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## THE REVISED UNIFORM CONSUMER CREDIT CODE AS A REPLACEMENT FOR PIECEMEAL CONSUMER LEGISLATION: THE ARIZONA CONTEXT

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In 1968 the National Conference of Commissioners on Uniform State Laws approved the final draft of the Uniform Consumer Credit Code [U3C] and recommended it to the states for enactment.<sup>1</sup> It was the commissioners' goal to deal with the wide range of abuses associated with the expansion of consumer credit<sup>2</sup> by bringing virtually the entire consumer process from advertising to collection within one comprehensive statute.<sup>3</sup> Although the U3C was significant as an attempt to meet a pressing need caused by state legislatures' piecemeal response to or outright neglect of consumer problems,<sup>4</sup> as originally proposed it was distinctly creditor-oriented.<sup>5</sup> Consequently there was a legitimate con-

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1. UNIFORM CONSUMER CREDIT CODE, Historical Note (1968 version) [hereinafter cited as U3C (1968)].

2. See Jordan & Warren, *The Uniform Consumer Credit Code*, 68 COLUM. L. REV. 387, 387-88 (1968); Kripke, *Consumer Credit Regulations: A Creditor-Oriented Viewpoint*, 68 COLUM. L. REV. 445 (1968).

3. See Jordan & Warren, *supra* note 2; Miller & Warren, *A Report on the Revision of the Uniform Consumer Credit Code*, 27 OKLA. L. REV. 1, 1-2 (1974).

4. See CONSUMER CREDIT IN THE UNITED STATES: REPORT OF THE NATIONAL COMMISSION ON CONSUMER FINANCE 3 (1972) [hereinafter cited as NCCF REPORT]; Boyd, *Representing Consumers—The Uniform Commercial Code and Beyond*, 9 ARIZ. L. REV. 372, 372-74 (1968).

5. See Boyd & Balentine, *Arizona's Consumer Legislation: Winning the Battle But . . .*, 14 ARIZ. L. REV. 627, 628 (1972); LoPucki, *The Uniform Consumer Credit Code: Consumer's Code or Lender's Code?*, 22 U. FLA. L. REV. 335 (1970); Willier, *A Uniform Consumer Creditor's Code*, 54 MASS. L.Q. 53 (1969).

cern that using the U3C to fill the legal void would be detrimental to consumer interests,<sup>6</sup> and the original draft met with relatively limited success by way of adoption.<sup>7</sup> The commissioners and the U3C's drafters were sensitive to these criticisms,<sup>8</sup> particularly the publication of a report by the National Commission on Consumer Finance<sup>9</sup> reinforcing many of the earlier criticisms,<sup>10</sup> and consequently they are now offering a revised text for adoption.<sup>11</sup> It is likely that the revised text will be considered sooner or later by the Arizona legislature.<sup>12</sup> The purpose of this Article, therefore, is to review and evaluate the revised U3C and make recommendations regarding its adoption in Arizona. Special attention will be given to existent Arizona consumer legislation and the criticisms leading to the rejection of the original U3C in Arizona. Of course, Arizona's situation is not unique, and much of the discussion will be relevant to consideration of the revised U3C in other jurisdictions as well. It will be convenient to consider the revisions essentially in the order presented in the prefatory note to the revised text.<sup>13</sup>

## THE PRICE OF CREDIT

### *Statutory Control of Finance Charges*

The price of credit, meaning rates of interest and finance charge, is of course a crucial matter, and has prompted pressure from both

6. See, e.g., CONSUMER VIEWPOINTS: CRITIQUE OF THE UNIFORM CONSUMER CREDIT CODE (R. Elbrecht ed. 1971) [hereinafter cited as CONSUMER VIEWPOINTS]; CONSUMER'S ADVISORY COUNCIL, [N.Y.] DEPT OF CONSUMER AFFAIRS, REPORT ON THE UNIFORM CONSUMER CREDIT CODE (1969); LoPucki, *supra* note 5; Willier, *supra* note 5.

7. By 1972, only six states had adopted the Uniform Consumer Credit Code [U3C]: Colorado, Idaho, Indiana, Oklahoma, Utah, and Wyoming. See 1 CCH CONSUMER CREDIT GUIDE ¶ 4770 (1975). Kansas adopted a substantially revised version of the U3C in 1973. KAN. STAT. ANN. §§ 16a-1-101 to -9-102 (1974). Iowa and Maine followed suit in 1974. See UNIFORM CONSUMER CREDIT CODE, Prefatory Note, at 86 (1974 version) (Cum. Supp. 1976) [hereinafter cited as U3C (1974)].

The U3C was introduced in Arizona on Feb. 18, 1969, as part of Senate Bill 161, S. 161, 29th Ariz. Legis., 1st Sess. (1969); see Boyd & Balentine, *supra* note 5, at 628, but failed to be enacted. See Boyd, *The UCCC and the NCA: A Comment and Comparison*, in CONSUMER VIEWPOINTS, *supra* note 6, at 663.

8. Unpublished memorandum prepared by Professor William D. Warren (principal drafter of the U3C) (1971), on file in the *Arizona Law Review* office; see U3C, Prefatory Note, at 87 (1974).

9. The National Commission on Consumer Finance is a federally sponsored commission authorized under the Consumer Credit Protection Act [Truth-in-Lending Act], 15 U.S.C. §§ 1601-1681t (1970), as amended, (Supp. IV, 1974), to "study and appraise the functioning and structure of the consumer finance industry, as well as consumer credit transactions generally." Consumer Credit Protection Act, Pub. L. 90-321, §§ 401-407, 82 Stat. 164-66, as amended, Pub. L. 91-344, § 404(b), 84 Stat. 440.

10. NCCF REPORT, *supra* note 3, at xix-xxv, xxviii-xxix; see U3C, Prefatory Note, at 87 (1974).

11. See U3C (1974).

12. The Arizona legislature has not been inactive in the consumer protection field. A number of laws ostensibly aimed at aiding consumers have been enacted. See Boyd & Balentine, *supra* note 5. The pressure for further action, particularly from the federal government, may be expected to continue and even intensify. See NCCF REPORT, *supra* note 4, at 1-4; proposed Federal Trade Comm'n Reg. §§ 444.1-2, 40 Fed. Reg. 16347 (1975) [hereinafter cited as FTC Credit Practices Rule].

13. See Miller & Warren, *supra* note 3.

debtors and creditors for special legislation governing rates.<sup>14</sup> The resulting hodgepodge of legislation has imposed more or less specific rates for various loan or sales transactions.<sup>15</sup> The original U3C, in contrast, was premised on the theory that free competition could control the price of credit more effectively than superimposed rate structures.<sup>16</sup> Accordingly, the original text chose to eschew rate controls in favor of rate ceilings and free competition.<sup>17</sup> The ceilings, so the argument went, would prevent the "gouging" that results when competitive forces break down while relying on competition as the basic regulation.<sup>18</sup>

The U3C's scheme of price ceilings was criticized for basically two reasons. One objection reflected skepticism regarding the existence of effective competition in the credit market.<sup>19</sup> Another was the related fear that, in practice, price ceilings would become "floors," with rates rising to the maximum levels permitted.<sup>20</sup> As an alternative to the ceiling system, it was suggested that a thorough study of the cost of credit in the various markets be conducted and specific rates reflecting those costs be imposed.<sup>21</sup> No such study has been made, however, and

14. In the absence of special legislation, the maximum interest rates that may be applied to credit transactions are governed by usury laws. See ARIZ. REV. STAT. ANN. §§ 44-1201 to -1202 (Supp. 1975-76); Lowell, *A Current Analysis of the Usury Law: A National View*, 8 SAN DIEGO L. REV. 193 (1971). Due to statutory exemptions and unrealistic rates, however, these laws have proven inappropriate in the context of modern consumer credit financing. See, e.g., U3C, Prefatory Note, at 87 (1974); 69 MICH. L. REV. 1368, 1370-73 (1971); 55 MINN. L. REV. 1244, 1245-47 (1971); 1971 WIS. L. REV. 296, 299-301. The result has been enactment of special laws to govern small loans, see ARIZ. REV. STAT. ANN. §§ 6-601 to -640 (1974), and creation of the "time-price" exception in the area of credit sales. See Boyd, *supra* note 4, at 389; Note, *Service Charges for Revolving Charge Accounts: A Time-Price Exemption or Usury?*, 71 COLUM. L. REV. 905, 906-12 (1971). Under the time-price doctrine, the difference between the time (credit) price and cash price of goods sold on credit is not considered interest and hence is outside the usury laws. See, e.g., Boyd & Balentine, *supra* note 5, at 642 & n.105; Kripke, *supra* note 2, at 452-54; Note, *supra* at 907-08. Consequently, in the absence of special legislation, charges imposed in time sales transactions are not set by law. Consumer-debtor pressure for reform, however, has led to successful attacks on the application of the doctrine. See Boyd & Balentine, *supra* at 643 & n.106. These attacks in turn have led creditors to seek legitimatization by special legislation of the rates presently charged. See *id.* at 643 & n.107.

15. See B. CURRAN, TRENDS IN CONSUMER CREDIT LEGISLATION 15-130 (1965).

16. See U3C, Prefatory Note, at 87 (1974); Jordan & Warren, *supra* note 2, at 394-96.

17. See U3C, Prefatory Note, at 87-88 (1974); Johnson, *The New Law of Finance Charges: Disclosure, Freedom of Entry, and Rate Ceilings*, 33 LAW & CONTEMP. PROB. 671, 683-85 (1968); Jordan & Warren, *supra* note 2, at 388-92.

18. Cf. Jordan & Warren, *supra* note 2, at 390. But see *id.*, at 393-95 (arguing that in fact ceilings offer only limited protection for the consumer, while arbitrarily excluding from the market high-risk consumers to whom credit can profitably be made available only at high interest rates).

19. See, e.g., NCCF REPORT, *supra* note 4, at 147; Boyd, *supra* note 7, at 665; Willier, *supra* note 5, at 53-55; Comment, *An Analysis of the Uniform Consumer Credit Code and the National Consumer Act*, 12 B.C. IND. & COM. L. REV. 889, 897 (1971).

20. See, e.g., Boyd & Balentine, *supra* note 5, at 643-44; Willier, *supra* note 5, at 56; Comment, *supra* note 19, at 897.

21. See NCCF REPORT, *supra* note 4, at 147. Other commentators have suggested total abandonment of rate controls, leaving this function to competitive forces. See Jordan & Warren, *supra* note 2, at 392-94. These authors recognize, however, that usury concepts may be too deeply imbedded to allow this course at present. *Id.* at 394.

such a study may in fact be infeasible.<sup>22</sup> In any event, the revised Code does not change the strategy.<sup>23</sup> In support of their decision to continue relying on rate ceilings the drafters repeat the argument that legislative controls are doomed to fail.<sup>24</sup> As a matter of consistency, the revised version also retains the earlier policy of eliminating artificial obstacles to competition.<sup>25</sup> Its supporters point out that the revised U3C has enhanced competition by eliminating separation and duplication in the treatment of sales and loans, thus increasing the efficacy of competition as a check on interest rates.<sup>26</sup>

Evaluating the revised U3C on the matter of rates is difficult; the objections to the scheme of competition as a regulator<sup>27</sup> have not yet been answered satisfactorily. However, support for the approach has been enhanced by the National Commission on Consumer Finance suggestion that the adopted ceilings are reasonable,<sup>28</sup> and by the somewhat conflicting indications that credit in states adopting the original U3C has been extended at rates lower than the permitted maximum.<sup>29</sup>

Arizona has enacted a relatively comprehensive installment sales law,<sup>30</sup> thus obviating to a large extent the problem of an absence of regulation stemming from the "time-price" doctrine.<sup>31</sup> Moreover, the maximum rates set by the Arizona statutes appear generally lower than those allowed under the U3C.<sup>32</sup> However, because the Arizona laws typically employ an "add-on" method for fixing rates,<sup>33</sup> the evidence is

22. *But see* NCCF REPORT, *supra* note 4, at 108; Smith, *The Arkansas Case: A Lesson in Industry Cooperation*, 29 PERS. FINANCE L.Q. REP. 36, 37-38 (1975).

23. *See* U3C, Prefatory Note, at 88 (1974).

24. *See id.*; Miller & Warren, *supra* note 3, at 5-6.

25. *See* U3C, Prefatory Note, at 88-89 (1974).

26. *See* Miller & Warren, *supra* note 3, at 6 & n.43. The separation of sales and loans into different sections of the Code, a major basis for criticism of the earlier draft, *see* Boyd, *supra* note 7, at 664-65; discussion note 14 *supra*, was essentially abandoned in the revision. *See* U3C, Prefatory Note, at 98 (1974). Although some duplication remains, it is defended as necessary due to certain inherent differences between sales credit and loans. *See* Miller & Warren, *supra* at 7. The assumption that there are differences between the two is embodied, for instance, in a provision of the revised Code prohibiting licensed lenders from selling goods or services on the premises in attempts to evade credit rate ceilings. *See* U3C § 2.309 (1974). *See also id.* § 2.302, Comment 1 (stating that more lenient licensing qualifications for lenders and certain exemptions from licensing requirements have been made to facilitate entry into the cash loan field in order that rates will be forced below the ceiling by the resulting competition).

27. *See* text & notes 19-20 *supra*.

