CREDIT CODE, Prefatory Note, iv (Working Redraft No. 4, 1972).

187. In fact, the entire cure-repossession package recommended by the Commission is essentially the same as that of the WCA:

At the time the creditor sends notice of the cure period (14 days), and prior to actual repossession (whether by replevin with the aid of state officers or by self-help), he may simultaneously send notice of the underlying claim against the debtor, and the debtor should be afforded an opportunity to be heard in court on the merits of such claim. Such time period for an opportunity to be heard may run concurrently with the cure period.

COMMISSION REPORT, *supra* note 23, at 29. Moreover, the Commission's specific approval of the WCA summons as providing adequate notice of the pending claim suggests that the Commission may have been strongly influenced by the Wisconsin approach. See *id.* at 30.

188. *Id.* at 30, quoting *Fuentes v. Shevin*, 407 U.S. 67, 81 (1972).

189. *Id.* at 30.

190. Among the *Fuentes* Court's examples of circumstances in which notice and hearing may be postponed are those cases in which the individual's interest is outweighed by that of the public, such as seizures on behalf of the United States for the collection of taxes, 407 U.S. at 91-92, citing *Phillips v. Commissioner*, 283 U.S. 589 (1931), and preventing a bank failure, 407 U.S. at 92, citing *Fahey v. Mallonee*, 332 U.S. 245 (1946). See *White*, *supra* note 164, at 510.

Commission survey disclosed that "creditors thought the single most important remedy or contract provision in a secured consumer credit transaction was the right to take a security interest in the goods . . . and the concomitant right to repossess if the debtor defaulted."¹⁹¹ Although it was unable to predict the effects with any certainty, the Commission thought any restriction of these remedies would probably have a significant impact on rates and credit availability.¹⁹²

Prior to the WCA, the creditor was able to repossess a delinquent debtor's collateral as soon as he decided to do so. Under the WCA, the creditor must normally wait at least fifty-five days after the initial delinquency.¹⁹³ Moreover, the creditor must wait at least eight days to obtain judgment even if his decision to repossess is made after the cure period has run.¹⁹⁴ Therefore, the delays required by the WCA will run from a minimum of eight to as long as fifty-five days.

In the case of automobiles, which depreciate at a significant rate, any delay in obtaining possession after the decision to repossess results in losses. Data from four of the creditors consulted by Professor Johnson in his study of automobile repossessions in California showed that 73.8 per cent of new-car and 75.3 per cent of used-car repossessions occur within sixty days after default in payment, and 22.8 per cent of new-car and 17.7 per cent of used-car repossessions occur within thirty days of default in payment.¹⁹⁵ Professor Johnson also calculates the cost of delay, once the decision to repossess has been made, to be \$2.70/day for new cars and \$1.30/day for used cars.¹⁹⁶ If these California figures are applicable to Wisconsin, the

191. COMMISSION REPORT, *supra* note 23, at 29-30.

192. *Id.* at 30.

193. Presuming that the debtor's payments are due monthly and no default other than nonpayment occurs, there is no default until the debtor is forty days delinquent (ten days delinquent on the second unpaid installment). If notice of right to cure is sent immediately, and if the action for possession is filed within seven days of the notice, the return date may be set on the day that the cure period runs out—fifteen days following notice of right of cure. Hence, judgment for possession may be obtained fifty-five days after the due date of the first unpaid installment.

194. Of course, the creditor could file the action for possession before deciding to repossess, but this seems an unnecessary expense. See note 145 *supra* and accompanying text. It is not likely to become a common practice.

The eight-day minimum predicted here is probably conservative. It assumes that the action can be filed immediately and that there will be no delay in taking the default. The practical minimum will probably be more like ten to twelve days.

195. Johnson, *supra* note 122, at 6. Default here means the default that stimulated the repossession. This is rarely the first default. As suggested above, see note 154 *supra*, creditors often try to work out a new arrangement with a defaulting debtor before resorting to repossession. According to Professor Johnson, the national work-out to repossession ratio is 2.8/1. Johnson, *supra*, at 9.

196. Professor Johnson estimates the depreciation cost over thirty days to average \$57 for new cars and \$31 for used cars. Johnson, *supra* note 122, at 34. Further, he

minimum delay loss on a new car will be twenty-one dollars and more than twenty per cent of the new car repossessions (those delayed as much as twenty-five days) will result in losses in excess of sixty-five dollars per car.¹⁹⁷ Since five to ten per cent of all automobile contracts ultimately end in repossession,¹⁹⁸ the cost impact of the WCA provisions will be appreciable.

As mentioned above, one of the most seriously affected creditor groups, the manufacturer-affiliated automobile finance companies, did not participate in the WCA negotiations. Their absence was particularly significant in the drafting of the provisions that increase the costs of repossessing collateral. One negotiator told me that throughout these discussions there was a feeling that this was really "their issue" and that at any moment they would show up to present their point of view. They never did. It is impossible, of course, to determine precisely what modifications would have been made if the automobile finance companies had participated. Their interests were represented in many respects by the banks, which formed what was probably the most influential creditor group in the negotiations. On the other hand, the passage of the bill was always in doubt, and the automobile financiers could probably have exacted some meaningful concessions in exchange for their support. I doubt that they could have effected significant changes in the repossession procedure. The consumer representatives were adamant on the elimination of non-judicial repossession, and the procedure could not have been streamlined much more than it was. However, the automobile financiers might well have reduced the periods of delay in the accrual of repossession rights. Perhaps they could have obtained a more stringent definition of subsequent defaults—that is, default after having cured once or, perhaps, twice. Quite possibly they could have obtained

estimates opportunity cost—the cost due to the loss of the use of the funds the creditor would have received but for the delay—to average \$24 for new cars and \$8 for used cars for thirty days. *Id.* These totals work out to \$2.70 per day for new cars and \$1.30 per day for used cars. *But see* White, *supra* note 164, at 521 n.54, where Professor White suggests that these costs should be scaled down to monthly rates of \$68 for new cars and \$32 for used cars.

197. Of course, during the delay the creditor will continue his efforts to induce payment. He may well be aided in this effort by the WCA in that the creditor is now permitted to engage in the otherwise unconscionable collection practice of sending official looking documents and legal process to the debtor. *See* note 142 *supra*. Before this practice was generally banned, it was presumably effective. To the extent the debtor makes payment, and, hence, to the extent the creditor would otherwise have repossessed too early, all parties benefit. Reduction of such premature repossessions is, of course, the goal of consumer advocates. Moreover, to the extent that such repossessions are prevented, not only is unfairness decreased, but delay losses are reduced. It seems unlikely, however, that such gains would approximate the losses.

198. Johnson, *supra* note 122, at 13.

additional exigent-circumstance exceptions to the right to cure. At any rate, the absence of this substantial credit group was undoubtedly a significant factor in determining the ultimate scope of the WCA.

C. *Restrictions on Security Interests*

The case of *Willidms v. Walker-Thomas Furniture Co.*¹⁹⁹ is a classic, if not typical, example of how the unrestricted availability of consumer property as security can be abused. In that case the standardized conditional sales contract used by appellee retail furniture store contained an add-on security clause. As long as the customer maintained an account the outstanding balance of which had never been zero, any debt incurred by the purchase of goods on credit was secured by *all goods previously purchased* by that customer on credit. In 1962, the appellant, a long-time customer of the store, had reduced her balance to 164 dollars. She then purchased a \$15-dollar stereo and defaulted shortly thereafter. The store obtained a replevin judgment for all items purchased from it by the appellant since 1957. On grounds not solely related to the add-on clause, the appellate court held that the transaction could be found to be unconscionable.²⁰⁰

Rather than relying solely on unconscionability clauses, modern consumer-credit legislation usually contains specific restrictions on the taking of security interests. A key presumption running throughout such legislation is that there is nothing abusive about taking a purchase-money security interest, that is, a security interest in an item the purchase of which was facilitated by the extension of credit.²⁰¹ There is also substantial agreement among draftsmen concerning the treatment of security interests in credit sales. However, no such general agreement exists as to the restrictions applicable to security interests in loans.

The Wisconsin negotiations over restrictions on security interests

199. 350 F.2d 445 (D.C. Cir. 1965).

200. The court held that, in light of all the circumstances, the trial court could refuse to enforce the contract if it found it to be unconscionable under section 2-302 of the Uniform Commercial Code. Among the contributing circumstances, in addition to the oppressive security interest, were that the customer was on relief and supporting seven children on a monthly stipend of 218 dollars and that the customer's financial situation was well known to the salesman. 350 F.2d at 448.

201. Put another way, the risk of losing the item purchased can hardly outweigh the value of the credit that made its acquisition possible. Obviously, and less obliquely, if the customer needs a refrigerator, the risk of losing it to repossession cannot be so great that he should be prohibited from obtaining it. *But see* MODEL CONSUMER CREDIT ACT §§ 2.411(2)(b), .411(4)(a), discussed in notes 215-16 *infra*.

for the most part paralleled these general trends. However, they were quite complex because of the diverse interests involved; even a quite narrow prohibition on the taking of a particular type of collateral could have a crushing impact on businessmen who rely heavily on that type. Even though consumer advocates felt that the taking of excessive security interests could be a severe abuse, they were also aware that there was a real danger of being overprotective.

1. Credit Sales

The draftsmen of consumer-credit legislation generally agree that a retail seller or indirect sales financier should not be able to look to the general property of the debtor for security unless the goods sold or services rendered bear some special relationship to the property in which a security interest is to be taken. Presumably, this view is based on the theory that if the goods sold are not sufficiently valuable in themselves to secure the extension of credit, a customer whose personal creditworthiness cannot support the extension of credit ought not to make the purchase.²⁰² A special relationship is generally found where the goods sold or the services rendered are closely connected to the property taken and the debt secured is substantial,²⁰³ and in add-on sales.

Original A.B. 1057 provided that a close connection exists where the goods sold are installed upon or annexed to other goods or to land, or where land is maintained, repaired, or improved as a result of the sale of the goods or services.²⁰⁴ This formulation was satisfactory to all Wisconsin negotiators. Differences arose, however, as to when a debt is sufficiently substantial to justify a security interest in closely connected property.

Under Original A.B. 1057, a debt was sufficiently substantial, in the case of a security interest in realty, if it exceeded 3,000 dollars or, in the case of a security interest in goods, if it exceeded 500 dollars.²⁰⁵ First-stage negotiators were not overly concerned with this provision. Neither banks nor large retailers regularly take nonpur-

202. Examples of goods or services that have little value as collateral are cosmetics, books, dancing lessons, kitchenware, and health club memberships. Many of these are commonly the subject of door-to-door sales, which have received much attention of late. See Sher, *The "Cooling-Off" Period in Door-to-Door Sales*, 15 UCLA L. REV. 717, 721-24 (1968).

203. The "closely connected-substantial debt" terminology is taken from UNIFORM CONSUMER CREDIT CODE § 2-407, Comment 1.

204. A.B. 1057, § 422.416(5). See NATIONAL CONSUMER ACT § 2.416(5).

205. A.B. 1057, § 422.416(5). See NATIONAL CONSUMER ACT § 2.416(5). The MCCA retains these limits. See MODEL CONSUMER CREDIT ACT §§ 2.411(2)(c)-(d).

chase-money security interests in credit sales. However, banks occasionally buy home improvement paper, which is normally secured by an interest in the improved realty. Such transactions rarely exceed 3,000 dollars, and bank representatives warned that credit for smaller home improvements would be restricted if the creditor could not take a security interest in the house. The consumer representatives' view was that the customer should never be required to risk losing his home unless the creditor has facilitated a substantial improvement of the property. There was, however, no rational way to define a "substantial improvement." Convinced that many legitimate home improvement transactions would be restricted by the provision as it stood, consumer advocates agreed to reduce the obligation requirement from 3,000 dollars to 2,000 dollars.

At second-stage negotiations, savings and loan representatives and, of course, home-improvement concerns were adamant about a further reduction at least to 1,000 dollars.²⁰⁶ Consumer representatives were quite reluctant to reduce the requirement any further, feeling that a 1,000-dollar transaction would not necessarily result in a substantial improvement to the home. However, political considerations prevailed. Convinced that they must compromise to obtain the support of the savings and loan companies, consumer representatives agreed at the last minute to reduce the requirement to 1,000 dollars.

Although the issue was discussed, no negotiating group seriously argued for a reduction of the 500-dollar requirement for security interests in closely connected goods. One negotiator told me that the only transactions in the 300- to 500-dollar range that they felt might benefit other goods were substantial repair work on automobiles or boats. Although repairmen were not represented in negotiations, they are substantially protected by mechanics' lien laws.

The result reached in Wisconsin is very similar to the UCCC provisions. The only difference is that the UCCC requires only a 300-dollar debt²⁰⁷ (as compared to a 500-dollar debt²⁰⁸) before a security interest in closely connected goods is allowed. Both require a debt of 1,000 dollars in the case of a security interest in realty.²⁰⁹

The National Commission, on the other hand, appears to take a

206. To a lesser degree, consumer finance companies were also concerned, since they occasionally buy home-improvement paper.

207. UNIFORM CONSUMER CREDIT CODE § 2.407(1).

208. Wisconsin Consumer Act § 422.417(1)(b).

209. UNIFORM CONSUMER CREDIT CODE § 2.407(1); Wisconsin Consumer Act § 422.417(1)(c).

different view. While it is not entirely clear that the Commission considered the matter thoroughly or that it intended its recommendation to reach so far,²¹⁰ apparently it would never allow the seller to take a nonpurchase-money security interest. This recommendation seems much too facile, especially with regard to security interests in land. Notwithstanding the notorious practices of the home-improvement industry,²¹¹ a legitimate builder who significantly improves the value of the debtor's home should not be expected to rely solely on the debtor's credit rating.

The second special relationship in which the WCA allows non-purchase-money security interests in a credit sale is found in add-on sales—that is, where a seller has obtained a security interest in the property of the customer as a result of a prior credit sale and now wishes to secure a subsequent sale to the same customer with the previously obtained interest. In astounding unanimity, the WCA, the MCCA, the UCCC, and the National Commission all permit the seller to secure the second debt²¹² in this way—with certain restrictions to prevent the interminable piling-up of security interests found in *Williams*.²¹³ The matter was not a contested issue in Wisconsin.

210. The Commission simply states that “the creditor should not be allowed to take a security interest in goods or property of the debtor other than the goods or property which are the subject of the sale,” with the exception of add-on sales. COMMISSION REPORT, *supra* note 23, at 27. Perhaps the Commission does not consider one who renders service a seller, or it might consider the connected property to be part of the subject of the sale. At any rate, this short statement is not typical of the Commission Report in either its lack of clarity or its apparent oversimplification of the problem.

211. *See, e.g., Mathews v. Aluminum Acceptance Corp.*, 1 Mich. App. 570, 137 N.W.2d 280 (1965); *Burchett v. Allied Concord Financial Corp.*, 74 N.M. 575, 396 P.2d 186 (1964).

212. Wisconsin Consumer Act §§ 422.418(1)-(2); MODEL CONSUMER CREDIT ACT § 2.412 (1); UNIFORM CONSUMER CREDIT CODE § 2.408; COMMISSION REPORT, *supra* note 23, at 27. The only differences in approach are that the WCA and the MCCA allow add-on security interests only if the two obligations are consolidated into one, whereas the UCCC and the Commission Report contain no such requirement. Hence, the WCA to some extent coerces the consolidation of multiple obligations. It probably has little impact, however, since the WCA goes to great lengths to insure that consolidations do not result in greater expense to the customer, Wisconsin Consumer Act § 422.206, and the added expense to the creditor in consolidating the two obligations should be minimal. Nevertheless, such coercion seems unnecessary.

213. Payments received on the two debts are deemed to pay the finance charges first and then the prior debt. When the first debt is deemed to have been paid off in this manner, the prior security interests are terminated. For example, suppose a debtor has an existing obligation of 300 dollars, which is secured by a purchase-money interest in a refrigerator. If he then buys a stereo on credit from the same merchant, both obligations may be secured by both the refrigerator and the stereo. However, when the payments on both obligations total 300 dollars plus the finance charges, the security interest in the refrigerator is terminated. For a mild dissenting view regarding the soundness of this scheme, see Kripke, *supra* note 46, at 474-75.

2. Consumer Loans

The general philosophical agreement in the area of security interests in credit sales does not exist in the loan field; the WCA, the MCCA, the UCCC, and the National Commission take widely variant positions on this subject.

Original A.B. 1057 prohibited securing a consumer loan with a nonpurchase-money security interest in (1) real property, where the amount financed is 3,000 dollars or less;²¹⁴ (2) personal property, the fair market value of which exceeds one and one-half times the amount financed;²¹⁵ or (3) "household furnishings, appliances [or] clothing of the customer and his dependents."²¹⁶ At first-stage negotiations, the banks were concerned about the first two prohibitions. Initially, and without great difficulty, they convinced consumer representatives that the second limitation was unworkable and counterproductive. They argued that it would require an appraisal of the value of the would-be collateral and that the cost of this appraisal would be passed on to the customer. In addition, the banks maintained that this restriction would severely affect debt-consolidation loans, in which the creditor normally relies on all available collateral. Consumer representatives agreed to eliminate the second restriction chiefly because they believed that consumers often benefit from debt consolidation loans.²¹⁷

The negotiations concerning security interests in real property followed a pattern similar to that followed in the case of sales. Because a number of Milwaukee banks were in the practice of making loans for the construction of residential garages, bank representatives sought a reduction in the loan-size requirement. They pointed out that if the 3,000-dollar limit remained, banks would rarely be

214. A.B. 1057, § 422.416(3)(a). See NATIONAL CONSUMER ACT § 2.416(3)(a).

The MCCA has retained this restriction, adding the requirement that the credit be extended "for the purpose of the substantial improvement of the real property." MODEL CONSUMER CREDIT ACT § 2.411(2)(d).

215. A.B. 1057, § 422.416(3)(b). See NATIONAL CONSUMER ACT § 2.416(3)(b).

The MCCA has expanded this restriction by making it also applicable to purchase-money security interests and by adding a prohibition of security interests in "tools of the trade of the consumer not exceeding a fair market value of five hundred dollars . . ." MODEL CONSUMER CREDIT ACT § 2.411(4)(a).

216. A.B. 1057, § 422.416(2). NATIONAL CONSUMER ACT § 2.416(2).

The MCCA has expanded this restriction by prohibiting purchase-money as well as nonpurchase-money security interests and by adding "personal effects" to the list. MODEL CONSUMER CREDIT ACT § 2.411(2)(b). These provisions are applicable to all consumer-credit transactions.

217. For a suggestion that the provision is probably meaningless since few borrowers have personal property suitable for use as collateral, see Moo, *supra* note 15, at 453 n.69.

able to secure their loans. Yet, few customers would qualify for loans of the size needed to construct a garage if the loan could not be secured by the realty. Consumer representatives were again faced with a line-drawing problem arising from their belief that a debtor's realty should be substantially improved before he risks the loss of his home. Unable to establish that a debtor's realty could not be substantially improved for less than 3,000 dollars, they agreed, at the end of first-stage negotiations, to reduce the requirement to 2,000 dollars.

By far the most influential voice at second-stage negotiations on security interests in loans was that of the consumer finance companies. Since the great bulk of their business consists of direct consumer loans, the issue was critical to them. The finance companies, as well as the banks, were still dissatisfied with the 2,000-dollar loan-size requirement for security interests in realty. Both institutions make loans in the 1,300- to 1,500-dollar range that are secured by realty, and they were not anxious to change their practices. Another source of pressure came from the fact that the savings and loan associations and the banks sought a similar reduction in the case of credit sales. In light of their "substantial improvement" philosophy, consumer representatives would have been hard pressed to justify treating security interests in sales and loans differently. Consequently, they reluctantly agreed, as a result of the severe pressure from all sides, to further reduce the loan-size requirement to 1,000 dollars.²¹⁸

By comparison, the National Commission makes no recommendation as to restricting real property security interests on loans,²¹⁹ while the UCCC restricts security interests in real property on loans only where the finance charge exceeds eighteen per cent per year and the loan is 1,000 dollars or less.²²⁰ The rationale for restricting security interests on loans less severely than those on sales is far from clear. However, it doubtless depends on how the problem is perceived. Certainly, the sales and loans businesses are quite different from one another, and the most notoriously abusive practices have occurred in the case of sales. (There is no such thing as a high-pressure door-to-door lender.) However, the fact that the customer might lose his home as a result of a relatively small purchase is apparently seen as a danger from which the consumer should be protected. That

218. See Wisconsin Consumer Act § 422.417(3)(b).

219. Presumably, the Commission's silence on this issue is a recommendation that there be no such restrictions.

220. UNIFORM CONSUMER CREDIT CODE §§ 3.501(3), .510.

danger hardly seems to be decreased by the fact that the funds used to make the purchase were obtained from a direct lender or were obtained at a rate of eighteen per cent or less. Moreover, since direct lenders rarely take real property security on smaller loans, there is little likelihood that any important source of credit will be curtailed as a result of further restrictions.²²¹ Hence, there seems to be little justification for failing to restrict the few direct lenders who do engage in this practice.