28. *See* U3C, Prefatory Note, at 88 (1974); NCCF REPORT, *supra* note 4, at 91-150.

29. *See* Miller & Warren, *supra* note 3, at 6.

30. ARIZ. REV. STAT. ANN. §§ 44-6001 to -6006 (Supp. 1975-76); *see* Boyd & Balentine, *supra* note 5, at 641-48. *See also* ARIZ. REV. STAT. ANN. § 44-1205 (Supp. 1975-76) (installment loans).

31. *See* discussion note 14 *supra*.

32. *Compare* ARIZ. REV. STAT. ANN. §§ 44-6002 and -6003 (Supp. 1975-76) with U3C § 2.201 (1974). *See also* Boyd & Balentine, *supra* note 5, at 645.

33. "Add-on" interest is determined by reference to the initial balance. Simple annual interest, on the other hand, is determined by applying a monthly rate to a declining balance. As a rough approximation it may be said that add-on rates would be

at best unclear.<sup>34</sup> Given these uncertainties, it may be fair to conclude that the revised U3C scheme is no worse than that existing in Arizona and arguably is an improvement.<sup>35</sup> Those areas which appear questionable do not themselves appear sufficiently objectionable to warrant rejecting the overall U3C scheme.<sup>36</sup>

### *Statutorily Supervised Lenders*

Another U3C revision relating to the price of credit involves licensing of supervised lenders. Both drafts of the U3C have required state licensing of persons or firms making loans at an interest rate in excess of 18 percent, unless such person or firm is already subject to supervision by the state or federal government.<sup>37</sup> The provisions in the original Code were criticized because of the ease of entry they allowed into the loan field,<sup>38</sup> the 18 percent interest rate,<sup>39</sup> and the lack of adequate state control following the initial licensing of a firm.<sup>40</sup> The

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nearly doubled when translated into simple annual interest rates. See Kripke, *supra* note 2, at 459.

34. See Opinion No. 69-16-L, 1969 OP. ARIZ. ATT'Y GEN. 96; Boyd & Balentine, *supra* note 5, at 645. Compare ARIZ. REV. STAT. ANN. § 44-1205(A)(2) (Supp. 1975-76) with *id.* § 44-6002(A).

35. Professor William D. Warren has made a persuasive argument that given the virtual standoff on rate regulation reform, "[t]he U3C appears to offer the best interim solution to the rate regulation problem." Warren, *Consumer Credit Law: Rates, Costs, and Benefits*, 27 STAN. L. REV. 951, 968 (1975). See generally *id.* at 964-68.

36. Another improvement resulting from adoption of these U3C provisions would be added uniformity in the state's laws governing retail installment transactions, ARIZ. REV. STAT. ANN. §§ 44-6001 to -6006 (Supp. 1975-76), including revolving charge accounts. These laws exclude motor vehicle transactions, *id.* § 44-6001(2); Opinion No. 72-26, 1972 OP. ARIZ. ATT'Y GEN. 57, because of their coverage under the Motor Vehicle Time Sales Disclosure Act. See ARIZ. REV. STAT. ANN. §§ 44-281 to -295 (1967); Opinion No. 72-26, 1972 OP. ARIZ. ATT'Y GEN. 57. The revised U3C contains no such exclusion. Bringing motor vehicle transactions within the coverage of a single law by adopting the U3C would be beneficial in Arizona, since the Motor Vehicle Time Sales Disclosure Act permits rates in excess of the revised U3C, as well as existing Arizona retail installment legislation. Compare ARIZ. REV. STAT. ANN. §§ 44-281 to -295 (1967) with *id.* § 44-6002(A) (Supp. 1975-76) and U3C § 2.201 (1974).

37. See U3C §§ 1.301(43), 2.301 (1974); *id.* §§ 3.501(3), .502 (1968). These provisions also apply to persons or firms taking assignments of such loans for collection or enforcement. State regulation of small lenders extending credit at high interest rates has existed ever since such lending practices were exempted from general usury laws. The purpose of such an exemption was to provide legitimate sources of credit for high-risk, and thus high-interest, borrowers who would otherwise have to look to lenders operating outside the law. See Jordan & Warren, *supra* note 2, at 389-90.

38. The ease of entry results from setting, as the qualification for licensing, the applicant's "financial responsibility, character, and fitness." U3C § 2.302(2) (1974); *id.* § 3.503(2) (1968), rather than adopting the test of "convenience and advantage" often used in prior small loan laws. See *id.* § 2.302, Comment 1 (1974). In practice, the latter test restricts entry, while the former results in essentially unlimited entry. Kripke, *supra* note 2, at 486. Both consumers—fearful of the entry of improper persons who will abuse the public or create financial disaster through mismanagement—and the small loan industry—appreciative of legal insulation from competition—had found the U3C test objectionable. See U3C, Prefatory Note, at 89 (1974); Kripke, *supra* at 486-87; Miller & Warren, *supra* note 3, at 7.

39. U3C § 3.501(3) (1968). A lower rate was urged in order to increase the number of institutions subject to regulation.

40. See generally *id.* §§ 3.503-.514. Banks and thrift institutions, unable to open

drafters responded only to the last criticism, amending the U3C to require separate licensing for each place of business rather than each firm;<sup>41</sup> thus, a firm's expansion would subject it to renewed scrutiny. The ease of entry criticisms were rejected on the ground that the Code's scheme of controlling interest rates through competition required a larger number of firms.<sup>42</sup> A reduction in the interest rate requiring regulation from 18 percent to 12 percent, although included in the working redraft, also was rejected.<sup>43</sup>

In considering these provisions for adoption in Arizona, any questions regarding ease of entry should be resolved in favor of the Code, since its general scheme of competitive control of rates relies to some extent on the provisions aimed at promoting competition. In regard to interest rates invoking state licensing control, although variations in a "uniform" law are not to be encouraged, it would be possible to adopt the sections proposed in the working draft rather than the final revised U3C, as was done in other states,<sup>44</sup> if sympathy for such an extension is strong.

### *Defining Credit Charges*

Determining which charges will be considered charges for credit and hence subject to laws governing credit rates can be problematical.<sup>45</sup> Both the original U3C and the revised version base their definitions of what constitutes a finance charge<sup>46</sup> on the definition contained in the federal truth-in-lending law.<sup>47</sup> Consequently, all charges imposed as a

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new offices without the approval of supervising agencies and subject to extensive supervision of their operations, contended that small loan lenders should be similarly regulated. *Id.*, Prefatory Note, at 89 (1974). Consumers also favored increased regulation.

41. *Id.* §§ 2.302(4), (6) (1974); *id.*, Prefatory Note, at 89.

42. *See id.* § 2.303, Comment 1. For discussion of the importance of competition in the U3C scheme, see text & notes 17-26 *supra*.

43. *See* U3C § 1.301(43) & Comment (1974); *id.*, Prefatory Note, at 89; Miller & Warren, *supra* note 3, at 7.

44. *See* U3C § 3.512, Action in Adopting Jurisdictions (Supp. 1976); COMMITTEE ON THE UNIFORM CONSUMER CREDIT CODE, REPORT No. 1 § 3.512, Comment (1972); *cf.* U3C, Prefatory Note, at 86 (1974).

45. Among the charges that have created definitional problems are "documentary service fees," "finders' fees," and "tag, title, and fees" associated with automobile sales. *See* Meyers v. Clearview Dodge Sales, Inc., 384 F. Supp. 722 (E.D. La. 1974). Whether delivery and packing charges by a photo album company were finance charges was the question in Mondik v. DiSimo, 386 F. Supp. 537 (W.D. Pa. 1974), *aff'd*, 521 F.2d 1399 (1975), while in Fisher v. Beneficial Finance Co., 383 F. Supp. 895 (D.R.I. 1974), the issue was whether additional interest charged for late payments at the contract rate was a finance charge, a delinquency charge, or a charge not subject to disclosure at all. Problems have also arisen as to the treatment of acceleration clauses in view of their impact on unearned finance charges. *See* McDaniel v. Fulton Nat'l Bank, 395 F. Supp. 422 (N.D. Ga. 1975) (holding that if an acceleration clause penalizes a debtor for missing a payment, the creditor may have to disclose the penalty). *See also* 15 U.S.C. § 1605 (1970) (defining "finance charge" for purposes of the federal truth-in-lending act); Jordan & Warren, *supra* note 2, at 394-400.

46. *See* U3C § 1.301(2) (1974); *id.* §§ 2.109, 3.109 (1968).

47. 15 U.S.C. § 1605 (1970); Reg. Z, 12 C.F.R. 226.4 (1976); *see* U3C §

condition of credit except those which are separately excluded are credit charges.<sup>48</sup> Among the important exclusions in the original U3C were charges for delinquency, default, and deferral.<sup>49</sup> Under the original version, however, there was some uncertainty as to whether certain practices involved finance charges such as to invoke U3C provisions concerning consumer credit transactions.<sup>50</sup> For example, some oil companies require full payment of the amount of each billing statement sent to credit card holders, assessing charges only if the payments are delinquent.<sup>51</sup> The revised U3C makes clear through its revised definitions of finance charge<sup>52</sup> and open end credit<sup>53</sup> that such transactions do not involve finance charges and are not subject to the consumer credit provisions.<sup>54</sup> True default or deferral charges imposed in connection with a transaction that is otherwise a consumer credit transaction<sup>55</sup> continue to be separately regulated.<sup>56</sup>

The Arizona statutes devote relatively little attention to defining credit charges.<sup>57</sup> To this extent, then, the revised U3C is more com-

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1.301(20) & Comment (1974); *id.* §§ 2.109 & Comment, 3.109 (1968). The federal truth-in-lending law, 15 U.S.C. §§ 1601-1681t (1970), *as amended*, (Supp. IV, 1974), requires creditors to disclose certain information regarding consumer credit transactions including any finance charge. A broad definition of finance charge is given followed by certain specific exemptions. *Id.* § 1605 (1970). *See generally* Boyd, *The Federal Consumer Credit Protection Act—A Consumer Perspective*, 45 NOTRE DAME LAW. 171 (1970).

48. *See* U3C § 1.301(2) & Comment (1974); *id.* §§ 2.109, 3.109 (1968). The basic definition in both the original and revised Codes is essentially the same: "all charges payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or as a condition of the extension of credit . . ." *Id.* § 1.301(20)(a) (1974); *see id.* § 2.109 (1968) (omitting words "or as a condition of"). Each goes on to enumerate certain types of charges included in this definition, these being identical except for one addition in the revision. *Compare id.* § 1.301(20)(a) (1974) *with id.* § 2.109 (1968).

49. *Id.* §§ 2.109, 3.109 (1968).

50. *See* Miller & Warren, *supra* note 3, at 24.

51. *Id.*

52. U3C § 1.301(20)(b)(i) (1974).

53. *Id.* § 1.301(28)(d).

54. *Id.* §§ 1.301(20), (28), Comments; Miller & Warren, *supra* note 3, at 24. A special limitation imposed on such delinquency charges is that they may not exceed allowable finance charges on open-end consumer credit sales. U3C § 2.601(2) (1974); *see id.* § 2.601, Comment 2. If delinquencies are ignored in practice, however, the charges are viewed as credit charges and the transaction is subject to all regulations governing consumer credit transactions. *See id.*; Miller & Warren, *supra* note 3, at 24.

55. Transactions are consumer credit transactions if a finance charge is imposed or the debt is payable in more than four installments excluding a down payment. *See* U3C §§ 1.301(12) & Comments (12), (14)-(15) (1974).

56. *See id.* §§ 1.301(20)(b), 2.502 & Comment 1, 2.503. The limitations imposed by sections 2.502 and 2.503 on default and deferral charges perhaps should be modified to prohibit charges in excess of those allowed by the rate limitation sections. *Id.* §§ 2.201-202, .401. A proposed Federal Trade Commission rule would prohibit late charges which exceed those permissible under the basic contract rate of finance charge. *See* FTC Credit Practices Rule, *supra* note 12, § 444.2(a)(9). This proposed rule, however, may go too far in disallowing any disparity between charges for credit when payments are timely and charges when payments are late or in default. Hence a limitation based on maximum rates seems preferable. *Cf.* ARIZ. REV. STAT. ANN. § 44-6003(D) (Supp. 1975-76); U3C § 2.601(2) (1974).

57. *Compare* ARIZ. REV. STAT. ANN. §§ 44-281(12), -6001(13) (Supp. 1975-76) *with* U3C § 1.301(2) (1974).

plete than current Arizona law and the difficulties of interpretation should be correspondingly reduced.<sup>58</sup> In particular, the attempt of the U3C to track federal law should avoid potential conflict and confusion between state and federal requirements in states adopting its provisions.<sup>59</sup> Moreover, the statutory exclusions in Arizona's rate-limiting laws are narrower, and somewhat less discriminating, than those of the U3C. The Arizona retail installment sales law does exclude delinquency payments from the definition of credit charges,<sup>60</sup> and to this extent resembles the U3C. However, the Arizona statute governing retail charge accounts applies where either a credit charge or a delinquency charge is involved.<sup>61</sup> Therefore, transactions which are not intended to be credit transactions,<sup>62</sup> for example, the oil credit card situation,<sup>63</sup> and perhaps other "30 days, same as cash"<sup>64</sup> transactions, appear to be within its scope. The U3C scheme of distinguishing credit and noncredit transactions and treating true deferral and default charges separately seems preferable. Should the U3C be adopted in Arizona, however, the provisions governing deferral and default charges should be modified to prohibit charges in excess of the ceilings established for finance charges.<sup>65</sup>

Another established policy borrowed from federal law by the revised U3C is the more-than-four-installment rule.<sup>66</sup> Under this rule, transactions in which a consumer is allowed to pay for goods or services or to repay a loan in more than four installments are considered credit transactions subject to the consumer credit provisions of the U3C.<sup>67</sup> The

58. Cf. *Browning v. Levy's of Tucson*, 20 Ariz. App. 325, 512 P.2d 857 (1973).

59. See *Boyd & Balentine*, *supra* note 5, at 646 (indicating how such confusion can occur under present Arizona law).

60. ARIZ. REV. STAT. ANN. § 44-6001(13) (Supp. 1975-76). *But see id.* § 44-1205 (installment loans). Limits on the amount of delinquency charges are established separately. See *id.* §§ 44-6002(C), -6003(D).