The second major concern of the consumer finance companies regarding security interests on loans was the prohibition on taking household goods. The common practice of Wisconsin finance companies had been to secure many of their consumer loans by taking an interest in all of the household goods owned by the customer. Although they admittedly repossessed such collateral only in rare circumstances, the finance companies believed that taking such security interests significantly increases the debtor's incentive to repay the obligation. Hence, the prospect of the total unavailability of such collateral was a matter of great concern.

Consumer advocates were ambivalent, since this is an area where serious abuses are common, yet the danger of overprotection is particularly great. They strongly believed that special protection should be provided for those items truly necessary to a minimum standard of living;²²² since household furnishings and the like rarely have any significant resale value, they were not considered to be legitimate collateral. Consumer representatives realized, however, that some household goods do have significant resale value and saw no reason why the consumer should not be able to borrow against such property as long as his livelihood was not endangered. Eventually, the two groups were able to agree on a list of specific household necessities that were made unavailable to the direct lender unless the proceeds of the loan were used to purchase the items.²²³ Notably available

221. One might imagine a hypothetical debtor who is in dire need of 500 dollars and whose credit rating is such that he can only obtain such a sum by mortgaging his house. The Wisconsin restrictions on security interests on loans would certainly work to his disadvantage. However, I think this is likely to be a very rare case, and if it were to occur, the debtor, by putting up his house, could probably borrow 1,000 dollars and avoid the limitation.

222. Put more paternalistically, the debtor should not be allowed to risk loss of household necessities in order to obtain loans for the purchase of what is likely to be less essential property.

223. Wisconsin Consumer Act § 422.417(3)(c). The list includes clothing, dining table and chairs, refrigerator, heating stove, cooking stove, radio, beds, bedding, couch and chairs, cooking utensils, and kitchenware.

for use as collateral are televisions, stereos, freezers, washers, dryers, pianos, organs, antiques, boats, outboard motors, snowmobiles, and cars. Although some consumers may consider their television to be more important than their dining table, the adamant position taken by the finance company representatives forced the exclusion of items not essential to a most basic existence, especially when the item is likely to have significant resale value.

In retrospect, both consumer and finance company representatives seem content with the accord reached. While the debtor need not fear sleeping on the floor, the creditor may take a security interest in enough of the debtor's property to provide the psychological impetus considered so important by the finance companies.²²⁴

The National Commission, by way of contrast, apparently does not consider the use of household items as collateral to be a justifiable practice. Notwithstanding the heavy creditor reliance on such security interests in some cases, the Commission recommends that no creditor be allowed to take a nonpurchase-money security interest in household goods. Stating simply that the right, in the event of default, to repossess household goods has "far too disruptive an impact on the family life of the debtor to be in the public interest," the Commission makes no further distinction between necessities and nonnecessities.²²⁵

In my opinion, the Commission's position is too simplistic. While I would perhaps expand the WCA list of necessities,²²⁶ and while it is not entirely clear what the Commission would include in the category of household goods, it seems to me that the debtor should have the opportunity to decide how disruptive the loss of his piano or antique desk would be, and to weigh that risk against the value of a loan he might otherwise be unable to obtain. Also, the Commission's position is curious in light of its recommendations regarding realty. Whereas the consumer is not allowed to borrow 500 dollars against his piano, he can grant a mortgage on his house. Surely the disruption attendant to a foreclosure action would exceed that resulting from repossession of a piano.

224. One finance company representative told me that he thinks that the items available to the lender are the ones that the average debtor cares most about and are likely to provide more psychological impetus than the furniture or pots and pans.

225. COMMISSION REPORT, *supra* note 23, at 27.

226. Compare the items classified as necessities in a different context (prejudgment attachment) by the California supreme court: television sets, refrigerators, stoves, sewing machines, and furniture of all kinds. *Randone v. Appellate Dept. of the Super. Ct.*, 5 Cal. 3d 536, 560, 488 P.2d 13, 29, 96 Cal. Rptr. 709, 725 (1971).

D. *Restrictions on Deficiencies and Voluntary Surrender*

When the secured creditor repossesses and disposes of collateral, the sale price is typically well below the outstanding balance of the account. To the extent that the sale price is insufficient to cover the debt plus allowable costs, the customer normally remains obligated to the creditor. This obligation is termed a "deficiency," and the judgment thereon is a "deficiency judgment." Great controversy has raged of late as to whether and to what extent deficiencies in the consumer setting should be restricted. The matter was no less controversial in Wisconsin.

What, then, is wrong with allowing the creditor to collect consumer deficiencies? The theory underlying deficiencies is simple and has a good deal of appeal. The customer has undertaken an obligation that he ought to repay in full. If the proceeds from enforcing a security interest exceed the amount owed, the creditor must remit the excess to the debtor. By the same token, if the proceeds do not satisfy the obligation, the debtor should be required to make up the difference. The critical flaw in this analysis is that this fifty-fifty model is a mirage; the deficiency is the only result that in fact occurs.²²⁷ Very simply, the amount of the deficiency all too often seems unjustifiably large in light of the circumstances.²²⁸

Suppose, for example, that a debtor borrows 1,200 dollars to buy a stove, a refrigerator, and a living room set, the debt to be paid off in two years at a yearly interest rate of eighteen per cent. The initial balance, including finance charge, would be approximately 1,440 dollars, and the monthly payments, about 60 dollars. After making payments for eight months, the debtor would have reduced the balance to about 850 dollars after deducting a 110-dollar rebate for unearned interest. If the debtor then defaults, repossession would yield a deficiency of 500 dollars (assuming the resale value of the used goods to be 400 dollars and repossession and storage costs to be 50 dollars²²⁹). This surely would seem onerous to a debtor who has already paid 480 dollars and has an empty kitchen and living room.

227. In Professor Shuchman's study of eighty-three automobile repossessions in Connecticut, only one resale price exceeded the creditor's claim (including cost of sale) against the debtor. Shuchman, *Profit on Default: An Archival Study of Automobile Repossession and Resale*, 22 STAN. L. REV. 20, 62-65 (1969).

228. The deficiency judgment reached the zenith of its potential absurdity in *Imperial Discount Corp. v. Aiken*, 38 Misc. 2d 187, 238 N.Y.S.2d 269 (N.Y. City Ct. 1963). The customer bought an automobile battery for \$35.00, paid the debt down to \$11.75, and defaulted. When the dust cleared, he was without battery or car and faced with a deficiency of \$128.00. See generally Shuchman, *Profit on Default: An Archival Study of Automobile Repossession and Resale*, 22 STAN. L. REV. 20 (1969).

229. This figure is probably conservative. Compare *Imperial Discount Corp. v.*

Presuming that the initial sales price, the resale price, and the costs assessed were all fair, the size of the deficiency cannot be said to be the fault of either the debtor or the creditor. Rather, this situation seems unfair primarily because the creditor received so little for the nearly new goods.²³⁰ The unfairness is magnified where the repossessed collateral is sold for less than its fair market value, as is too often the case.²³¹ If the debtor originally paid an inflated price for the goods, the resale will cancel an even smaller portion of his obligation.

There are those who argue²³² for a complete return to the common law doctrine that the creditor not be allowed to look to both the debt and the collateral, but must elect one or the other.²³³ They apparently reason that deficiency judgments are generally so oppressive that they should not be permitted regardless of any adverse impact on costs or credit availability that might result from their prohibition. However, this approach ignores the possibility that collecting deficiencies might in some cases be reasonable. If so, the cost of eliminating those deficiencies should not be borne by the paying customer.

I should note that the complete elimination of deficiencies makes sense if the over-all creditor success in collecting deficiencies is minimal. In that case creditor resistance to eliminating deficiencies is just much ado about nothing, and efforts to define intricate limitations would not be worthwhile. However, based on the vigorous creditor opposition to restrictions on deficiencies, and on my own eclectic experience,²³⁴ I suspect that this is not the case. Although no definitive information is available,²³⁵ this suspicion is bolstered somewhat by Professor Shuchman. His excellent study of automobile deficiency judgments in Connecticut suggests that in over half of the deficiency judgments taken the creditor appears to collect.²³⁶ Of

Aiken, 38 Misc. 2d 187, 238 N.Y.S.2d 269 (N.Y. City Ct. 1963), where costs for repossession, storage, and sale of an automobile were 150 dollars.

230. Adding to the disillusionment of at least some debtors is the fact that over 25 per cent of the payments made by the debtor went to pay finance charges.

231. See text accompanying notes 261-63 *infra*.

232. See, e.g., Clark, *supra* note 14, at 339.

233. See 2 G. GILMORE, *supra* note 119, at 1185-88.

234. In information supplied by nine Wisconsin banks, the estimated pre-WCA success in collecting deficiencies ranged from 10 to 50 per cent, with most estimates falling into the 15 to 20 per cent range.

235. Perhaps some of the National Commission studies will be helpful.

236. Shuchman, *supra* note 228, at 38.

course, most of the time no deficiency judgment is sought,²³⁷ either because it is not necessary or because it is not worthwhile.

The two reforms generally proposed are that deficiencies on smaller obligations be prohibited and that the method of calculating deficiencies be altered. A third, and very volatile, issue is whether deficiencies arising from credit sales should be treated differently from those arising from consumer loans.

1. *Elimination of Deficiencies on Smaller Obligations*

Why eliminate deficiencies on smaller obligations?²³⁸ Where the value of the collateral is very small the objective is clear: If the cost of repossession, storage, and disposal is comparable to the sale price of the collateral, the repossession will not reduce the debt significantly.²³⁹ As long as the costs do not exceed the resale price, the creditor loses nothing, but the loss to the debtor may be significant. Although the creditor stands to gain little through repossession, he has a powerful coercive tool. Hence, where collateral has little resale value, repossession is primarily a means for harassment.²⁴⁰ Certainly, the law should not condone such conduct.