61. See *id.* §§ 44-6001(8), -6003.

62. Cf. *Browning v. Levy's of Tucson*, 20 Ariz. App. 325, 512 P.2d 857 (1973). Moreover, there is doubt in Arizona as to the treatment of default and deferral charges in loan transactions. See ARIZ. REV. STAT. ANN. § 44-1205 (Supp. 1975-76). Whether the loan statute or the installment sales statute should apply may itself be subject to doubt in some situations. See *id.* § 44-1205(A)(2).

63. See text accompanying note 51 *supra*.

64. Cf. U3C § 1.301(3), Comment (1974).

65. See discussion note 56 *supra*. One district court has held that an additional interest charge in the case of late payments is not a delinquency charge which must be disclosed under federal law. See *Fisher v. Beneficial Finance Co.*, 383 F. Supp. 895 (D.R.I. 1974).

66. See U3C § 1.301(30) (1974). This section adopts the more-than-four-installment rule as its definition of the phrase "payable in installments," which is one of the categories of transaction constituting a consumer credit sale, *id.* § 1.301(12) (a) (iv), or a consumer loan. *Id.* § 1.301(15) (a) (iii).

67. See *id.* §§ 1.301(13)-(15), (30) & Comment. In the federal context the rule has meant that the truth-in-lending requirements apply, see 15 U.S.C. § 1602(f) (Supp. IV, 1974); Reg. Z, 12 C.F.R. § 226.2(s) (1976), and has been upheld in this context by the United States Supreme Court. See *Mourning v. Family Publications Servs., Inc.*, 411 U.S. 356 (1973).

simplicity of this rule, however, belies the problems in its administration created by a U3C presumption that the cash price as stated by the seller in a disclosure statement required by law<sup>68</sup> is the actual cash price.<sup>69</sup> This means that although the installment transaction is a credit transaction to which the U3C applies generally, in order to invoke the specific rate limitations, the consumer may be required to prove that a finance charge is in fact included in the cash price.<sup>70</sup> Arguably, the creditor, who is in a better position to prove the costs considered in setting the price to the consumer, should bear the burden of proving that no finance charge is involved.<sup>71</sup> The Arizona statutes do not adopt the more-than-four installment rule; hence, again they are less complete and less consistent with federal law. The present statutes avoid the U3C's burden-of-proof problem, however, by defining cash price in essentially the same manner as does the revised U3C, but without the presumption.<sup>72</sup> If the State adopts the U3C, the presumption should be omitted.<sup>73</sup>

Although many states have passed special laws to permit the financing of insurance premiums and clarify the applicable regulatory scheme,<sup>74</sup> the problem was not addressed in the original U3C.<sup>75</sup> The revised Code adds a definition for insurance premium loan as a form of consumer loan<sup>76</sup> and includes several substantive provisions<sup>77</sup> which, together with other general provisions of the U3C, make special statutes unnecessary.<sup>78</sup> However, insurance transactions not involving installments are still not considered credit transactions, and properly disclosed insurance charges made in connection with a consumer credit

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68. See text & notes 124-58 *infra*.

69. This presumption is contained in both the original and revised versions of the Code. See U3C § 1.301(9) (1974); *id.* § 2.110 (1968). Thus, a clever seller, by including the costs of financing in the reported cash price, can avoid the U3C's restrictions on rates unless the consumer is able to disprove the presumption. Cf. *Mourning v. Family Publications Servs., Inc.*, 411 U.S. 356, 371 (1973); U3C §§ 1.301(9), Comment, 1.301(36), Comment (1974).

70. See U3C § 1.301(34) (1974).

71. See *Boyd*, *supra* note 47, at 178. Efforts to have this presumption deleted from the revised U3C nevertheless failed. Cf. *Miller & Warren*, *supra* note 3, at 12-13 (indicating that the presumption had been deleted in the working draft of the revised Code).

72. Compare ARIZ. REV. STAT. ANN. §§ 44-281(2), -6001(1) (Supp. 1975-76) with U3C § 1.301(9) (1974).

73. The presumption also might affect the application of the disclosure provisions. The U3C imposes a duty to disclose as required by the federal Truth-in-Lending Act. That law requires disclosures where a finance charge is imposed, whether or not identified as such. See *Boyd*, *supra* note 47, at 177-78.

74. See *Miller & Warren*, *supra* note 3, at 24.

75. *Id.*

76. U3C § 1.301(22) (1974).

77. See *id.* § 2.302(2) (criteria for licensing insurance premium lenders); *id.* § 2.401(6) (commencement of term of insurance premium loan); *id.* § 3.207 (form of insurance premium loan agreement); *id.* § 5.110(3) (notice of consumer's right to cure); *id.* § 5.111(4) (notice of cancellation of policy).

78. See *id.*, Prefatory Note, at 97.

transaction are not finance charges.<sup>79</sup> Arizona is not one of those states which has passed special legislation in regard to insurance financing,<sup>80</sup> and it is unclear from the language of its retail installment sales act whether finance charges on insurance premiums are excluded from its coverage.<sup>81</sup> In any event, insurance premium financing is sufficiently unregulated in Arizona that the revised U3C would be a measurable improvement.<sup>82</sup>

### *Methods of Computing Finance Charges*

As important as the interest rates permitted are the methods of computing the balance to which rates may be applied. A continuing controversy has surrounded the choice of formulas to be used in determining balances in open-end credit transactions.<sup>83</sup> The dispute has centered on the choice between the "previous balance" and "adjusted balance" methods.<sup>84</sup> Under the previous balance formula, finance charges are computed on a balance reflecting all charges and payments during a certain billing period, but are not billed to the customer until the close of the next billing cycle.<sup>85</sup> This method allows the customer to avoid all finance charges by paying the total amount when billed.<sup>86</sup> If the customer makes only a partial payment, however, a finance charge is billed on the entire previous balance.<sup>87</sup> The adjusted balance method, on the other hand, calculates charges using the previous balance minus all payments and credits, but without including any purchases made during the current billing period.<sup>88</sup> Another approach, and one that may most accurately reflect earned interest, is the "average daily bal-

79. See *id.* §§ 1.202(2), 2.501(2) & Comment.

80. See generally ARIZ. REV. STAT. ANN. §§ 20-101 to -167 (1975).

81. The act excludes from its definition of a credit charge "the amount, if any, charged for insurance premiums." *Id.* § 44-6001(13) (Supp. 1975-76). This language could refer only to the premiums themselves, or also to finance charges thereon.

82. It should be noted that the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015 (1970), has been held to exempt financing of insurance from federal disclosure law where the state regulates such financing. See *Ben v. General Motors Acceptance Corp.*, 374 F. Supp. 1199 (D. Colo. 1974). But see Krischer, "Truth" in Insurance Premium Financing, 30 BUS. LAW. 969 (1975).

83. See Miller & Warren, *supra* note 3, at 17. Open-end credit allows the debtor repeated extensions of credit which may be repaid as he or she sees fit. Although generally some minimum payment is required, the finance charge cannot be determined at the inception of the transaction. Closed-end credit, on the other hand, involves transactions in which the total amount of the finance charge to be imposed and the terms of payment can be fully disclosed by the creditor at the time credit is extended. See Brandel, *Open End Credit Disclosure*, 26 BUS. LAW. 815, 815-17 (1971).

84. See Miller & Warren, *supra* note 3, at 18-20.

85. *Id.* at 18.

86. *Id.* "The deferral feature of the previous balance method was designed to accommodate customers who wanted the option of using their revolving accounts like the formerly common 30-day charge accounts." U3C, Prefatory Note, at 94 (1974).

87. U3C, Prefatory Note, at 94 (1974). Thus, the customer pays a finance charge on the amount paid as well as on the amount carried over.

88. *Id.* at 95. See discussion note 96 *infra*.

ance" method.<sup>89</sup> Under this method finance charges are computed on the sum of the balances outstanding each day divided by the number of days in a billing period. There may or may not be provision for avoidance of all finance charges by full payment.<sup>90</sup>

Although Congress recently joined the debate over which method should be used,<sup>91</sup> the problem was not conclusively resolved.<sup>92</sup> Federal law presently requires only that the method used be disclosed to the debtor.<sup>93</sup> The original U3C took a similarly noncommittal position, permitting finance charges to be computed on a daily or monthly basis.<sup>94</sup> Under the revised U3C the daily balance method continues to be recognized as legitimate,<sup>95</sup> and states are given the additional option of sanctioning either the previous balance or adjusted balance method.<sup>96</sup> The Arizona legislature has already made a choice in favor of the adjusted balance method.<sup>97</sup> To this extent adoption of the U3C may appear to consumer advocates to present a risk of regression. Any such risk can be easily avoided, however, simply by electing the adjusted balance alternative as provided in the U3C.<sup>98</sup>

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89. This new method, requiring computer technology, could not be utilized until recent years. See U3C, Prefatory Note, at 94 (1974).

90. *Id.* See generally FTC Consumer Policy Statement No. 4, "The Previous Balance Method," [1969-1974 Transfer Binder of Truth-in-Lending Special Releases & Correspondence] CCH CONSUMER CREDIT GUIDE ¶ 30,369 (1970).

91. See S. 2101, 93d Cong., 1st Sess. (1973); Miller & Warren, *supra* note 3, at 20. Senate Bill 2101 introduced amendments to the Truth-in-Lending Act with the purpose of protecting consumers against unfair billing practices. Some of the amendments would prohibit the use of the previous balance method. See S. 2101, 93d Cong., 1st Sess., Amends. 362, 363 (1973). These amendments, however, were rejected by the Senate Committee on Banking, Housing, and Urban Affairs, which felt that the previous balance method was the simplest means available for computing finance charges and the one used by most small retail firms. Making this method illegal could have a serious impact on these small firms. See *Truth in Lending Act Amendments of 1973*, CCH CONSUMER CREDIT GUIDE, SPECIAL REPORT No. 1, at 12 (July 16, 1973) [hereinafter CCH SPECIAL REPORT].

92. See Miller & Warren, *supra* note 3, at 20; CCH SPECIAL REPORT, *supra* note 91. See discussion note 91 *supra*.

93. See 15 U.S.C. § 1637(a) (1970), *as amended*, (Supp. IV, 1974); Reg. Z, 12 C.F.R. §§ 226.7(a), (b)(3) (viii) (1976).

94. See U3C § 2.207(2) & Comment 3 (1968).

95. See *id.* § 2.202(2)(a) (1974). However, the revised U3C more specifically delineates how the average daily balance is to be computed. *Id.*

96. See *id.* § 2.202(2)(b) & Comment 2. The comment to section 2.202 indicates an inclination to follow any federal approach which may eventually be arrived at. Those supporting abolition of the previous balance method will be disappointed in the revised U3C. However, in all fairness, it should be pointed out that advocates of the adjusted balance approach, while pressing for deductions based on payments made during the billing cycle, never support adjustments upward based on new purchases. See Miller & Warren, *supra* note 3, at 20. The adjusted balance method in section 2.202(2)(b) adopts this consumer-advocated, but somewhat one-sided, approach, though referring to the "failure of protagonists for different views to recognize or openly discuss the basic questions involved." U3C, Prefatory Note, at 94 (1974).

97. ARIZ. REV. STAT. ANN. § 44-6003(B) (Supp. 1975-76); see *Browning v. Levy's of Tucson*, 20 Ariz. App. 325, 512 P.2d 857 (1973); Boyd & Balentine, *supra* note 5, at 644. But see ARIZ. REV. STAT. ANN. § 44-1205(A)(2) (Supp. 1975-76).