The water muddies, however, as the size of the obligations in which a deficiency is denied becomes larger. If the collateral is sold for its actual value and if its value is not eaten up by the costs, why should the creditor be forced to choose between the collateral and a money judgment? The answer to this question turns on a judgment regarding who should absorb the loss when the resale value of the goods is substantially less than the original purchase price.²⁴¹

If the burden of deficiencies is shifted to the creditor, the primary impact will probably be on the motor vehicle market. The vast majority of repossessions take place in this market because mo-

237. The National Commission study of deficiency suits in the District of Columbia showed that "there were only two deficiency suits for every nine repossessions." Johnson, *supra* note 122, at 43.

238. Advocates of this action are not entirely in accord on the rationale for eliminating such deficiencies. See Kripke, *supra* note 46, at 477.

239. See Jordan & Warren, *supra* note 46, at 441. For example, if the cost of repossessing, storing, and disposing of the debtor's refrigerator is 50 dollars and its sale brings only 75 dollars, the debt is reduced by only 25 dollars, and the debtor has lost his refrigerator. That the debtor could theoretically avoid this result by selling the collateral himself is no answer. First, the creditor would probably try to *prevent* the debtor from disposing of the collateral, and, second, as a practical matter, debtors in distress rarely take advantage of the steps available to them. See Shuchman, *supra* note 228, at 36-38 (74 of the 78 deficiency judgments studied were obtained by default).

240. See H. KRIPKE, *supra* note 7, at 297.

241. See Kripke, *supra* note 46, at 478. Of course, if the value of the goods has not dropped substantially, the election subjects the creditor to little hardship.

tor vehicles are the only common consumer personalty with any appreciable resale value. Professor Shuchman's study of eighty-three automobile deficiency suits showed that the average deficiency was approximately 600 dollars.²⁴² If his figures are typical of deficiencies where no suit is filed, and if creditors succeed in collecting fifteen per cent of their deficiencies,²⁴³ the complete prohibition of deficiencies could result in losses of roughly 90 dollars per repossession.

In order to reduce these losses, creditors could either avert deficiencies to the extent possible or increase interest rates and retail prices. But brisk competition between creditors and retailers in most states for the automobile dollar would tend to make price and rate increases a secondary creditor response. Instead, creditors would probably restrict the availability of credit to the higher risk customer. However, since even careful screening will never completely eliminate the need for deficiencies,²⁴⁴ price and rate increases are certainly possible.

If this analysis is correct, the impact of restricting deficiencies will be visited primarily on the high-risk automobile purchaser. He will be required to make a down payment sufficient to cover the initial depreciation, to buy a cheaper car, or, in markets where no down payment is required, to forgo the purchase entirely. This result is appealing in that the class of consumers sought to be protected—that is, the class most likely to default—is also the class that pays for most of the protection. On closer analysis, however, this is still a case of one person paying for the protection of another. Since no creditor can identify with certainty who will and who will not default, he must simply restrict credit to the customers that he considers most marginal. Within that group, some would have defaulted and some would not. To those customers who would otherwise have defaulted but do not because they bought a cheaper car, and to those who still default but without the possibility of a deficiency, the added protection is a boon. The price of that protection has been paid by the customer who would not have defaulted, but whose credit was restricted.

How can this benefit be weighed against this burden? With

242. The average net total claim was 1,416 dollars, and the average first resale price was 806 dollars. This results in an average deficiency of 610 dollars. Shuchman, *supra* note 228, at 62-65.

243. See note 234 *supra*.

244. The most common causes of default are loss of job, overextension, illness, and family break-up. COMMISSION REPORT, *supra* note 23, at 43. Most of these cannot be predicted at the time credit is extended.

certainty, it cannot; yet I am astonished at how many consumer advocates seem so certain that deficiencies should be restricted. Nevertheless, with some hesitation, I side with them for a number of reasons.

First, deficiencies are a tremendous burden on the individual—not only on the individual who pays, but on the individual who does not. The burden is not only financial; it is also emotional. Deficiencies nearly always seem unduly large to the customer; it is no help to tell him that the charges and resale price were legitimate. To be deluged for months by letters and phone calls demanding the payment of what seems to be an unjust debt is a severe drain.

Second, the argument, commonly made by creditors, that the party at fault should bear the burden is not appropriate. In most cases, the concept of fault has no place in a discussion of consumer default because the causes of default are largely out of the debtor's control.²⁴⁵

If deficiencies on smaller obligations are to be eliminated, two basic issues must be resolved: first, the obligation size below which deficiencies may not be collected, and second, whether to base this cutoff point on the size of the initial obligation or on the size of the obligation at the time of the default. A third issue, which was considered briefly in Wisconsin, is whether special consideration should be given to the portion of the original obligation that has been paid at the time of default.

Original A.B. 1057 provided that where the creditor repossesses, the customer is liable for the outstanding balance *only if* (a) the unpaid balance at the time of default is 2,000 dollars or more, and (b) the customer has paid less than one third of the deferred payment price.²⁴⁶ Since these provisions significantly affect automobile financing, the negotiations between bank and consumer representatives were arduous. In contrast, national retailers, who rarely repossess, were largely unconcerned.

245. The only common reason for default that is substantially within the debtor's control is overextension. See note 244 *supra*. However, this is also within the control of the creditor. Default due to overextension works to the detriment of everybody, yet its frequency indicates that neither debtors nor creditors have paid sufficient attention to the problem. Of course, to force creditors to be more concerned about overextension is to take away, to some extent, the debtor's ability to make his own decisions as to what he can and cannot afford. This is regrettable, but clearly too many debtors have been making poor decisions. In my view, some additional concern on the part of the credit community is not unwarranted.

246. A.B. 1057, § 425.211. The corresponding provision of the NCA (section 5.211) did not include the requirement that less than one third of the obligation have been paid. The MCCA would simply eliminate deficiencies altogether. See MODEL CONSUMER CREDIT ACT § 7.208(1).

According to the draftsmen of the NCA, the "major concern" of the legitimate creditor is the consumer who defaults on an early payment, leaving used collateral and a substantial unpaid balance.²⁴⁷ Apparently, the elimination of deficiencies where more than one third of the amount financed is paid reflected this concern. While creditor representatives were willing to discuss restrictions on creditors in areas of great consumer interest, the converse position, that creditor remedies be available only in areas of "major creditor concern," was totally unacceptable and even posed a threat to future negotiations. In addition, the banks argued that it would be irrational and arbitrary to allow a debtor to escape liability for a deficiency regardless of the obligation size once he has paid one third of the obligation. Consumer representatives relented rather quickly.

The true clash came on the questions of obligation size and cut-off point. In the hypothetical case discussed at the beginning of this section, the original amount financed was 1,200 dollars, and the balance, excluding interest, at the time of default was 850 dollars. If deficiencies were prohibited only where the *original obligation* was 1,000 dollars or less, the creditor would be allowed to collect this deficiency. However, if deficiencies were prohibited where the *obligation at the time of default* was 1,000 dollars or less, no deficiency would be allowed.

The banks were extremely unhappy that the cutoff under Original A.B. 1057 was based on the outstanding obligation at the time of default. All consumer accounts could fall within the provision, and on large accounts the creditor would not know whether he would be put to an election until the time of default. In addition, the banks vigorously insisted that the 2,000-dollar cutoff be reduced. They argued that forcing an election on accounts of that size went far beyond what was needed in light of the evil to be remedied. Moreover, and more important to the outcome of the negotiations, they took the position that too many of their accounts would be affected and that a reduction was essential if they were to support the bill.

Consumer representatives, on the other hand, disliked the prospect of reducing the cutoff size; yet, for practical reasons, they were willing to accede. However, they insisted on basing the cutoff on the balance at the time of default, as provided in the original bill. One of the most severe consumer criticisms of the UCCC had been its use of the original obligation size as the point of reference. Since the

247. See NATIONAL CONSUMER ACT § 5.211, Comment 1.

seller and the creditor can combine to control the cash price, the trade-in allowance, and finance and other charges,²⁴⁸ consumer representatives felt that the availability of a deficiency gave creditors too much control. Further, the banks' complaints about the uncertainty created by the provision did not convince the consumer representatives.

At the end of first-stage negotiations, a compromise was achieved, based, not on rational calculation, but on political necessity. The obligation-size cutoff was reduced to 1,500 dollars, and the basis for its determination remained the size of the obligation at the time of default. In addition, consumer representatives willingly agreed to add a provision making the customer liable in damages for wrongfully damaging or hiding the collateral.²⁴⁹

Second-stage negotiations yielded no change. However, this was one area in which the automobile finance companies influenced the WCA. On the floor of the Wisconsin senate they pushed through an amendment, which further reduced the obligation-size cutoff from 1,500 dollars to 1,000 dollars.²⁵⁰ The members of the consumer-credit coalition had agreed to stand behind the negotiated bill and oppose all amendments regardless of their individual interests. This was the only proposed amendment that they could not stop. One of the negotiators told me that he thought that the senate was simply "itching" to approve at least one amendment, and this turned out to be it.²⁵¹

If Professor Shuchman's data are typical of Wisconsin, the WCA will prohibit deficiencies on only thirty-eight per cent of the reposessions, and the average deficiency on these will be about two thirds of the over-all average deficiency.²⁵² Hence, Wisconsin creditors will lose only about twenty-five per cent of their pre-WCA deficiency recovery. The rough loss estimation of ninety dollars per repossession cited above for the entire denial of deficiencies then becomes twenty-two dollars.

In contrast to the WCA, both the UCCC and the UCCC Redraft eliminate deficiencies where the original cash price of the goods

248. See Shuchman, *supra* note 228, at 47.

249. See Wisconsin Consumer Act § 425.209(5).

250. The amendment as proposed would also have changed the cutoff basis to the initial sale price. However, this was averted by a last minute amendment to the amendment offered by one of the coalition members.

251. Conversation with John Holbrook, Milwaukee, February 1973.

252. Assuming that repossession costs in the cases studied by Shuchman were 100 dollars per car, the WCA would have denied deficiencies on 32 of the 88 claims studied. See Shuchman, *supra* note 228, at 62-65; Wisconsin Consumer Act § 425.209(2).

repossessed is 1,000 dollars or less.²⁵³ This provision will, of course, preclude deficiencies in far fewer repossessions²⁵⁴ than the WCA and will also allow the creditor to determine the availability of a deficiency in many cases. The intent of the UCCC Special Committee is apparently to protect debtors only in those cases in which the value of the collateral at the time of default is quite small and not to shift much of the burden of depreciation to the creditor.²⁵⁵

The National Commission, on the other hand, had no qualms about shifting this burden to the creditor. The Commission recommends eliminating deficiencies where the purchase, in sales, or the amount financed, in loans, is 1,765 dollars or less.²⁵⁶ Despite the probability that such a restriction will increase rates and reduce credit availability, the Commission believes that "implementation of that recommendation would afford consumers protection in areas particularly susceptible of abuse," that is, in repossessions of household goods and used cars.²⁵⁷

Regarding household goods, the Commission simply believes that too great a personal hardship would be caused if the creditor is allowed both the collateral and the deficiency.²⁵⁸ Although this does not seem to me to be a clear abuse, at least where the costs assessed are reasonable and a fair price is obtained for the collateral, the Commission believes that the burden created by the inevitably poor resale value of household goods ought to be spread throughout the community. I agree, chiefly because repossessions of household goods are rare and the impact of the limitation should be slight.

253. UNIFORM CONSUMER CREDIT CODE § 5.103(2); UNIFORM CONSUMER CREDIT CODE § 5.103(2) (Working Redraft No. 4, 1972). The Redraft changes the cutoff basis from "cash price" to "cash sale price." However, the impact of this change should not be great since there is no separate definition for "cash sale price," and the definition of "cash price" remains substantially the same. Compare UNIFORM CONSUMER CREDIT CODE § 2.110 with UNIFORM CONSUMER CREDIT CODE § 1.301 (Working Redraft No. 4, 1972). In an earlier draft, the UCCC based the cutoff on the amount financed. UNIFORM CONSUMER CREDIT CODE § 5.103(1) (Working Draft No. 6, 1967). This would have precluded deficiencies in more transactions than the present sale price formulation with which the Special Committee appears content. A still earlier draft, however, drew the line where the obligation at the time of repossession was 500 dollars or less, which would probably have permitted more deficiencies but would have eliminated creditor control. See Jordan & Warren, *A Proposed Uniform Code for Consumer Credit*, 8 B.C. IND. & COMM. L. REV. 441, 457-58 (1967).

254. Of the eighty-three cases studied by Professor Shuchman, deficiencies would have been prohibited in thirteen under the UCCC. Shuchman, *supra* note 228, at 62-65.

255. See Jordan & Warren, *supra* note 46, at 441 (emphasizing situations in which costs eat up the value of the collateral); Moo, *supra* note 15, at 452 (emphasizing the use of the threat of repossessing low-value collateral to coerce payment).

256. COMMISSION REPORT, *supra* note 23, at 29.

257. *Id.* at 30.

258. *Id.* at 31.

The Commission arrived at the figure of 1,765 dollars by identifying the point at which the used- and new-car markets are not in competition. Using a study of deficiencies in Washington, D.C., the Commission found abuses "peculiar to the used car market,"²⁵⁹ and calculated the cutoff figure accordingly. Since, at this writing, the studies underlying the Commission Report are not available, it is difficult to evaluate this conclusion.

2. Calculation of Deficiencies

The scuttlebutt has long been that repossessed cars are often sold for less than they appear to be worth. The reason, it is said, is that "repossessed cars are usually of below-average quality because a consumer is not motivated to invest in the maintenance of an asset he may shortly lose," and there is occasional "spite damage."²⁶⁰ Professor Shuchman's study indicates that repossessed cars are indeed usually sold at prices well below their apparent wholesale value, but not because they are worth less than wholesale.²⁶¹ He suggests, rather, that the low return on repossessed cars results from the economics of the present system, which provide "no incentive for the financier and little incentive for the dealer to resell the repossessed car at the highest price obtainable."²⁶² Rather, a pervasive system of backscratching exists among the majority of the automobile sales financiers and dealers.²⁶³ Clearly, to the extent consumers pay in deficiencies the differential between their cars' actual value and the resale price, the automobile sale-finance community receives added income. Equally clearly, those funds belong in consumer pockets.

In response to this problem, Original A.B. 1057 provided that the computation of the deficiency was to be based on the fair market value at the time of sale rather than the actual sale price of the

259. *Id.* at 30-31.

260. Johnson, *supra* note 122, at 15.

261. Shuchman used the *Redbook*, published by the National Automotive Publishers, to estimate the true value of repossessed cars. The *Redbook* is generally relied upon for accurate retail and wholesale automobile prices. See Shuchman, *supra* note 228, at 27 n.28. His data showed that the price of the first resale of repossessed cars (from creditor to retailer) averaged only 71 per cent of *Redbook* wholesale. By comparison, where dealers buy and sell at weekly wholesale auctions, he found that the average price is 93 per cent of *Redbook* wholesale. However, since the second resale of repossessed cars (dealer to consumer) averaged 92 per cent of *Redbook* retail, the extremely low first resale price cannot be attributed to the cars' poor condition. In addition, examination of about 20 repossessed cars revealed that all could be driven and all appeared in normal condition. Only two out of 150 cars were "junked" after repossession. *Id.* at 31-33.

262. *Id.* at 26.

263. *Id.* at 37-38.

collateral; published trade estimates of *retail* values were presumed to be fair market value.²⁶⁴ The banks were willing to accept the elimination of the actual-sale-price doctrine but strongly objected to the presumption of *retail* value. They argued that since they are not in the business of selling automobiles, they could never dispose of automobiles at that price. Nevertheless, consumer representatives held fast. The bill submitted to the legislature retained the presumption. However, the presumption did not survive. The legislature accepted an amendment that deleted it. Thus, the determination of fair market value is left entirely to the Wisconsin courts.²⁶⁵

Surely it is unrealistic to expect creditors to become retail automobile sellers, but it does seem entirely reasonable to expect the creditor to obtain a price comparable to the wholesale auction price. Professor Shuchman's data show that at the time of repossession the average *Redbook* retail value is 108 per cent of the average net total claim, and the average *Redbook* wholesale value is 77 per cent of the average claim.²⁶⁶ To calculate deficiencies based on *Redbook* retail figures would be tantamount, on the average, to denying a deficiency. Since the car is probably worth only 77 per cent of the claim to the creditor, a rule using retail value actually places the entire burden of motor vehicle depreciation on the creditor. It seems to me that, where this is the desired result, the legislature ought to disclose its purpose. The burden should be given to the creditor either in the form of a complete denial of deficiencies or not at all. Where deficiencies are available, the creditor should have to deduct only the price he can reasonably expect to obtain—the fair market wholesale value of the goods.

Unlike the WCA, the National Commission does not recommend a method of calculating deficiencies. Presumably, the Commission would solve the problem, at least in the used car market, by simply denying deficiencies altogether. However, a great number of cars are sold for prices in excess of 1,765 dollars, and I see no reason why, when these cars are repossessed, consumers should receive credit for less than fair market wholesale value.

3. *Special Treatment for Loans*

The deficiency restrictions in Original A.B. 1057 applied to all consumer-credit transactions,²⁶⁷ whereas the UCCG restrictions ap-

264. A.B. 1057, § 425.212. See NATIONAL CONSUMER ACT § 5.212.

265. See Wisconsin Consumer Act § 425.210.

266. Shuchman, *supra* note 228, at 32-33.

267. A.B. 1057, § 425.212. See NATIONAL CONSUMER ACT § 5.212.

ply only to credit sales.²⁶⁸ While the UCCC Redraft includes interlocking loans²⁶⁹ in its restrictions,²⁷⁰ the UCCC Special Committee otherwise adheres to its initial decision not to restrict deficiencies on loans. The National Commission, however, recommends only a minor distinction between sales and loans on the deficiency issue.²⁷¹

Although I have found no published explanation of the rationales underlying these widely variant approaches, it is evident that the solution again turns on one's perception of the problem. Examples of the potential oppressiveness of deficiencies always seem to involve the purchase of an item that is later repossessed. In contrast, when a direct lender forecloses on his nonpurchase-money security interest in all the debtor's home furnishings in order to reduce the debt by twenty-five dollars it is usually seen as an abusive taking of a security interest, rather than as a deficiency problem.²⁷² Arguably, then, it makes some sense to restrict deficiencies only in credit sales. Further, since a lender is generally permitted to take as much security as the debtor is willing to put up,²⁷³ restricting deficiencies in loans would simply encourage, to the extent it is available, the taking of more security than the lender would ordinarily require—hardly a desirable result from the consumer viewpoint.

On the other hand, if the debtor is to be relieved of the burden of the depreciation of consumer goods, whether they be cars, household items, or other goods, why should the mechanism by which credit is extended be relevant? Though the direct lender is not as involved in the sale as the indirect lender or the seller, the customer is no less disillusioned when the direct lender repossesses than when the seller does. Further, if the object of restricting deficiencies is to remedy the problem of the less-than-actual-value sale, it is not realistic to expect a bank, which may engage in both direct and in-

268. UNIFORM CONSUMER CREDIT CODE § 5.103(1).

269. For a discussion of the alternative definitions of "interlocking loans," see text accompanying notes 70-103 *supra*.

270. UNIFORM CONSUMER CREDIT CODE § 5.103(1) (Working Redraft No. 4, 1972).

271. COMMISSION REPORT, *supra* note 23, at 29. Slightly different treatment is recommended in the definition of the deficiency cutoff basis. For loans, no deficiency would be permitted if the *amount financed* is 1,765 dollars or less, whereas on credit sales, an *original sales price* of 1,765 dollars or less precludes a deficiency. If the customer makes a sufficiently large down payment in a credit sale of goods in excess of 1,765 dollars, the seller could escape these restrictions while extending credit in an amount less than 1,765 dollars. Consequently, deficiencies in consumer loan cases are somewhat more severely restricted than are those in credit sales.