98. Another controversy which often arises in the area of finance charges involves credit cards. Traditionally, when a bank loans money it is entitled to charge interest from the date of the loan until the loan is paid. See U3C, Prefatory Note, at 95 (1974);

### Computing Deferral Charges and Rebates

The determination of deferral charges and rebates<sup>99</sup> has also been a subject of controversy in the consumer credit field, largely because of the industry's customary usage of the "sum of the balances" method<sup>100</sup> for computing such amounts.<sup>101</sup> Rebates in particular are a continuing subject of criticism by consumer advocates, based on the popular misconception that if, for example, the consumer repays the entire bill in one-half the installment time, a 50 percent refund should be given.<sup>102</sup> The sum-of-the-balances method allows for a refund of only 21/78 of the finance charge under such circumstances.<sup>103</sup> The original U3C created uncertainty regarding this prevailing practice by requiring separate calculation of deferrals and rebates.<sup>104</sup> Under the revised U3C, however, the industry practice has been reaffirmed.<sup>105</sup>

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Miller & Warren, *supra* note 3, at 19. However, when banks moved into the credit card field in the 1960's, use of this time period as a basis for interest charges was dropped in favor of allowing a 30-60 day "free period," thus enabling the banks to compete more effectively with retailers' credit card programs. U3C, Prefatory Note, at 95 (1974); Miller & Warren, *supra* at 19. Arizona has adopted the concept of a "free period" for finance charges under its adjusted balance method. See ARIZ. REV. STAT. ANN. § 44-6003(G) (Supp. 1975-76). If adopted, the revised U3C should be modified to retain this provision. It is worth noting that Citibank, the nation's second largest bank, has recently begun charging a 50-cent service fee on accounts paid in full within the billing period, thus abrogating to some extent the free period for customers paying promptly. Arizona Daily Star, April 18, 1976, § E, at 2, col. 5-8. Whether this practice will spread is presently uncertain. *Id.*

99. A deferral charge is a charge made by the lender to compensate for postponement of the scheduled due date of an installment. See U3C § 2.503 (1974). A rebate, on the other hand, is a cancellation of the unearned portion of a finance charge where the borrower prepays the balance due on a loan or other credit transaction. See *id.* § 2.510.

100. The sum-of-the-balances method, sometimes referred to as the "rule of 78" is a somewhat arbitrary approach to interest charges, assuring the creditor that the greatest amount of interest is earned early in the term of the contract. See Kripke, *supra* note 2, at 454-55. Kripke explains this method using as an example the financing of a \$1200 used car, payable in 12 monthly installments. "As a first simplification, it is apparent that during the first month of the credit the buyer has the use of his 12 \$100 bills. After he makes the first payment, he still has the use of 11 \$100 bills for another month; after the second payment he has the use of 10 \$100 bills; and so on. Over 12 months of the contract he has the use of 78 \$100-months, and the finance charge must pay for this use. In the first month of a 12-month contract, the creditor, therefore, earns 12/78 of the finance charge; the second month he earns 11/78; and so on." *Id.* at 454. For a more detailed explanation of this method, see U3C § 2.503, Comment 2 (1974). See generally Hunt, *Rule of 78: Hidden Penalty for Prepayment in Consumer Credit Transactions*, 55 B.U.L. REV. 331 (1975).

101. See Miller & Warren, *supra* note 3, at 21 (stating that both deferrals and rebates are computed by this method, which permits single computations in transactions involving both one or more deferrals and a subsequent rebate).

102. See Kripke, *supra* note 2, at 454-55.

103. See discussion note 97 *supra*. The U3C drafters argue that this method "simplifies computations and not only does not prejudice consumers but also reduces their costs." U3C, Prefatory Note, at 96 (1974); accord, Kripke, *supra* note 2, at 454-55. Consumer expectations of a proportional rebate are viewed as not reflecting commercial realities. See *id.* at 454-55.

104. See U3C §§ 2.210(6), 3.210(6) (1968); Miller & Warren, *supra* note 3, at 21. Under this requirement, a rebate following a deferral must be computed as though the extension had not occurred. U3C § 2.210, Comment, Example 6(a) (1968). Compare discussion note 101 *supra*.

105. See U3C §§ 2.503, .510 (1974); *id.*, Prefatory Note, at 96. However, use of the

Arizona law is presently silent concerning deferrals, rebates, and prepayment computations in the revolving charge context,<sup>106</sup> and would benefit from adoption of the guidelines contained in the revised U3C.

### *Attorneys' Fees as a Default Charge*

The Uniform Commercial Code [UCC] and laws of most jurisdictions allow creditors to include in their contracts provisions for recovery of attorneys' fees in cases of default.<sup>107</sup> Normally only reasonable attorneys' fees may be awarded;<sup>108</sup> however, as the determination of reasonableness is left to the courts, this award often constitutes a substantial part of the judgment debt.<sup>109</sup>

The U3C narrows the situations in which such provisions may be included in consumer credit contracts, treating attorneys' fees in most situations as a cost of doing business.<sup>110</sup> The original U3C offered adopting states a choice between two alternative treatments of attorneys' fees.<sup>111</sup> One alternative completely prohibited recovery of attorneys' fees,<sup>112</sup> while the second allowed recovery where the attorney was not a salaried employee of the creditor and the fee did not exceed 15 percent of the unpaid debt.<sup>113</sup> The revised U3C, with minor revisions, continues to offer these alternatives. The option to ban altogether the creditor's recovery of attorneys' fees is retained.<sup>114</sup> This approach assumes that the expense of paying an attorney is part of the creditor's cost of doing business, and that rate ceilings contained in the Code are generous enough to justify treating the attorneys' fees as part of overhead.<sup>115</sup> The second alternative, while still permitting recovery of fees up to 15 percent of the unpaid debt after default if the attorney is not a salaried

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actuarial method of computing refunds is mandated where the transaction involves a large number of payments and use of the sum-of-the-balances method would result in an unduly high cost to consumers. *See id.* § 2.510; *id.*, Prefatory Note, at 96. This method entails determination by reference to declining balances with corresponding ceilings in terms of simple annual interest rates. Boyd & Balentine, *supra* note 4, at 645.

106. Compare ARIZ. REV. STAT. ANN. § 44-6003 (Supp. 1975-76) with *id.* § 44-6002(B). *See also id.* § 44-6001(9). As to loans, see *id.* § 44-1205(A)(1).

107. *See id.* § 44-3150(A)(1); UNIFORM COMMERCIAL CODE § 9-504(1)(a) (1972 version) [hereinafter cited as UCC (1972)]; 1 CCH CONSUMER CREDIT GUIDE ¶ 4250 (1969).

108. 1 CCH CONSUMER CREDIT GUIDE ¶ 4250 (1969).

109. *See* CONSUMER'S ADVISORY COUNCIL, [N.Y.] DEP'T OF CONSUMER AFFAIRS, *supra* note 6; Note, *Resort to the Legal Process in Collecting Debts from High Risk Credit Buyers in Los Angeles—Alternative Methods for Allocating Present Costs*, 14 U.C.L.A.L. REV. 879, 896 & n.71 (1967); *cf.* *Equitable Lumber Corp. v. I.P.A. Land Development Corp.*, 18 UCC REP. SERV. 273 (N.Y. 1976) (consideration of reasonableness of liquidated damage clause which included attorneys' fees in the amount of 30 percent of the debt recovered).

110. U3C §§ 2.507 (Alt. A), (Alt. B), Comments (1974).

111. *See id.* §§ 2.413, 3.404 (1968).

112. *Id.* § 2.413 (Alt. A) (sales); *id.* § 3.404 (Alt. A) (loans).

113. *See id.* § 2.413 (Alt. B) (sales); *id.* § 3.404 (Alt. B) (loans).

114. *See id.* § 2.507 (Alt. A) (1974).

115. *See id.*, Comment.

employee of the creditor,<sup>116</sup> now restricts the types and amounts of loans in regard to which such recovery is possible.<sup>117</sup> The theory behind this alternative is that attorneys' fees, other than those involved in transactions resembling small loans, ought to be charged to the defaulting consumer who gives rise to the expense.<sup>118</sup>

As with the latter alternative of the U3C, the Arizona installment sales legislation allows recovery of fees only when the contract is referred for collection to an attorney who is not a salaried employee of the creditor.<sup>119</sup> Such recovery is permitted, however, wherever provided for by contract, limited only by the traditional reasonableness standard.<sup>120</sup> The lack of restriction on attorneys' fees in Arizona law is compounded by the fact that attorneys' fees are not even dealt with in the statute on loans.<sup>121</sup> Even a recently enacted statute allowing the recovery of attorneys' fees by any successful litigant in an action arising out of contract employs a reasonableness standard.<sup>122</sup> Some further limitation and clarification of the present statutory framework is, therefore, in order. Adoption of the revised U3C would provide such clarification. Which alternative would be preferable in Arizona is open to question, and the choice may have little practical effect: consumers ultimately may pay under either approach. The Federal Trade Commission has offered a proposed rule containing the same alternatives as those in the revised U3C, inviting comment thereon.<sup>123</sup> Completion of the FTC investigations will provide additional guidance on the merits of the two options and should be consulted by the legislature in making any decision between them.

### THE DISCLOSURE SCHEME

Coincidental with the increased concern over consumer protection, the theory has developed that if consumers know what they are getting into, particularly regarding the cost of credit, most abuses will be

116. See *id.* § 2.507(2) (Alt. B).

117. Attorneys' fees may not be provided for in other than open-end supervised loans where the amount financed is \$1000 or less, or where the balance at the time of default is \$1000 or less. See *id.* § 2.507(1) (Alt. B).

118. See *id.* § 2.507 (Alt. B), Comment. The right to recovery of attorneys' fees is not dependent on the attorney's filing suit against the defaulting consumer. *Id.*

119. See ARIZ. REV. STAT. ANN. § 44-289(A)(2) (1967); *id.* §§ 44-6002(C), -6003(E) (Supp. 1975-76).

120. See *id.* § 44-3150(A)(1) (Supp. 1975-76); *id.* § 44-289(A)(2) (1967); *id.* §§ 44-6002(C), -6003(E) (Supp. 1975-76). See text & notes 108-09 *supra*.

121. See ARIZ. REV. STAT. ANN. § 44-1205(A) (Supp. 1975-76).

122. Newly enacted section 12-341.01 provides: "In any contested action arising out of a contract, express or implied, the court may award the successful party reasonable attorney's fees." Ch. 170, § 2, 1976 Ariz. Sess. Laws 791 (effective Sept. 1, 1976). Since it is to be assumed that most installment sales contracts have a standard clause providing attorneys' fees for the creditor, this new provision creates a distinct new benefit for the debtor who is the successful litigant. See notes 148, 419 *infra*.

123. FTC Credit Practices Rule, *supra* note 12, at § 444.2(a)(8) & Statement of Reasons for the Proposed Rule.

avoided.<sup>124</sup> Disclosure, therefore, has been the object of legislation at both the state<sup>125</sup> and federal level. A far-reaching federal disclosure law, commonly referred to as the truth-in-lending law,<sup>126</sup> was enacted by Congress in 1968 to promote the informed use of credit.<sup>127</sup> Despite this preexisting federal disclosure law, the scope and effect of which had not yet been clarified through judicial interpretation,<sup>128</sup> the original U3C contained provisions treating in depth the disclosure of credit terms.<sup>129</sup> Although well intended, this double treatment raised doubts and created many problems.<sup>130</sup> Congress' intention to preserve local autonomy by allowing states to enact their own disclosure statutes<sup>131</sup> simply was not realized,<sup>132</sup> instead, massive duplication and confusion resulted.<sup>133</sup> The confusion was multiplied by the original U3C's giving creditors a choice between following the U3C or the truth-in-lending law.<sup>134</sup>

124. See Boyd, *supra* note 4, at 376-77; Whitford, *The Functions of Disclosure Regulation in Consumer Transactions*, 1973 WIS. L. REV. 400. But see Jordan & Warren, *supra* note 2, at 408-09; Kripke, *Gesture and Reality in Consumer Credit Reform*, 44 N.Y.U.L. REV. 1, 1-11 (1969).

125. ARIZ. REV. STAT. ANN. §§ 44-286 to -287 (1967) (Motor Vehicle Time Sales Disclosure Act); WIS. STAT. ANN. §§ 422.101-420 (1974), *as amended*, (Supp. 1975-76) (Consumer Credit Transaction Act); *id.* §§ 423.101-302 (Consumer Approval Transactions and Advertising Act); see Boyd, *supra* note 4, at 376-77.

126. See Consumer Credit Protection Act [Truth-in-Lending Act], 15 U.S.C. §§ 1601-1681t (1970), *as amended*, (Supp. IV, 1974). See generally Boyd, *supra* note 47.

127. See 15 U.S.C. § 1601 (1970), *as amended*, (Supp. IV, 1974). Theoretically, disclosure of credit terms to the consumer would enable him to compare rates and other terms available and choose the most advantageous, thus promoting both informed consumer decisions and competition among lenders. See *id.* As its method for achieving this goal the Act requires full, simple, and clear disclosure of credit charges computed and reported in terms of a "finance charge" and an "annual percentage rate," *id.* §§ 1631, 1636-1639; see H.R. REP. NO. 1040, 90th Cong., 1st Sess. 9 (1968); Rumsey, *Truth-in-Lending: Congress Reacts to the Creditors' Dilemma*, 24 EMERY L.J. 379, 379 (1975), both of which terms are extensively defined. 15 U.S.C. §§ 1605-1606 (1970). These items must be disclosed more conspicuously than other information given to consumers, Reg. Z, 12 C.F.R. § 226.6(a) (1976); Rumsey, *supra*, which includes the amount financed, payment schedule, default or delinquency charges, and any security interest taken. 15 U.S.C. §§ 1637-1639 (1970), *as amended*, (Supp. IV, 1974).

128. See Miller, *Living with Both the UCCC and Regulation Z*, 26 OKLA. L. REV. 1, 35 (1973).

129. See U3C §§ 2.301-313 (1968), *discussed in* Jordan & Warren, *supra* note 2, at 408-17; Kripke, *supra* note 2, at 455-69. The federal truth-in-lending law, provided for exemptions from the requirements of the Act of states whose laws were sufficiently similar thereto. 15 U.S.C. § 1633 (1970).