272. See text accompanying notes 222-24 *supra*.

273. See text between notes 221-22 *supra*.

direct financing, to dispose of one repossessed good any differently from another merely on the basis of the way in which its purchase was financed.²⁷⁴

In Wisconsin, the issue was first raised by the banks. It had been their practice to make debt consolidation loans, some portion of which was normally secured. However, debtors who need these loans rarely own sufficient property to cover the entire loan. Consequently, they actually are made partly in reliance on collateral and partly in reliance on the debtor's creditworthiness. Bank representatives argued that such loans are beneficial to consumers and that their availability would be curtailed by the elimination of deficiencies with regard to them.

Very basically, consumer representatives believed that, since the majority of deficiencies go uncollected, very little consumer credit, except for cars, is truly collateral-based. They were largely unconvinced by creditor projections of decreased credit-availability. Therefore, as of the end of the first-stage negotiations, they were unwilling to create any exception for loans. But the banks were not ready to give up.

At the second stage, the consumer finance companies, the majority of whose business is direct loans, were greatly concerned by the prospect of loan restrictions resulting from abuses normally thought to arise out of credit sales. They vehemently insisted that consumer representatives identify their exact objectives in limiting deficiencies. Consumer representatives conceded that their primary concern—that is, the most glaring area of abuse—was the sale of repossessed collateral at a price below its actual value, especially when the sale is between financiers and retailers who have a continuing arrangement. Finance company representatives argued that such practices did not occur in the loan industry; in the rare circumstance where finance companies repossess they have every reason to seek the maximum price for the collateral. Restricting deficiencies on loans would only force finance companies to be more conservative in their lending policies with no correlative benefit to the consumer.

Under the combined pressure exerted by the banks and the finance companies, and in light of what they saw as their primary objectives, consumer representatives agreed, out of political necessity, to exempt noninterlocking loans from the WCA deficiency restrictions.²⁷⁵

274. Of course, as suggested above, this problem can be largely overcome by calculating deficiencies using fair market wholesale value.

275. See Wisconsin Consumer Act § 425.209(1).

This decision was clearly dictated by the political realities of the situation. Thus, there is no reason to expect it to be judicious, which, in my opinion, it is not. I agree that there is good reason for affording special treatment to some loans, but if deficiencies are to be restricted in credit sales, only the exemption of nonpurchase-money loans makes any sense. The fact that the direct lender, in making a purchase-money loan, may be less closely tied to the sale than the indirect lender does not seem to be significant. The rationale for restricting deficiencies is not that the lender is somehow culpable, but, simply as a matter of policy, that he seems better able to bear the burden of depreciation. In that respect the purchase-money lender and the sales financier are identical.

In comparison, nonpurchase-money collateral loans seem quite different. Where the debtor borrows against collateral he already owns, there is none of the rapid depreciation normally attendant to signing on the dotted line. The debtor is more likely to see the value of the collateral as being the amount that he could sell it for—which is always the creditor viewpoint—than the amount he paid for it—which, I suspect, is the debtor's view at the time of purchase. On repossession there is no burden of substantial depreciation to be allocated, and the amount of the deficiency does not appear unreasonably large.²⁷⁶ In my opinion, special treatment of nonpurchase-money loans is perfectly rational,²⁷⁷ and probably advisable. Otherwise, the decreased availability of such collateralized loans is likely to be balanced by only minimal consumer benefit.

There is at least one notable problem in prohibiting deficiencies only on purchase-money loans. It is common for lenders to make multipurpose loans where the proceeds are used partly to purchase goods and partly to consolidate prior debts, pay taxes, or finance a vacation. It is thus necessary to devise a scheme that denies a deficiency only with regard to the portion of the loan that went toward the purchase. Although some difficulty is unavoidable, the problem is not insurmountable.

While many satisfactory schemes might be devised, one method of allocation is to treat this situation in the way that security in-

276. As suggested above, this apparent unreasonableness is the core of the deficiency problem. Another factor vitiating the debtor's disillusionment is that, whereas in a credit sale the debtor receives goods on credit, in a nonpurchase-money loan, he receives money on credit. Consequently, in a loan transaction, the debtor is more likely to know that the creditor expects the debt to be repaid and that giving up the collateral may not be sufficient.

277. The Wisconsin banks were chiefly concerned about debt-consolidation loans. Naturally, when consumer representatives agreed to exclude loans completely, the banks were delighted.

terests in add-on sales are treated.²⁷⁸ For example, where a portion of the proceeds from a multipurpose loan is used to purchase goods in which a security interest is taken, the payments on the obligation would be deemed to be first applied to pay off that portion of the loan.²⁷⁹ If the goods are repossessed before that portion is deemed to be paid off and, in keeping with the WCA formulation, if the outstanding balance on that portion is 1,000 dollars or less, the entire obligation is reduced by the amount of that balance. That is, the creditor forfeits the difference between the balance on the purchase-money portion of the loan and the sale price of the repossessed collateral. This method treats the loan as two separate loans—one purchase-money loan and one nonpurchase-money loan. It would also be necessary to prohibit foreclosure on any nonpurchase-money security interests in satisfaction of the purchase-money part of the debt. To the extent that proceeds of the sale of such collateral exceeded the nonpurchase-money portion of the obligation, a rebate would be due the customer.

A final bothersome point with this method of allocation is the treatment of the security interest in goods that are deemed to be paid off. Termination of the security interest will disappoint the creditor, who is accustomed to relying on the security for the duration of the entire loan. Further, he could eliminate the problem by advancing the purchase money on Monday and then advancing the remainder on Wednesday, taking a second, nonpurchase-money security interest in the newly purchased item. Presumably, paying off the purchase-money loan would have no effect on the second security interest. Such loan-splitting gyrations should not be encouraged.²⁸⁰

Accordingly, I would be inclined, in keeping with the WCA restrictions on security interests,²⁸¹ to provide for the termination

278. See text accompanying notes 212-13 *supra*.

279. Of course, it would be possible, as suggested by Professor Kripke, to deem payments to be applied to this portion of the debt ratably in the ratio that this portion bears to the entire obligation. Kripke, *supra* note 46, at 474-75. This would work to the detriment of the creditor in that the possibility of being forced to an election would exist through the entire term of the loan. However, if the security interest in the goods terminates as that portion of the loan is deemed to be paid off, such a payment allocation would work to the detriment of the customer since the security interest would not terminate until the entire obligation was paid.

280. Because of the split rate provisions (18 per cent on the first 500 dollars, 12 per cent on the excess), the WCA explicitly prohibits loan splitting for the purpose of obtaining a higher rate. Wisconsin Consumer Act § 422.414. The creditor could avoid a violation here by charging only 12 per cent on the second loan. Clearly, however, encouraging the creditor to double his paperwork serves only to increase complexity and costs.

281. See text accompanying notes 222-23 *supra*.

when deemed paid of security interests in those household necessities in which no nonpurchase-money security interest can be taken and to allow the continuation of security interests in other property. Consequently, if the property is the type in which a nonpurchase-money security interest may be taken, an election to repossess would be required only until the property is deemed paid for, whereupon the property remains available as security for the nonpurchase-money portion of the loan.

4. *Voluntary Surrender*

Original A.B. 1057 provided, notwithstanding any waiver by the creditor of his security interest, that the customer had the right at any time voluntarily to surrender the collateral to the creditor, the effect of such surrender being the equivalent of repossession.²⁸² The creditor would thus be denied a deficiency if the outstanding balance at the time of surrender was below the deficiency cutoff point. This, in effect, gave the customer the power to make the creditor's election for him.²⁸³ The Wisconsin consumer representatives never intended to force creditors into such a clearly inequitable position and they agreed willingly to redraft the section.

Those who did the redrafting intended the provisions on enforcement of security interests to work generally as follows: The creditor would always be free to request the collateral. Having made his election, upon the return of the collateral the limitations on deficiencies would apply. However, if the customer surrendered with neither solicitation nor suggestion by the secured party—that is, if there was a so-called “voluntary surrender”—no deficiency limitations would apply.²⁸⁴ In effect, the provisions were intended to give the customer the right to avail himself of the creditor's means for disposition of collateral, while leaving the election between the debt and the collateral to the creditor. Although the draftsmen may not have achieved this objective,²⁸⁵ their reasoning was sound, and their objective, I think, correct.

282. A.B. 1057, § 425.205. See NATIONAL CONSUMER ACT § 5.205.

283. See Moo, *supra* note 15, at 453.

284. Holbrook & Bugge, *Creditor's Responsibilities and Duties Under the WCA*, 46 WIS. BAR BUL., Feb. 1973, at 37, 45.

285. Defining in terms of objective behavior the point at which the creditor has made the subjective election to resort to collateral proved quite difficult. The result was the following: “The surrender of collateral by a customer is not a voluntary surrender if it is made pursuant to a request or demand by the [creditor] for the surrender of the collateral, or if it is made pursuant to a threat, statement or notice by

The Commission Report does not touch upon the treatment of surrender; the UCCC and the UCCC Redraft take a different tack. By denying deficiencies only where the creditor repossesses or "voluntarily accepts surrender,"²⁸⁶ the UCCC presumably allows a creditor to avoid a forced election by refusing to accept surrender.²⁸⁷ Hence, under the UCCC the debtor cannot avail himself of the creditor's means of disposing of collateral. Although this does not appear to be a critical difference, the Wisconsin approach seems preferable. Occasionally an overburdened customer simply deposits the collateral on the creditor's doorstep. In such cases, the creditor should be encouraged to dispose of the collateral without having to refuse surrender in order to avoid losing his right to a deficiency.

IV. SUMMARY: WHAT HAPPENED IN WISCONSIN AND WHAT DOES IT MEAN FOR THE REST OF THE COUNTRY?

We have seen, in the context of some specific issues, the manner in which the negotiation and drafting of the WCA proceeded and the results of those efforts. We may now look more closely at the various factors that contributed to the creation of the WCA. An understanding of these factors may be helpful in predicting what to expect in other states.

the [creditor] that the [creditor] intends to take possession of the collateral." Wisconsin Consumer Act § 425.204(3).

Unfortunately, the "request or demand" formulation leaves open the question of what happens where the creditor simply notifies the debtor of his right to surrender. However, the administrator has cleared up this uncertainty. The creditor may notify the debtor of his right voluntarily to surrender without fear that such notification will amount to an election. WIS. ADMIN. CODE, BANKING § 80.69 (1973).