130. See Boyd, *supra* note 7, at 665; Miller, *supra* note 128; *cf.* Boyd & Balentine, *supra* note 5, at 646.

131. See discussion note 129 *supra*.

132. See U3C, Prefatory Note, at 96 (1974); LoPucki, *supra* note 5, at 335-36.

133. See U3C, Prefatory Note, at 96 (1974); Miller, *supra* note 128; Miller & Warren, *supra* note 3, at 22. The U3C drafters found that "in substantially all cases, creditors engaging in consumer credit look to the federal law and Regulation Z as the controlling law in the area of disclosure. Creditors have found that any additional provisions of state law on the subject constitute a nuisance in attempts to comply with federal law and frequently add confusion in these efforts to comply. Further, in those States obtaining exemptions from the Federal Reserve Board, state officials charged with the duty of enforcing state statutes and regulations designed to parallel the federal Act and Regulation Z find the task of keeping state law parallel onerous and troublesome." U3C, Prefatory Note, at 96 (1974).

134. See U3C §§ 2.301(2)-(3) (1968).

The revised U3C leaves the content of required disclosure to the federal law.<sup>135</sup> In place of the specific disclosure requirements of the original U3C, therefore, the revised version simply adopts the provisions of the federal truth-in-lending act, and extends their applicability to consumer credit transactions within state jurisdiction.<sup>136</sup> The federal provisions detailing basic financial disclosures,<sup>137</sup> those credit transactions to which the disclosure rules apply,<sup>138</sup> and the credit advertising directives<sup>139</sup> are thus incorporated by reference in the U3C.<sup>140</sup> The administrator of the U3C<sup>141</sup> is empowered to enforce the disclosure provisions of the federal law as state law,<sup>142</sup> and civil penalties essentially identical to those of the federal law are provided.<sup>143</sup> Additionally

135. The Code provides:

A person upon whom the Federal Truth in Lending Act imposes duties or obligations shall make or give to the consumer the disclosures, information, and notices required of him by that Act and in all respects comply with that Act. To the extent the Federal Truth in Lending Act does not impose duties or obligations upon a person in a credit transaction, except a consumer lease, that is a consumer credit transaction under this Act, the person shall make or give to the consumer disclosures, information, and notices in accordance with the Federal Truth in Lending Act with respect to the credit transaction.

*Id.* § 3.201(1) (1974). Thus, the revision "evidences the conclusion that the Congress has preempted the field of disclosure and any attempt of States to remain in the field by enacting statutes and regulations of their own cause [sic] substantially more harm than good." *Id.*, Prefatory Note, at 96. It should be noted, however, that the Code's definition of the truth-in-lending laws, *see id.* § 1.302, is not fully inclusive of the complete protective federal scheme as now enacted. *See text & notes 136-40 infra.*

136. *See* U3C § 3.201(2) & Comment.

137. 15 U.S.C. §§ 1631-1641 (1970), *as amended*, (Supp. IV, 1974).

138. *Id.* §§ 1601-1613; *id.* § 1614 (Supp. IV, 1974).

139. *Id.* §§ 1661-1665 (1970); *id.* § 1665a (Supp. IV, 1974).

140. *See* U3C § 1.302 (1974); discussion note 135 *supra*. The appropriate regulations issued by the Board of Governors of the Federal Reserve System are also incorporated. U3C § 1.302 (1974).

Under the U3C, "Federal Truth in Lending Law" is defined as Title I of the Consumer Credit Protection Act. *See id.* Therefore, the Fair Credit Reporting Act, 15 U.S.C. §§ 1681-1681t (1970), and the Equal Credit Opportunity Act, *id.* §§ 1691-1691e (Supp. IV, 1974), which are set forth as separate titles, are not within the incorporation-by-reference scheme of the revised U3C. The newly enacted Consumer Leasing Act of 1976, Pub. L. No. 94-240, 90 Stat. 257 (effective Mar. 3, 1977), should be within the U3C incorporation, however, as the Act amends Title I of the federal truth-in-lending law. *Id.* § 2; *see* U3C § 1.302 (1974). The Fair Credit Billing Act, 15 U.S.C. §§ 1666-1666j (Supp. IV, 1974), also was enacted as a subchapter of Title I. "[T]he provisions concerning issuance, liability of holders, and fraudulent use of credit cards" are specifically excluded from the U3C incorporation scheme. U3C § 1.302 (1974). *See* 15 U.S.C. §§ 1642-1644 (1970); *id.* § 1645 (Supp. IV, 1974). The revised U3C adopts, however, the federal approach to the question of whether credit card issuers should be subject to defenses available against the seller. *See* U3C § 3.403 (1974); *id.*, Prefatory Note, at 91. *See also text & notes 187-93 infra.*

141. "Administrator" is not defined under the revised U3C, though a blank section is included for such definition. This position will vary from state to state, and designation, therefore, is left to each adopting state. *See* U3C § 6.103 & Comment (1974). The administrator, generally, is the person or organization having the centralized power to administer the U3C. For a list of powers, *see id.* § 6.104.

142. *Id.* § 6.104(2).

143. *Compare id.* §§ 5.203(1), (5) with 15 U.S.C. § 1640(a) (Supp. IV, 1974). By explicitly providing that disclosure liability under the U3C is in lieu of liability under the federal law, U3C § 5.203(8) (1974), the revised Code avoids an uncertainty which has existed in states adopting the 1968 version. *See Redhouse v. Quality Ford Sales, Inc.*, 511 F.2d 230, 236 (10th Cir. 1975); U3C § 5.203(8), Comment 5 (1974).

debtors are allowed to assert in state courts other claims and defenses available under the federal truth-in-lending law.<sup>144</sup>

The revised Code's deference to federal law raises a question concerning the availability under its provisions of class actions based on disclosure violations. In sections imposing penalties for other than disclosure violations the revised U3C separates penalty and damages remedies, expressly precluding class suits as to the former.<sup>145</sup> No similar bar is stated, however, in the section imposing penalties for disclosure violations,<sup>146</sup> indicating that class actions in that context are permissible to the extent allowed by state procedural rules.<sup>147</sup> Indeed, if the scheme of deference to federal law is to be complete, class suits should be authorized in state courts to the same extent as in federal courts,<sup>148</sup> particularly if the "in lieu of" federal liability provision is to be effective.

144. U3C § 5.203(5) & Comment 3 (1974). This same section recognizes a right of rescission in certain real estate transactions comparable to that conferred by federal law. See 15 U.S.C. § 1635 (Supp. IV, 1974); Boyd, *supra* note 71, at 188-92. Additionally, section 5.203(6) expands the general definition of a creditor to permit compliance with the federal disclosure act. Compare U3C § 1.301(18) (1974) with *id.* § 5.203(6) & Comment 4.

145. See U3C §§ 5.201(1), (3) (1974); Miller & Warren, *supra* note 3, at 16. Recovery of a penalty, in an amount not less than \$100 nor more than \$1000, depending on the seriousness of the offense and other circumstances of the violation, is allowed in order to deter potential violators and to encourage consumer actions against violators. U3C § 5.201, Comment 2 (1974). The penalty may be recovered in addition to actual damages in certain types of actions. See *id.* § 5.201(1). The U3C treatment of class actions will be discussed further at text & notes 555-70 *infra*.

146. Compare U3C §§ 5.201(1), (3) (1974) with *id.* § 5.203.

147. See Dole, *Consumer Class Actions Under Recent Consumer Credit Legislation*, 44 N.Y.U.L. REV. 80, 97-114 (1969). But cf. Hall v. Coburn Corp., 26 N.Y.2d 396, 259 N.E.2d 720, 311 N.Y.S.2d (1970).

148. See FED. R. CIV. P. 23; cf. Dole, *supra* note 147, at 109-14. Actions for violations of the Consumer Credit Protection Act may be brought in any federal district court without regard to the amount in controversy. See 15 U.S.C. § 1640(e) (1970); R. JOHNSON, R. JORDAN & W. WARREN, ATTORNEY'S GUIDE TO TRUTH-IN-LENDING 205 (1969) [hereinafter cited as R. JOHNSON]. See also text & notes 555-70 *infra*.

Consumer class actions for disclosure violations have been a subject of controversy even in the federal context since the decision in *Ratner v. Chemical Bank New York Trust Co.*, 54 F.R.D. 412 (S.D.N.Y. 1972), refusing to allow a class action where a minor, technical violation could have subjected the defendant to 13 million dollars in penalties (\$100 each to 130,000 plaintiffs). See, e.g., Fischer, *From Ratner to Qui Tam: Truth-in-Lending Class Action Developments*, 24 HASTINGS L.J. 813 (1973); Hausmann, *Class Actions Under the Truth-in-Lending Act*, 1 CLASS ACTION REP. 26 (1972); Note, *Class Actions Under the Truth-in-Lending Act*, 83 YALE L.J. 1410 (1974). The *Ratner* balancing approach is not accepted by all courts, though the judicial concern regarding excessive penalties seems widespread. See *Evvaldi v. First Nat'l Bank*, 57 F.R.D. 545 (N.D. Ill. 1972) (class action permitted on condition that plaintiffs waive the \$100 minimum recovery and seek only actual damages and attorneys' fees); *Kristiansen v. John Mullins & Sons, Inc.*, 59 F.R.D. 99 (E.D.N.Y. 1973) (class action allowed where claim involved standard forms of credit contracts to be compared against the disclosure requirements of the Truth-in-Lending Act).

In 1974 Congress amended section 1640 to limit class action recovery to the lesser of \$100,000 or 1 percent of the net worth of the creditor and to make the \$100 minimum inapplicable. See 15 U.S.C. § 1640(a)(2)(B) (Supp. IV, 1974). Congress further provided that in determining the amount of awardable attorneys' fees in any class suit, the court should consider, *inter alia*, "the amount of any actual damages awarded, the frequency and persistence of failures of compliance by the creditor, the number of persons adversely affected, and the extent to which the creditor's failure of compliance was intentional." *Id.* § 1640(a)(3).

tive.<sup>149</sup> Under the revised U3C, the administrator is authorized to "adopt rules to keep this section in harmony with the Federal Truth in Lending Act."<sup>150</sup> This provision should be interpreted as empowering the administrator to promulgate procedural rules authorizing class actions for disclosure violations. Such an interpretation is strengthened by the fact that Congress recently amended the federal truth-in-lending law expressly to permit class actions for penalty recovery.<sup>151</sup>

A related question which has arisen under the federal truth-in-lending law is whether a creditor may be fined more than once for multiple disclosure violations to a single customer. Courts have gone both ways.<sup>152</sup> In a recent attempt to resolve this conflict, Congress amended the federal act in 1974 to provide that "[t]he multiple failure to disclose to any person . . . shall entitle the person to a single recovery . . . but continued failure to disclose after a recovery has been granted shall give rise to rights to additional recoveries."<sup>153</sup> The administrator's duty to harmonize state and federal disclosure procedures appear to oblige his application of this rule to the U3C civil liability section.<sup>154</sup>

Arizona in general has deferred to federal legislation in matters of disclosure, a deference largely attributable to the state's declining to adopt the original U3C.<sup>155</sup> Certain disclosure laws of limited applicability are nonetheless on the statute books.<sup>156</sup> The adoption of the revised U3C should be accompanied by a revision or repeal of all such laws to the extent that they apply to consumer credit transactions.<sup>157</sup> Adoption of the revised U3C with appropriate modification would result

149. See U3C § 5.203(8) (1974); discussion note 143 *supra*.

150. U3C § 5.203(9) (1974).

151. See Pub. L. No. 93-495, § 408(a), 88 Stat. 1518, amending 15 U.S.C. § 1640(a) (1970) (codified at 15 U.S.C. § 1640(a) (Supp. IV, 1974)); Evans, *Amendments to the Truth in Lending Act*, 29 PERS. FINANCE L.Q. REP. 9, 12-13 (1974). The amendment limits penalty recovery in a class action. See discussion note 148 *supra*.

152. Compare *Baker v. Shaker Savings Ass'n*, No. C 71-6, 8 UCC LAW LETTER NO. 8, at 7 (N.D. Ohio, Apr. 4, 1974), with *Thomas v. Myers-Dickson Furniture Co.*, 479 F.2d 740 (5th Cir. 1973).

153. See Pub. L. No. 93-495, § 407, 88 Stat. 1518, amending 15 U.S.C. § 1640 (1970) (codified at 15 U.S.C. § 1640(g) (Supp. IV, 1974)). There still might be a question whether this amendment eliminates multiple penalties for numerous errors in the same transaction as opposed to repetitions of the same error on successive disclosures. But see Evans, *supra* note 151, at 12. Two recent Seventh Circuit cases held that there can be only one recovery no matter how many violations or how many creditors, but, where joint debtors are involved, such as a husband and wife, then each may be entitled to separate recovery. *Mirabel v. General Motors Corp.*, Nos. 75-1048 to -1050 (7th Cir., Mar. 26, 1976); *Allen v. Beneficial Fin. Co.*, 531 F.2d 797 (7th Cir. 1976).

154. See U3C §§ 5.203(1), (9) (1974).

155. See text & note 7 *supra*.

156. See Motor Vehicle Time Sales Disclosure Act, ARIZ. REV. STAT. ANN. §§ 44-286 to -287 (1967); Small Loans Act, *id.* § 6-621 (1974). See generally Boyd, *supra* note 4, at 376-79.

157. See U3C § 9.103 & Comment (1974).

in substantial uniformity between state and federal disclosure law, thereby eliminating a problem of compliance that presently exists.<sup>158</sup>

### THE HOLDER-IN-DUE-COURSE AND RELATED DOCTRINES

One of the more well-known areas of consumer grievance has been the holder-in-due-course doctrine.<sup>159</sup> According to this doctrine, a transferee of negotiable paper takes free of most defenses and claims which may exist between the transferor and the debtor.<sup>160</sup> This doctrine, which has a long history of support in commercial circles,<sup>161</sup> has come under increasing criticism when applied in the consumer context.<sup>162</sup> The conflict between the need for ready transferability of debt instruments, on the one hand, and the legitimate complaint that creditors buying consumer paper have an obligation to police the practices of sellers doing business with relatively unknowing consumer-buyers<sup>163</sup> was resolved under the original U3C in favor of consumers. Creditors were prohibited from taking negotiable notes in consumer sale and lease transactions, thus vastly reducing that area of transactions in which the holder-in-due-course doctrine might apply.<sup>164</sup> The protection offered by the original U3C was not, however, complete, as an unknowing transferee retained the right to rely on the doctrine.<sup>165</sup> It remained

158. See Boyd & Balentine, *supra* note 5, at 646; text & notes 132-33 *supra*.

159. See Benson & Squillante, *The Role of the Holder in Due Course Doctrine in Consumer Credit Transactions*, 26 HASTINGS L.J. 427, 427-30 (1974).

160. See UNIFORM COMMERCIAL CODE § 3-305 [hereinafter cited as UCC]; E. PETERS, A NEGOTIABLE INSTRUMENT PRIMER 31-33 (2d ed. 1974); Countryman, *The Holder in Due Course and Other Anachronisms in Consumer Credit*, 52 TEX. L. REV. 1 2-4 (1973). In order to invoke the rule, the transferee must have given value for the negotiable paper and must have taken it in good faith and without notice of potential defenses. UCC § 3-302. Even then the transferee remains bound by certain defenses which go to the validity of the instrument itself, the so-called real defenses. See *id.* § 3-305(2); J. WHITE & R. SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE § 14-10 (1972).

161. See, e.g., E. PETERS, *supra* note 160, at 31; Countryman, *supra* note 160, at 2; LoPucki, *supra* note 5, at 344.

162. See, e.g., Benson & Squillante, *supra* note 159, at 428-30; Countryman, *supra* note 160; Jordan & Warren, *supra* note 2, at 436; Kripke, *supra* note 2, at 471-73; Littlefield, *Good Faith Purchase of Consumer Paper: The Failure of the Subjective Test*, 39 SO. CALIF. L. REV. 48 (1966); Murphy, *Another "Assault upon the Citadel": Limiting the Use of Negotiable Notes and Waiver-of-Defense Clauses in Consumer Sales*, 29 OHIO ST. L.J. 667 (1968).

163. See U3C, Prefatory Note, at 89-90 (1974). One commentator, noting that purchasers of consumer paper themselves have no effective way of policing dealer practices, suggests nonetheless that allocation of the risk of dealer misconduct to the creditor rather than the consumer serves the social policy of starving out merchants with bad track records: such merchants would, absent the holder-in-due-course doctrine, have difficulty finding a market for their paper. Rohner, *Holder in Due Course in Consumer Transactions: Requiem, Revival, or Reformation?*, 60 CORNELL L. REV. 503, 542-43 (1975).

164. See U3C § 2.403 (1968). The holder-in-due-course doctrine applies only to negotiable instruments. See *Carper v. Kanawha Banking & Trust Co.*, — W. Va. —, —, 207 S.E.2d 897, 915 (1974); E. PETERS, *supra* note 160, at 31. By prohibiting negotiable instruments other than checks in consumer transactions, the U3C thereby eliminated most of the holder-in-due-course problem.

165. See U3C § 2.403 & Comment (1968); LoPucki, *supra* note 5, at 345. Section

possible, therefore, for an unscrupulous seller to take a note illegally and then negotiate it to an unknowing creditor who could claim the protection of the holder-in-due-course doctrine.<sup>166</sup> Moreover, the original provision, being limited to sales and leases, offered no protection in the loan context.<sup>167</sup>

Under the revised U3C the victory for the consumer is much more comprehensive. The prohibition against taking negotiable instruments in consumer transactions is continued and broadened to include postdated checks.<sup>168</sup> Moreover, the exception for creditors without notice has been eliminated,<sup>169</sup> a new section specifically subjects any assignee of the seller's right to consumer claims and defenses.<sup>170</sup> Two limitations are placed on the assignee's liability, however: the amount of such liability cannot exceed the amount owed when the assignee learned of the claim or defense, and the liability does not arise until the debtor has made a good faith attempt to get satisfaction from the seller or lessor.<sup>171</sup>

In a more revolutionary vein,<sup>172</sup> the revised U3C also extends protection beyond sales and leases into the loan context. Under a new section,<sup>173</sup> a lender<sup>174</sup> who makes a loan enabling a consumer to buy or lease property or services may be subject to claims and defenses to the same extent as assignees.<sup>175</sup> Such liability is dependent on the existence of a close relationship between the lender and the seller or lessor, or actions by the lender which tie him closely to the seller or sales transaction.<sup>176</sup> The provision is aimed at reaching the situation where the loan

2.403 states that a holder is not in good faith if he knowingly takes a negotiable instrument issued in violation of the section. Thus a holder who took without knowledge of the instrument's origin might still avail himself of the holder-in-due-course doctrine. See U3C § 2.403, Comment (1968). To this extent the policy favoring negotiability was preferred over consumer interests. *Id.*

166. See U3C § 2.403, Comment (1968); J. WHITE & R. SUMMERS, *supra* note 160, § 14-9, at 485. In *Circle v. Jim Walters Homes, Inc.*, 19 UCC REP. SERV. 158 (10th Cir. 1976), a transferee of notes issued by consumers was held to be a holder in due course under Oklahoma's version of the U3C which is identical to the original U3C.

167. See U3C § 2.403 (1968); Benson & Squillante, *supra* note 159, at 436; Boyd, *supra* note 7, at 670; Littlefield, *Preserving Consumer Defenses: Plugging the Loophole in the New UCCC*, 44 N.Y.U.L. REV. 272, 292-93 (1969).

168. See U3C § 3.307 (1974).

169. Compare *id.* with *id.* § 2.403 (1968).

170. See *id.* § 3.404(1) (1974).

171. See *id.* § 3.404 & Comment. Under this provision oral notice to the assignee is effective unless the assignee requests written confirmation and the debtor fails to give such confirmation. See *id.* § 3.404(2).

172. The trend, as evidenced by recent state legislation, has been toward providing the degree of protection against holders in due course now embodied in the revised U3C. See A. LAFRANCE, M. SCHROEDER, R. BENNETT, & W. BOYD, *LAW OF THE POOR* § 114, at 56-57 (1973) [hereinafter cited as A. LAFRANCE].

173. U3C § 3.405 (1974).

174. The section excludes issuers of lender credit cards, *id.*, who are regulated by a separate section. See *id.* § 3.403; text & notes 191-94 *infra*.

175. Compare U3C § 3.404 (1974) with *id.* § 3.405.

176. See *id.* § 3.405, Comment. Under section 3.405(1) the requisite relationship between the lender and seller or lessor exists if:

and sale, although legally and technically separate transactions, are so interlocked that insulating the lender from liability is unjustified.<sup>177</sup>

Another device with much the same effect as the holder-in-due-course doctrine is the waiver-of-defense clause,<sup>178</sup> a provision frequently included in consumer credit contracts whereby the debtor waives defenses against potential assignees of the contract.<sup>179</sup> Such clauses, though subject to increasing consumer criticism,<sup>180</sup> are given effect in the absence of special consumer legislation or court decision.<sup>181</sup> The original U3C provided alternative sections addressing the problem, one prohibiting such clauses<sup>182</sup> and the other giving effect to the waiver unless the assignee was given notice of the defense or claim within 90 days after the assignment.<sup>183</sup> Such notice conditions have been severely criticized as giving to financial institutions "the best of both

(a) the lender knows that the seller or lessor arranged for the extension of credit by the lender for a commission, brokerage, or referral fee;

(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 has knowledge of the credit terms and participates in preparation of the document;

(e) the loan is conditioned upon the consumer's purchase or lease of the property or services from the particular seller or lessor, but the lender's payment of proceeds of the loan to the seller or lessor does not in itself establish that the loan was so conditioned; or

(f) the lender, before he makes the consumer loan, has knowledge or, from his course of dealing with the particular seller or lessor or his records, notice of substantial complaints by other buyers or lessees of the particular seller's or lessor's failure or refusal to perform his contracts with them and of the particular seller's or lessor's failure to remedy his defaults within a reasonable time after notice to him of the complaints.

177. See *id.*, Prefatory Note, at 89. For a description of the type of interlocking loan system at which the U3C provision is aimed, see Rohner, *supra* note 163, at 508 (including a reported instance where a door-to-door salesman had a loan company official accompanying him on his rounds).

The factors that will suffice to establish the requisite relationship under the U3C are clearly less than have been demanded by most courts as a precondition to a finding that holder-in-due-course status has been undermined. Compare Rohner, *supra*, and U3C § 3.405(1) (1974) (as set forth in note 176 *supra*) with *Slaughter v. Jefferson Fed. Sav. & Loan Ass'n*, 19 UCC REP. SERV. 171 (D.C. Cir. 1976) (refusing to deny holder-in-due-course status to a bank in the absence of a showing of specific facts which should put the bank on notice).

178. See A. LAFRANCE, *supra* note 172, § 115, at 58; Countryman, *supra* note 160, at 11-12. The similarity is intensified by the fact that under the Uniform Commercial Code [UCC] a waiver effectively cuts off all defenses against assignees who take in good faith, for value and without notice of a claim or defense—the same conditions under which a transferee of a negotiable instrument becomes a holder in due course. Compare UCC § 9-206(1) (1972) with *id.* § 3-302.

179. See A. LAFRANCE, *supra* note 172, at § 115; Rohner, *supra* note 163, at 507-08.

180. See U3C, Prefatory Note, at 89-90 (1974); Boyd, *supra* note 4, at 380-81.

181. See UCC § 9-206; Boyd, *supra* note 4, at 380. Moreover, under this section of the UCC a debtor who signs both a security agreement and a negotiable note makes an agreement to waive defenses as against an assignee of the security agreement. See UCC § 9-206(1) (1972).

182. See U3C § 2.404 (Alt. A) (1968).

183. See *id.* § 2.404 (Alt. B).

worlds."<sup>184</sup> The revised U3C, apparently responding to this criticism, now makes assignees of consumer contracts subject to the same defenses and claims as transferees of negotiable notes.<sup>185</sup>

The U3C revisions were induced partly by the burgeoning field of three-party credit cards.<sup>186</sup> The original U3C did not take sufficient account of the problems associated with this development, especially in the area of buyers' claims and defenses against credit card issuers.<sup>187</sup> The problems presented are not dissimilar to those associated with the holder-in-due-course doctrine and its counterpart, the waiver-of-defense clause. Consequently, the arguments raised by banks and other issuers favoring continued protection from such claims on the one hand, and card holders arguing for greater recourse on the other, are familiar. Perhaps because of the centralized nature of those opposing increased protection, however, the debate has been of somewhat greater intensity.<sup>188</sup> Congress, in response, recently enacted a Fair Credit Billing Act,<sup>189</sup> the approach of which was adopted by the revised U3C.<sup>190</sup> The compromise scheme offered by both the Act and Code subjects a card issuer to claims or defenses only if the original amount owing exceeds \$50, the cardholder has made a good faith effort to resolve the dispute

184. Jordan & Warren, *supra* note 2, at 435; *see, e.g.*, Boyd, *supra* note 7, at 671; Countryman, *supra* note 160, at 12-13; Littlefield, *supra* note 167, at 278-79.

185. U3C § 3.404 (1974). *See text & notes 170-71 supra.*

186. *See* Miller & Warren, *supra* note 3, at 4, 11-12; Note, *Development of Consumer Defenses Under a Tripartite Credit Card System*, 24 SYRACUSE L. REV. 1279 (1973). Three-party credit card transactions are those in which the credit card issuer is someone other than the seller. Bank credit cards are perhaps the most widely used form at present. Three-party cardholder agreements regularly include waiver-of-defense clauses, though the issuers do not concede that their status is one of an assignee. Rohner, *supra* note 163, at 509.

The liability of two-party credit card issuers is given special attention under the U3C. It is made clear that the section on card issuer liability is not intended to include issuers who are either manufacturers, suppliers, sellers, or lessors. U3C § 3.403(1) (1974). Liability as to these issuers presents a different problem than recourse against credit card issuers. *See id.* § 3.403, Comment 2. However, a manufacturer or supplier who sells or leases to licensed or franchised dealers is treated as an issuer under the credit card section up to the amount of credit extended. *See id.* § 3.403(2) & Comment 2.

187. The original U3C attempted primarily to fit the developing credit card device into the loan-sale framework, treating a three-party credit sale as a cash sale with regard to the seller and a loan with regard to the issuer. *See* Jordan & Warren, *supra* note 2, at 404. This approach, however, did not take into account the particular features of credit card arrangements.