To add to the initial uncertainty, the automobile-finance-company-sponsored amendment, which reduced the deficiency cutoff point to 1,000 dollars, *see* text accompanying note 251 *supra*, was very poorly drafted. It left Wisconsin Consumer Act § 425.209(2) to read that the customer is not liable for the deficiency "[i]f the merchant repossesses or accepts voluntary surrender" This was certainly not the intent of anybody, including the sponsors of the amendment. The result is this: Where a customer voluntarily surrenders, section 425.209(2) eliminates customer liability for the deficiency and section 425.204(2) makes the customer liable for the deficiency. To add to the confusion, the "accepts voluntary surrender" language of section 425.209(2) implies that a creditor may refuse to accept voluntary surrender, whereas section 425.204(2) guarantees the customer the right so to surrender collateral. Clearly, the Wisconsin legislature has its work cut out.

286. UNIFORM CONSUMER CREDIT CODE § 5.103(2); UNIFORM CONSUMER CREDIT CODE §§ 5.103(2)-(4) (Working Redraft No. 4, 1972). Perhaps the draftsmen of the amendment discussed in note 285 *supra* intended to use this UCCC language. If so, the seemingly innocent transposition of "voluntarily accepts surrender" to "accepts voluntary surrender" caused a surprising amount of excitement and confusion. *See* note 285 *supra*.

287. The MCCA appears to have adopted this approach. The consumer is permitted to "offer to voluntarily surrender" the collateral, and the creditor is precluded from seeking judgment on the obligation if he "elects to accept the surrender." MODEL CONSUMER CREDIT ACT § 7.203(1).

A. *Significant Factors Influencing the Creation of the WCA*

Recall the setting in which the WCA came into being. In the summer of 1971, the Wisconsin banks, retail merchants, and consumer finance companies were all working toward the passage of special interest legislation. At the time, Original A.B. 1057 was sitting in the Wisconsin legislature with little likelihood of passage. By March 1972, the WCA had been negotiated, drafted, and passed. The critical factors were (1) the initial decision on the part of consumer forces to stop opposing rate increases in exchange for comprehensive consumer protection, (2) the forthright action taken by Governor Lucey, (3) the split in the credit community, (4) the unquestioned authority of the consumer negotiators to represent all consumer groups, (5) the personalities of the parties, (6) the fact that the framework of the negotiations was Original A.B. 1057, (7) the information upon which negotiators based their decisions, (8) the disparity in the resources available to consumer and creditor representatives, and (9) the nonparticipation of the automobile finance companies.

1. *The Decision To Trade Rate Increases for Other Benefits*

The paramount policy decision made by consumer advocates in entering into a coalition with creditors was that allowing increases in interest rates would be a worthwhile exchange for comprehensive consumer-credit protection. This decision, in my opinion, can neither be criticized nor applauded with any certainty because it requires the answer to an unanswerable question: To what extent should the paying consumer subsidize the protection of the nonpaying consumer? The consumer who has a secure source of income, maintains a sensible amount of debt, makes his payments on time, and never has trouble qualifying for credit is not greatly in need of protection. Granted, some of the protections of the WCA, such as disclosure requirements, the elimination of financier immunity from claims against sellers, regulation of consumer-approval transactions, and advertising restrictions, aid all consumers. However, most of the protections of the WCA, especially those with the greatest potential cost impact, apply to the consumer who has trouble meeting his payments. To the extent that his rates are increased, the paying consumer is bearing the cost of protections primarily intended for the benefit of others.

While the over-all question is indeed unanswerable, I think that at least a partial answer may be attempted: Regardless of the cost im-

pact, no creditor should be allowed to engage in practices that are patently unfair and oppressive. For example, even though the prohibition will increase costs (or reduce profits), no creditor should be allowed to sell repossessed collateral for less than its actual value and then pursue a deficiency on the basis of the sale price. Further examples of such egregious abuses are false advertising and oppressive collection practices. Beyond these fairly obvious instances, however, certainty evaporates.

Nevertheless, the decision in Wisconsin was not a difficult one for consumers because rate increases in Wisconsin were, in my opinion, inevitable. If national averages can be validly compared, 1971 rates in Wisconsin were low. At the twelve per cent rate, the profitability of bank and retailer revolving-credit plans was marginal, and these groups were moving quickly for relief. Moreover, the finance companies had already convinced the legislature that they needed an increase. It seems doubtful that consumers would have been able to resist these forces permanently. By allowing the inevitable to occur, consumer forces were able to obtain comprehensive protection at a very small cost. Of course, if consumer forces had staunchly opposed the creditor legislation, the rates might have increased to only fifteen, rather than eighteen, per cent. However, the decision made in Wisconsin can hardly be criticized on the basis of such speculation.

2. *The Role of the Governor*

Probably none of the factors influencing the creation of the WCA was more significant than the timely action of Wisconsin Governor Patrick J. Lucey. Prior to his decision to veto piecemeal, creditor-sponsored legislation, the consumer-finance company rate increase bill had nearly passed the legislature without its two-year time limitation. In addition, there were no foreseeable obstacles in the path of the bank and retailer legislation. By taking the position that he did, Governor Lucey forced the creditors to choose between doing without legislation they desired or accepting comprehensive legislation. In addition, by instructing the legislature to take up A.B. 1057, Governor Lucey greatly reduced any possibility that the comprehensive legislation would be based on the UCCC. By clearly placing his confidence in the proponents of A.B. 1057, the Governor, in substance, vested these individuals with the authority to speak for all consumer groups. Since each of these was a critical factor, the Governor had a tremendous impact on both the formation of the consumer-creditor coalition and on the direction of the negotiations.

3. *The Split in the Credit Community*

The position taken by the Governor set the stage for the split in the credit community. Only the banks, retailers, and consumer finance companies stood to gain by supporting comprehensive legislation. However, while they were certainly in an uncomfortable position, they were not helpless. Since consumers needed creditor support to obtain passage of comprehensive legislation, these creditors could certainly have forced a stalemate. Assuming that sympathy for consumer interests was not rapidly on the increase in the legislature, time was on the side of the creditors. The only creditors who were under any serious time pressure were the large retailers, primarily because of the possibility of continued liability for usury violations and the adverse publicity arising out of the *Penney* case. The banks and finance companies could probably have afforded to wait for rate increases. It seems to me, then, that if the entire credit community had refused to work within the framework of A.B. 1057, and if they offered to negotiate at least some substantial changes in Wisconsin law, the Governor might eventually have backed down to some extent. Creditor solidarity in Wisconsin could then have resulted in far weaker legislation.

The responsibility for the split, it seems to me, rests almost wholly with the banks. The national retailers are not nearly as influential in the Wisconsin credit community as are the Wisconsin banks. Although the support of the retailers at first-stage negotiations was helpful, the participation of the banks was the critical element.

Why did the Wisconsin banks participate? Certainly their interest in a rate increase was central to their decision. An additional factor, however, should not be underemphasized: The banks were not intimidated by the prospect of comprehensive consumer-credit legislation. They had the foresight to know that such legislation was, to some extent, inevitable and that the legitimate creditor has nothing to fear from such legislation if it is sensibly drafted and responsive to the interests of all affected groups. If agreement on sensible legislation could be reached, the banks saw that it would be the most direct route to the legislation they desired. Hence, they took the position that, if the proponents of Original A.B. 1057 were willing to negotiate substantial modifications in the bill, they would be willing to give their support.

Soon after the banks had begun serious negotiations with consumer representatives, the representatives of the retail merchants joined the discussions, and the first-stage coalition was formed. By

the end of first-stage negotiations, many of the most severe bank and retailer objections to Original A.B. 1057 had been resolved, and the negotiators had become confident that most of their remaining differences could be ironed out. With such influential creditors backing the bill, a number of other creditors, such as the credit unions, the savings and loan associations, and the farm-implement dealers, joined the bandwagon. Whereas six months previously it had appeared that these creditors would gain nothing by supporting A.B. 1057, the staunch support of the banks and retailers had changed matters considerably. Since A.B. 1057 now appeared to have a good chance of passage, new groups were willing to trade their support of the bill for concessions in their specific areas of interest.

From the standpoint of the coalition's strength, the most important creditor group to enter the second-stage negotiations was the consumer finance companies. While they were confident that with the help of the automobile finance companies they could block passage of the WCA, they realized that such action would make it difficult to obtain legislative approval for increases in interest rates. Moreover, many reputable consumer finance companies desired comprehensive legislation. They felt that many abuses in the consumer-credit field were unjustly attributed to the substantial consumer finance companies; supporting comprehensive reform could only enhance their reputation. Many consumer finance companies also saw consumer-credit reform as inevitable but believed that piecemeal legislation might suffer from overkill. Sensible comprehensive legislation seemed a better alternative.

Accordingly, the consumer finance companies supported the adoption of some form of the UCCC in Wisconsin. They held fast to this position until January 1972, primarily because of doubts that negotiations with the proponents of A.B. 1057 would be fruitful. Having seen the significant results of first-stage negotiations, most consumer credit companies joined the negotiations.²⁸⁸

4. The Unquestioned Authority of the Consumer Representatives

A common legislative problem in dealing with consumer representatives is that there are normally quite a few of them, each with his own ideas as to what consumers want. There was no such confusion in Wisconsin. Governor Lucey had, in substance, told credi-

288. Household Finance Corporation had long been a staunch supporter of national adoption of the UCCC. Hence, it opposed the WCA to the end. See note 45 *supra*.

tors that if they could come to terms with the proponents of A.B. 1057, he would support the result. Given this strong backing, the proponents of A.B. 1057 were in a position to be able to deliver the support of nearly all consumer groups. Rarely do consumer representatives have this kind of unquestioned authority. It was, in my opinion, critical both to the creditors' willingness to enter the coalition and to the consumer representatives' ability to negotiate effectively.

5. *Personalities*

As is probably always the case in such situations, personalities played an important role in the formation of the consumer-creditor coalition, especially at the very beginning of first-stage negotiations. All parties to the first-stage negotiations approached the negotiations with caution. Although the banks were in an uncomfortable position, they did not regard the prospect of continuing without a rate increase to be a total disaster. Hence, they were not to be pressured into supporting legislation, such as Original A.B. 1057, that would severely prejudice their interests. While the retailers may have felt a little more pressure than the banks, primarily because of their potential liability for usury violations, they too approached negotiations cautiously. Consumer representatives were similarly circumspect; they had no intention of supporting a watered-down package that did not substantially change existing Wisconsin law. Consequently, it was essential to the formation of any coalition that the representatives consider each other to be reasonable and sensitive to all legitimate interests. This is, of course, what happened.