188. *See* Miller & Warren, *supra* note 3, at 10-12. Banking interests have argued strenuously that in issuing credit cards and making payments to sellers, banks know nothing about sellers or the sales transactions involved and, therefore, should be completely insulated from any claims or defenses cardholders may have against the sellers. *See* U3C, Prefatory Note, at 91 (1974). Consumer advocates, on the other hand, contend that banks issuing credit cards are better equipped to police sellers than are consumers. For example, banks in their agreements with sellers can include special provisions for charge-backs against the seller when claims arise. *Id.*

189. *See* Pub. L. No. 93-495, § 306, 88 Stat. 1511 (1974), *amending* 15 U.S.C. §§ 1601-1681t (1970) (codified at 15 U.S.C. §§ 1666-1666j (Supp. IV, 1974)); McManus, *A Federal Fair Credit Billing Act*, 29 PERS. FINANCE L.Q. REP. 7 (1974).

190. U3C, Prefatory Note, at 91 (1974); *see id.* § 3.403.

with the seller or lessor, and the cardholder resides within 100 miles of the place of the sale or lease.<sup>191</sup> As with assignee liability, the credit card issuer is liable only as to the amount owing when the issuer gets notice of the claim or defense.<sup>192</sup> While the commercial necessity of these limitations on issuer liability is subject to dispute,<sup>193</sup> the provisions at least begin to pierce the immunity of issuers of the widely used three-party credit cards.

The new U3C provisions on preserving defenses represent a considerable improvement over the original U3C.<sup>194</sup> The abrogation of the holder-in-due-course doctrine and the protection against waivers is almost complete. There can be no doubt that the revised U3C represents a vast improvement over existing Arizona law. Even though the Arizona legislature has not been dormant in this area, the laws enacted leave much to be desired.<sup>195</sup> In particular, the law specifically designed to protect consumers against the holder-in-due-course doctrine and defense waivers<sup>196</sup> employs a cumbersome notice requirement, devoid of any warning to the consumer, with the result that the protection afforded may be largely illusory.<sup>197</sup> Also, the minimal protection afforded con-

191. 15 U.S.C. § 1666i(a) (Supp. IV, 1974); U3C § 3-403(3) (1974).

192. 15 U.S.C. § 1666i(b) (Supp. IV, 1974). Compare U3C §§ 3.403(3)(d), (4) (1974) with *id.* §§ 3.404(2)-(3).

193. It is argued that the already existing interbank system provides a ready mechanism for charge-backs throughout the nation, and that better means than use of holder-in-due-course status in small transactions exist to prevent overburdening card issuers with insignificant complaints. Rohner, *supra* note 163, at 548-49.

194. On the federal level, much the same result as that achieved by the U3C in this area is accomplished in relation to three-party credit cards by the Fair Credit Billing Act, 15 U.S.C. §§ 1666-1666j (Supp. IV, 1974), see text & notes 189-92 *supra*, together with a new Federal Trade Commission regulation abrogating the effectiveness of the holder-in-due-course doctrine and waiver-of-defense clauses. 16 C.F.R. § 433.2 (1976); see 40 Fed. Reg. 53506 (1975), as amended, 40 Fed. Reg. 58131 (1975). This regulation makes it an unfair or deceptive trade practice under section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45 (1970), as amended, (Supp. IV, 1974), for a seller or creditor in a purchase money loan, sale, or lease transaction directly or indirectly to take or receive a consumer credit contract which fails to contain the following provision in at least 10 point, boldface type:

#### NOTICE

ANY HOLDER OF THIS CONSUMER CREDIT CONTRACT IS SUBJECT TO ALL CLAIMS AND DEFENSES WHICH THE DEBTOR COULD ASSERT AGAINST THE SELLER OF GOODS OR SERVICES OBTAINED PURSUANT HERETO OR WITH THE PROCEEDS HEREOF. RECOVERY HEREUNDER BY THE DEBTOR SHALL BE LIMITED TO AMOUNTS PAID BY THE DEBTOR HEREUNDER.

For a discussion of the effectiveness of this rule, see Rohner, *supra* note 163, at 524-27.

195. In addition to enacting a statute aimed specifically at limiting the holder-in-due-course doctrine and waiver-of-defense clauses, ARIZ. REV. STAT. ANN. § 44-145 (Supp. 1975-76), the legislature has passed provisions subjecting home solicitation sales, *id.* § 44-5005(A), and assignors of security interests in consumer goods, *id.* § 44-3119 (1956), to such limits as well. See Boyd & Balentine, *supra* note 5, at 634-41.

196. ARIZ. REV. STAT. ANN. § 44-145 (Supp. 1975-76).

197. The Arizona statute subjects the transferee of negotiable consumer paper to defenses and claims only if there is proper notice of the claim within 90 days of the consumer's receipt of the goods or services. *Id.* Such notice must be provided in writing by certified mail to the seller or lessor. *Id.* There is no requirement that the consumer be notified of these requirements at the time of sale. Full compliance by an aggrieved consumer is therefore very unlikely. See Boyd & Balentine, *supra* note 5, at 637.

sumers does not extend to loan transactions<sup>198</sup> or to three-party credit card sales<sup>199</sup> as does the revised U3C. The U3C provisions, therefore, would provide Arizona consumers more complete protection and should be adopted. The fact that notice continues to play a role is something of a problem; however, the notice requirements are minimal.<sup>200</sup> Any uneasiness here could be alleviated by the addition of a requirement that consumers be advised of their rights in those transactions where assignments are contemplated.<sup>201</sup>

### RESTRICTIONS ON SECURITY INTERESTS

Consumer groups have been vocal for some time regarding the absence of limitations on a creditor's right to obtain an interest in any or all of a consumer's property as security for an indebtedness.<sup>202</sup> The original U3C responded to these complaints with a laudable provision prohibiting the creation of a security interest in property of the buyer other than that which was the subject of the consumer credit transaction.<sup>203</sup> This prohibition would tend to prevent such abuses as securing the sale of automobiles by a mortgage on the debtor's home.<sup>204</sup> Also proscribed in the original U3C was the creation of an interest in any of the lessee's property to secure a debt arising from a consumer lease.<sup>205</sup> The prohibitions, however, were subject to several important exceptions, which weakened their effectiveness in protecting consumers. Among these was an exemption for agricultural sales and leases.<sup>206</sup> A seller also was permitted to take a security interest in goods upon which services were performed or to which sold goods were installed or annexed.<sup>207</sup> Land could be taken as security where sold goods had been affixed thereto or where the land had been improved by the goods or services sold.<sup>208</sup> These exceptions were designed to carry forward the

198. ARIZ. REV. STAT. ANN. § 44-145(B)(3) (Supp. 1975-76); see Boyd & Balentine, *supra* note 5, at 640. See text & notes 167, 173-77 *supra*.

199. ARIZ. REV. STAT. ANN. § 44-145(B)(1) (Supp. 1975-76); see Boyd & Balentine, *supra* note 5, at 639-41. See text & notes 186-92 *supra*.

200. See text & notes 170-71 *supra*.

201. See Boyd & Balentine, *supra* note 5, at 637. See also U3C § 5.116(2) & Comment 2 (1974). As to present Arizona notice requirements, see text & note 197 *supra*.

202. See A. LaFRANCE, *supra* note 172, at 51-54; Robertson, *Consumer Protection Under the Uniform Consumer Credit Code*, 41 Miss. L.J. 36, 65 (1969).

203. U3C § 2.407(1) (1968); see Boyd, *supra* note 7, at 664.

204. See A. La FRANCE, *supra* note 172, § 113, at 52; cf. Boyd & Balentine, *supra* note 5, at 649.

205. See U3C § 2.407(2) & Comment 4 (1968).

206. *Id.* §§ 2.407(1)-(2). This exemption was intended to maintain the existing practice of farmers' giving a security interest in their land or equipment to secure the unpaid balance on a sale. *Id.* § 2.407, Comment 5.

207. *Id.* § 2.407(1). To qualify for this exemption, the debt must amount to at least \$300. *Id.*

208. *Id.* This exception was applicable only if the debt equalled \$1000 or more. *Id.*

established practice of utilizing improved goods or land as security in financing the goods or services by which they were improved.<sup>209</sup>

Another exception to the provision on security interests under the original U3C was made for cross-collateral security arrangements, whereby a seller secures the price of goods sold by taking an interest in both those goods and goods previously sold.<sup>210</sup> Although cross-collateral clauses themselves are permitted under the UCC,<sup>211</sup> when coupled with a payment arrangement that prevents the release of an item of collateral until all the items are paid for, they may be attacked on grounds of unconscionability.<sup>212</sup> The original U3C sought to meet the attacks, while allowing cross-collateral arrangements, by requiring that payments be applied on a first-in-first-out basis to assure that property would be released as security in the order of purchase.<sup>213</sup> A creditor thus could not retain security interest in all items purchased pending payment of the entire combined debt.<sup>214</sup>

These protections against excess security interests and oppressive cross-collateral and payment arrangements were welcomed by consumers, but there remained a major objection. The original U3C provisions were limited to consumer credit sales<sup>215</sup> and consumer leases,<sup>216</sup> leaving

209. See, e.g., Boyd & Balentine, *supra* note 5, at 650; Johnson, *The Uniform Consumer Credit Code and the Credit Problems of Low-Income Consumers*, 37 GEO. WASH. L. REV. 1117, 1124-25 (1969); Robertson, *supra* note 202, at 65-67.

210. U3C § 2.408 (1968).

211. See UCC § 9-204(3) (1972).

212. *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445 (D.C. Cir. 1965). In *Williams* the consumer's debts were consolidated and payments on a series of purchases were applied pro rata. Therefore, no single item was paid for until all were paid. In the event of default on any payment, the creditor could foreclose on all items. See *id.* at 447; A. LaFRANCE, *supra* note 172, § 113, at 53.

213. See U3C § 2.409 (1968); A. LaFRANCE, *supra* note 172, § 113, at 53.

214. See U3C § 2.409, Comment 1 (1968).

215. A consumer credit sale was defined:

(1) Except as provided in subsection (2), "consumer credit sale" is a sale of goods, services, or an interest in land in which

(a) credit is granted by a person who regularly engages as a seller in credit transactions of the same kind,

(b) the buyer is a person other than an organization,

(c) the goods, services, or interest in land are purchased primarily for a personal, family, household, or agricultural purpose,

(d) either the debt is payable in instalments or a credit service charge is made, and

(e) with respect to a sale of goods or services, the amount financed does not exceed \$25,000.

(2) Unless the sale is made subject to this Act by agreement (Section 2.601), "consumer credit sale" does not include

(a) a sale in which the seller allows the buyer to purchase goods or services pursuant to a lender credit card or similar arrangement, or

(b) except as provided with respect to disclosure (Section 2.301) and debtors' remedies (Section 5.201), a sale of an interest in land if the credit service charge does not exceed 10 per cent per year calculated according to the actuarial method on the unpaid balance of the amount financed on the assumption that the debt will be paid according to the agreed terms and will not be paid before the end of the agreed term.

(3) The amount of \$25,000 in subsection (1) is subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

*Id.* § 2.104. The definition in the revised Code is similar.- See *id.* § 1.301(12) (1974).

unaffected security interests for loans arranged in response to consumer sales.<sup>217</sup> This omission enabled a seller to circumvent the restrictive provisions by sending his customer to a lender rather than financing the sale himself.<sup>218</sup> Unfortunately, the revised U3C does not obviate this problem entirely. It does, however, offer certain mitigating improvements. Under the revision, the basic prohibition against security interests in property other than that sold applies to property generally, not just the property of the buyer or lessor.<sup>219</sup> This alteration is designed to close any potential loophole existing under the original U3C whereby a creditor might be allowed to take a security interest in a spouse's goods although prohibited from taking such interest in the consumer's own goods.<sup>220</sup> More importantly, a new section on supervised loans<sup>221</sup> has been added prohibiting enforcement of a non-purchase-money security interest<sup>222</sup> in a good when the good is in the possession of and is being used by the consumer-debtor, and is exempt under state law.<sup>223</sup> This section goes quite a distance toward meeting a primary objection raised against the original U3C, namely, a loophole in the restrictions on security interests.

216. A consumer lease was defined:

- (1) "Consumer lease" means a lease of goods
  - (a) which a lessor regularly engaged in the business of leasing makes to a person, other than an organization, who takes under the lease primarily for a personal, family, household, or agricultural purpose,
  - (b) in which the amount payable under the lease does not exceed \$25,000, and
  - (c) which is for a term exceeding four months.
- (2) "Consumer lease" does not include a lease made pursuant to a lender credit card or similar arrangement.
- (3) The amount of \$25,000 in subsection (1) is subject to change pursuant to the provisions on adjustment of dollar amounts (Section 1.106).

*Id.* § 2.106 (1968). For the virtually identical definition in the revised version of the Code, see *id.* § 1.301(4) (1974).

217. See *id.* §§ 2.407-408 (1968); A. LaFRANCE, *supra* note 172, § 113, at 53.

218. A. LaFRANCE, *supra* note 172, § 113, at 53. A seller apparently could avoid the effect of the restrictions by dividing his sale and credit operations into two separate firms. *But see* First Nat'l Bank v. LaJoie, 537 P.2d 1207 (Okla. 1975) (holding that a finance company which buys a contract containing a security interest in goods other than those the subject of a sale and then repossesses the goods on default is acting illegally because state law prohibited such a security interest and may not assert lender status as a defense).