The creditor representatives willingly agreed that in many instances consumers had suffered serious abuse and that in those cases sensibly drafted legislation was needed. Similarly, while consumer representatives felt that there was a great need for change, they hoped that change could be achieved through means that would have a minimal cost impact on the credit community; they were well aware that creditor costs would be passed on to the consumer to the extent possible. Although they shared the general objectives of the NCA, none of the Wisconsin consumer representatives had participated in the drafting of the NCA, so they were not personally committed to its specific provisions. They took the position that they would be willing to make sweeping changes if it could be rationally shown that A.B. 1057 was unworkable as written or that their objectives could be achieved through means more acceptable to the credit community. With the early development of mutual respect and the

mutual discovery that meaningful results were possible, serious first-stage negotiations began.

6. *Original A.B. 1057—the Framework for the Negotiations*

One of the most influential factors regarding the total content of the WCA is that the negotiations were based on Original A.B. 1057, rather than on the UCCC. As a result, the creditors were always in the position of arguing for change, and the consumer representatives were in the position of resisting change. Clearly, the consumer representatives had inertia on their side.

In addition, a negotiator has only a finite amount of influence, which is dissipated to some extent with every concession he receives. Hence, creditor representatives were forced to marshal their "influence points" and expend them only on the matters most critical to their interests. The result was that many original provisions remained unchanged or only slightly changed, not because creditor representatives were unconcerned about them, but simply because creditors were more concerned with other matters. Probably the best example of this phenomenon is the WCA penalty structure. The WCA provides remedies and penalties in varying degrees for violations of its provisions. In many cases, substantial penalties are imposed for what many creditors consider to be relatively harmless violations.²⁸⁹ Yet, due to the concern with other areas of the bill, creditor representatives never objected to the penalty structure.

289. This is true, for example, of restrictions on debt collection practices. For example, Wisconsin Consumer Act § 407.104 provides:

(1) In attempting to collect an alleged debt arising from a consumer credit transaction, a debt collector shall not:

...

(f) Disclose or threaten to disclose information concerning the existence of a debt known to be reasonably disputed by the customer without disclosing the fact that the customer disputes the debt;

...

(j) Claim, or attempt or threaten to enforce a right with knowledge or reason to know that the right does not exist;

...

(l) Threaten action against the customer unless the action is taken in regular course or is intended with respect to the particular debt.

Violation of this section subjects the creditor to the greater of (1) twice the finance charge involved in the transaction (but not less than 100 dollars or more than 1000 dollars) or (2) actual damages sustained by the customer. Wisconsin Consumer Act § 425.304. "Actual damages may include mental anguish with or without accompanying physical injury." Wisconsin Consumer Act § 427.105(1). See generally Holbrook & Bugge, *supra* note 284, at 46.

Similarly, the inclusion of an unenforceable confession of judgment clause in a consumer contract renders the entire transaction void, and the customer is entitled to retain the proceeds of the transaction without obligation. Wisconsin Consumer Act §§ 422.405, 425.305.

While the fact that negotiations were based on Original A.B. 1057 affected all creditors, its impact was greatest on those creditors with the least influence in the negotiations. Thus, while it probably did not severely affect the banks, its impact was undoubtedly felt by door-to-door sellers, independent furniture dealers, debt collectors, and the automobile finance companies.

7. How the Negotiators Made Their Decisions

One factor that is probably critical to the outcome of any negotiations is the manner in which negotiators determine what their clients want: When faced with a decision between two alternatives, how is the choice made? The creditor representative has no serious problem here. He knows his client well, his client's interests are normally clear, and he can consult with his client if the need arises. Representing consumers, however, is a far different matter. The client is unmanageably large, impossible to communicate with in any meaningful sense, and has widely varying, often contradictory, interests.

The process through which the Wisconsin consumer representatives made their decisions was very similar to the procedure I have followed in analyzing their work product: They first tried to identify what the problem was, they thought about the alternative solutions, and they made some substantial guesses. Of course, identifying the problem was the critical step. Here, the Wisconsin consumer representatives relied heavily on personal experience, obtained primarily through work in legal aid clinics. Since reliable empirical information is rarely available, personal experience with the problems of the poor was probably as good a basis on which to rely as any. Moreover, since most of the provisions of the WCA are aimed at alleviating the problems of the poor, the Wisconsin consumer representatives were probably as well-equipped as anyone could be to identify accurately the problems most in need of attention.

Regarding the problems of the middle class, however—and this includes the vast majority of automobile buyers—the Wisconsin consumer representatives had no particular expertise. In fact, considering the general dearth of empirical data in this area, no one may have the necessary expertise. At any rate, the Wisconsin consumer representatives were forced to make their choices on the basis of common sense, hearsay, and the scant empirical research of others. They were often forced to guess at answers to such questions as:

How many consumers will benefit from a right to cure? How many will benefit from notice and opportunity to object to repossession? In these areas I believe there is the greatest likelihood that the WCA has struck an improper balance. I should emphasize that I have no serious criticism of the choices made in Wisconsin: The answers are just as elusive to me as they were to the Wisconsin negotiators. However, the decisions made in this area were critical to the ultimate shaping of the WCA. Consequently, since they were largely based on assumption, the impact of the WCA should be monitored particularly closely in this area, and all parties should be open to change if the benefits turn out to be miniscule in light of increased costs.

Creditors generally made their decisions on the basis of data from their own records. For example, in order to determine the possible impact of a particular deficiency cutoff point, creditors could look to their records to evaluate the prospective costs. The various alternatives could then be more rationally weighed. However, creditors also did some guessing, especially as to what impact various provisions would have on the average customer's attitude toward debt.

8. *The Disparity in Resources*

Whereas creditor representatives generally had an unlimited source of manpower available to them, the resources of the Wisconsin consumer representatives were very limited. On occasion, consumer representatives simply were unable to amass the information necessary to present a satisfactory argument for their point of view and were forced to back down. For example, when negotiators were faced with a difficult policy issue, creditors would often base their arguments on self-generated data. The limited consumer resources made it impossible to evaluate carefully such statistics or to generate contrasting data. Therefore, the Wisconsin consumer representatives were probably not as effective as they might otherwise have been.

9. *The Nonparticipation of Automobile Finance Companies*

As I have suggested at some length,²⁹⁰ the nonparticipation of the automobile finance companies in the negotiations may have been

290. See text accompanying notes 41-43 *supra*.

a significant factor, for they almost certainly could have exacted at least a few noteworthy consumer concessions in exchange for their support of the WCA.

B. *What the WCA Means for Other States*

The complex situation that occurred in Wisconsin is not likely to be duplicated in other states, so not all the factors critical to the creation of the WCA will be important elsewhere. Yet, there will undoubtedly be similarities between the problems facing consumers in other states and those that faced consumers in Wisconsin. For example, the passage of comprehensive consumer protection in nearly all states will presumably require at least some cooperation on the part of creditors. I doubt that in many state legislatures consumer sympathy runs so high that creditor forces can simply be overpowered.

A few basic lessons can be learned from the Wisconsin experience, some less surprising than others. First, unsurprisingly, a strong consumer political position is essential to the passage of far-reaching legislation. Second, and perhaps a little surprising to some, creditors are not monolithic. They have diverse, sometimes contradictory interests; they have different attitudes toward change; and they make their own decisions. Hence, they can be split. Third, the experience of the automobile finance companies suggests that if comprehensive legislation ultimately passes, those creditors who did not participate in its design will probably have made a mistake. Fourth, the existence of realistic consumer leaders capable of delivering the support of most consumer groups is essential to effective cooperation between consumers and creditors.

The political atmosphere in each state and the factors contributing to political influence generally are extremely diverse. It would hardly seem worthwhile to attempt here to predict the future of consumer political influence in other states. To be sure, consumer consciousness in the United States has increased significantly in the past few years. If this increase continues, sympathy for consumers in state legislatures is sure to follow. Yet, it is quite possible that awareness of consumer problems will prove to be a cyclical phenomenon and will soon begin to wane. If so, the WCA may be the national high-water mark in consumer-credit protection. In any event, it is not likely to have much significance for other states until consciousness

of consumer needs reaches substantial proportions. Once consumer forces within a particular state begin to gain strength, however, the WCA could and should influence the legislative process in a number of ways. It may, for instance, be the starting point for consumer-creditor negotiations. Since the WCA arose out of negotiations in which the competing parties enjoyed substantially equal bargaining positions, it already represents a great deal of compromise by both sides. Moreover, even if negotiations in other states do not begin with the WCA, it still provides an excellent reference.

If consumer strength reaches the point where some change is imminent, the Wisconsin experience should soften creditor resistance to change. Many creditors fear that substantial change will have disastrous effects. They fear that far-reaching legislation will not only complicate their operations, but also undermine the customer's attitude toward debt. A creditor who envisions such a calamity, whether his fears are founded or unfounded, is not likely to support change. The broad creditor support ultimately enjoyed by the WCA shows that many Wisconsin creditors were eventually convinced they could live with the WCA. Moreover, if after a few years under the WCA the Wisconsin consumer-credit community is alive and well, general creditor apprehension of impending doom should begin to subside.

The WCA should soften creditor resistance to change in another way—through the example of what happened to the automobile finance companies. Once change is imminent, it is clearly to the advantage of the creditor to participate in the negotiations. No draftsman can be expected to foresee all the likely effects of a particular restriction. The realistic consumer representative wants to know, to the extent possible, how the proposed legislation will affect the creditors in his state.

Perhaps the WCA may influence the legislative process in other states most significantly by illustrating what can be accomplished by capable, open, and cohesive consumer forces. Even if consumer awareness runs high in the state, and even if a few influential creditors are willing to negotiate, meaningful results are not likely if consumer forces are fragmented or if consumer representatives do not realistically view the functional relationship between consumers and creditors. Consumer representatives must realize that what is bad for creditors is not necessarily good for consumers. No creditor will be willing to cooperate with consumer representatives who, as is often the case, do not understand this. Equally important, if not

more so, no creditor will be willing to cooperate with representatives of only a few of the consumer groups within the state. To expend a large amount of energy reaching an accord with one consumer representative makes little sense if the result is opposed by other consumer groups.

Accordingly, if the WCA induces consumer forces in other states to unite under capable leadership, it will indeed have a meaningful impact outside Wisconsin.