219. Compare U3C § 3.301(1) (1974) with *id.* § 2.407(1) (1968).

220. See *id.*, Prefatory Note, at 92 (1974). Another potential loophole was closed by expanding the definition of "sale of goods" to include situations where, under a bailment or lease arrangement, the consumer agreed to pay rent substantially equivalent to the value of the goods. See *id.* § 1.301(35). These disguised sales were used to circumvent statutes regulating the sale of goods. See Miller & Warren, *supra* note 3, at 13.

221. A supervised loan is "a consumer loan, including a loan made pursuant to open-end credit, in which the rate of finance charge, calculated according to the actuarial method, exceeds 18 per cent per year." U3C § 1.301(43) (1974). See text & notes 43-44 *supra*.

222. A non-purchase-money security interest is an interest in a good other than one taken to secure the price of the good or to secure an advance used by the debtor to acquire rights in the good. Cf. UCC § 9-107 & Comment (1972).

223. U3C § 5.116 (1974). Under this section a consumer may voluntarily surrender

Arizona's laws regulating security interests provide only limited protection for consumers,<sup>224</sup> and are, in fact, inferior even to the original U3C.<sup>225</sup> The 1974 revisions, closing several loopholes, strengthen the argument favoring adoption of the revised U3C in Arizona.<sup>226</sup>

#### DEFAULT, REPOSSESSION, AND DEFICIENCY

Another area of continuing controversy in the developing field of consumer credit involves creditors' remedies. The seller or lender extending credit to consumers needs to be able to rely on effective legal remedies for recovery of losses when the consumer fails to fulfill his part of the bargain.<sup>227</sup> On the other hand, the consumer needs protection from creditor practices which unwarrantedly deprive him of the purchased item or other property. While prior law has been more responsive to the concerns of the creditor than those of the consumer, the revised U3C presents a more balanced approach.

#### *Default*

The critical event in any such remedial scheme is default by the consumer, which is the legal prerequisite to the creditor's right to take self-protective action.<sup>228</sup> Despite the importance of the default concept, the UCC does not define the term,<sup>229</sup> with the result that its definition is largely a matter of contract.<sup>230</sup> In the consumer context, definition by

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possession of the good. *Id.* § 5.116(2). Absent such a surrender, however, a lender may repossess the good only pursuant to a court order issued after a full hearing. *Id.* §§ 5.116(2)-(3). If the court finds that the consumer lacks the means to pay the debt and that continued possession is necessary to avoid undue hardship, it has the discretion not to issue process. *Id.* § 5.116(3) & Comment 2. This provision does not apply to interests in motor vehicles. *Id.* § 5.116(1). As to this exception, see discussion note 226 *infra*. For a discussion of the exemption laws, see text & notes 428-37 *infra*.

224. Arizona's Retail Installment Sales Act contains a provision permitting cross-collateral security, "but only until such time as the total of payments under the previous contract or contracts is fully paid." ARIZ. REV. STAT. ANN. § 44-6002(D)(6) (Supp. 1975-76). This limitation is applicable only to retail installment transactions as defined by the Act, *see id.* § 44-6001(10), and thus applies neither to leases nor loans. Other provisions governing security interests in consumer goods are found at *id.* §§ 44-3128(B), -5501(C).

225. *See* Boyd & Balentine, *supra* note 5, at 651. For example, under both the original U3C and ARIZ. REV. STAT. ANN. § 44-5501(C) (Supp. 1975-76), security interests are permitted on goods as to which services are rendered. However, under the U3C such interests are limited to secure only debts of \$300 or more. *See* U3C § 2.407(1) (1968).

226. It may also be of interest that the limitations on creating security interests coincide nicely with a proposed Federal Trade Commission rule. *See* FTC Credit Practices Rule, *supra* note 12, at § 444.2(a)(4). A major difference is that the proposed rule does not except security interests in motor vehicles. *Id.* Should the revised U3C be adopted, it would be advisable to consider eliminating this exception.

227. *See* NCCF REPORT, *supra* note 4, at 27.

228. *See* UCC § 9-501 (1972). Such action taken in the absence of a default may expose the creditor to serious legal consequences. *See id.* § 9-507(1); A. LAFRANCE, *supra* note 172, § 121, at 73.

229. J. WHITE & R. SUMMERS, *supra* note 160, § 26-2, at 956.

230. *See* Borochoff Properties, Inc. v. Howard Lumber Co., 115 Ga. App. 691, 696,

contract has meant definition by the creditor.<sup>231</sup>

The consumer is also disadvantaged under existing commercial law by the ease with which creditors can force the acceleration of debts.<sup>232</sup> Typically a consumer credit contract contains an acceleration clause allowing the creditor to accelerate or render due and payable the entire unpaid balance upon default of any one payment.<sup>233</sup> The law permits the creditor to go even further, and many take advantage of the law's leniency. Thus, creditors may provide in their contracts that a debt may be accelerated if the creditor feels "insecure."<sup>234</sup> The only limit on the creditor's ability to accelerate under such clauses is that he must act in good faith.<sup>235</sup> This, however, is not a terribly significant limitation because good faith generally requires only that the creditor act honestly in fact.<sup>236</sup> In any event, the burden of proving bad faith is on the debtor.<sup>237</sup> In reality, then, insecurity clauses allow creditors not only to accelerate in response to a default, but also to force debtors into default.<sup>238</sup>

When coupled with this rather extensive freedom to accelerate debts, the ability to define what constitutes default gives creditors essentially unfettered power—power which, in the minds of consumer advocates, is too easily abused<sup>239</sup> The original U3C failed to respond to the need for further limitations on the creditor's ability to declare default, though more progressive proposals such as the National Con-

155 S.E.2d 651, 654 (1967). It has been observed that "apart from the modest limitations imposed by the unconscionability doctrine and the requirement of good faith, default is 'whatever the security agreement says it is.'" J. WHITE & R. SUMMERS, *supra* note 160, § 26-2, at 956.

231. See U3C § 5.109, Comment 1 (1974).

232. See UCC § 1-208; *cf.* UCC § 9-506, Comment (1972); J. WHITE & R. SUMMERS, *supra* note 160, § 26-3, at 958.

233. See J. WHITE & R. SUMMERS, *supra* note 160, § 26-3, at 958. Such clauses, desired by creditors in order to avoid a series of lawsuits for each payment as it becomes due, are uniformly upheld by the courts. *Id.*

234. See UCC § 1-208; J. WHITE & R. SUMMERS, *supra* note 160, at § 26-3.

235. UCC § 1-208; A. LAFRANCE, *supra* note 172, § 121, at 75; J. WHITE & R. SUMMERS, *supra* note 160, § 26-3, at 959. Although such clauses present temptations for trigger-happy creditors, their use is generally upheld by courts. *Id.* at 961.

236. UCC §§ 1-201(19), 1-203 & Comment; see *Fort Knox Nat'l Bank v. Gustafson*, 385 S.W.2d 196 (Ky. App. 1964). There is, however, some confusion as to whether a subjective or objective standard should apply. See J. WHITE & R. SUMMERS, *supra* note 160, at 26-3. *But see* 2 G. GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY § 43.4, at 1197 (1965).

237. UCC § 1-208; see *Sheppard Federal Credit Union v. Palmer*, 408 F.2d 1369, 1371 (5th Cir. 1969); Comment, *Acceleration Clauses in Sales and Secured Transactions: The Debtor's Burden Under Section 1-208 of the UCC*, 11 B.C. IND. & COM. L. REV. 531 (1970).

238. Whatever the technical niceties of the standard of good faith and the burden of proof, "the courts before and after enactment of the Code [were] loathe to find acceleration of a debt under an 'insecurity clause' to be unreasonable." J. WHITE & R. SUMMERS, *supra* note 160, § 26-3, at 961.

239. See U3C § 5.109, Comment 1 (1974); NCCF REPORT, *supra* note 4, at 25.

sumer Act<sup>240</sup> did propose limits.<sup>241</sup> The revised U3C has responded to the need for a definition of default and, has ameliorated the harsh consequences of the creditor's freedom to accelerate debts.<sup>242</sup>

Failure to pay is the most common and probably least disputed event constituting a default.<sup>243</sup> The revised U3C, acknowledging non-payment as a clearly legitimate basis for creditor action, thus separates default into nonpayment and other events.<sup>244</sup> An agreement whereby failure to pay is made a default is clearly enforceable.<sup>245</sup> More controversial is the classification as default of events which affect prospective performance and ultimate satisfaction of the debt.<sup>246</sup> Under the revised U3C, agreements making default a function of the prospect of payment, performance, or realization of collateral are enforceable only to the extent that such prospect is significantly impaired.<sup>247</sup> Moreover, the creditor has the burden of proving that the impairment is substantial.<sup>248</sup> Although these provisions do not go as far as those of the National Consumer Act,<sup>249</sup> they clearly do much to limit the presently existing freedom of creditors to define what constitutes a default. Moreover, the standard of significant impairment precludes a creditor from accelerating a debt simply because it deems itself insecure.<sup>250</sup> By introducing a quantitative dimension and shifting the burden of proof to the creditor, the revised U3C renders default standards more objective.<sup>251</sup>

In a more dramatic departure from existing law, the revised U3C provides that a creditor may take action upon a default consisting of failure to make a payment only after giving the consumer notice and an

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240. NATIONAL CONSUMER LAW CENTER, NATIONAL CONSUMER ACT § 5.103(1) (First Final Draft, 1970) [hereinafter cited as NCA]. The National Consumer Act [NCA], a product of the National Consumer Law Center in Boston, has been superseded by the Model Consumer Credit Act. See NATIONAL CONSUMER LAW CENTER, MODEL CONSUMER CREDIT ACT iv (1973) [hereinafter cited as MCCA]; Miller & Warren, *supra* note 3, at 2.

241. See Boyd, *supra* note 7, at 669.

242. See U3C § 5.109, Comment (1974).

243. See *id.*, Comment 2. But see 1 D. CAPLOVITZ, DEBTORS IN DEFAULT 7-1 to -50 (1970). There may be disputes, of course, as to whether the consumer was obligated to pay—for example, where the consumer claims a breach of warranty or waiver on the part of the creditor. See A. LAFRANCE, *supra* note 172, § 121, at 74.

244. See U3C § 5.109 (1974).

245. See *id.* § 5.109(1).

246. Cf. *id.* § 5.109, Comment 2.

247. *Id.* § 5.109(2). The comment to this section defines this type of default as involving "behavior of the consumer which endangers the prospect of a continuing relationship." Examples given are the buyer's insolvency, illegal activity, or impending removal of assets from the jurisdiction. *Id.* § 5.109, Comment 2.

248. *Id.* § 5.109(2) & Comment 2.

249. The NCA limits default to situations where the debtor has failed to make three successive payments within a certain period, where the debtor has failed to pay any remaining balance within 3 months of the due date for the final installment, or where unpaid delinquent installments reach 30 percent of the amount financed. NCA, *supra* note 240, § 5.103; see Boyd, *supra* note 7, at 669; Comment, *Consumer Protection Under the UCC and the NCA—A Comparison and Recommendations*, 12 ARIZ. L. REV. 572, 581 (1970).

250. See text & notes 234-38 *supra*.

251. Contrast the existing law as discussed in text accompanying notes 237-38 *supra*.

opportunity to cure the default.<sup>252</sup> The required notice must state the fact and amount of the default, and explain that the consumer may cure the default<sup>253</sup> by paying within 20 days the amount currently due plus any unpaid delinquency or deferral charges.<sup>254</sup> If cure is effected, the consumer is restored to his rights under the agreement as though no default had occurred.<sup>255</sup> A creditor may not accelerate a debt during the period available for cure;<sup>256</sup> thus, to the extent that a debtor may reinstate the arrangement by curing the default, the harsh consequences of acceleration are avoided.<sup>257</sup>

The concept of cure, which has been promoted by consumer advocates for some time,<sup>258</sup> at its inception seemed quite revolutionary.<sup>259</sup> Nonetheless, there is some support for cure in judicial decisions,<sup>260</sup> including those of Arizona.<sup>261</sup> It has been observed that since sellers are allowed an opportunity for cure, it is only fair that consumers have such a right as well.<sup>262</sup> In any event, the cure provisions of the revised U3C represent a progressive step. If there is any legitimate objection to the revised U3C measures, it is more likely to be that the provisions do not go far enough; for instance, cure is available only in regard to failure to make required payments.<sup>263</sup> Other defaults, though otherwise circumscribed,<sup>264</sup> may not be cured and may result in an acceleration that forecloses redemption. It is not immediately apparent why the concept of cure is thus limited under the U3C. The limitation may be simply the result of a compromise, or it may reflect a concern that cure would be unmanageable as to defaults other than nonpayment.<sup>265</sup> Although these are not totally persuasive reasons,<sup>266</sup> the effect

252. U3C § 5.111 (1974). Notice is not to be given until the consumer has been in default for 10 days. *Id.* § 5.110.

253. *Id.* § 5.110(2). There are special notice requirements in the case of insurance loans. *See id.* § 5.110(3).

254. *Id.* § 5.111(1).

255. *Id.*

256. *Id.*

257. The notice and cure requirements do not apply where the debtor has voluntarily surrendered possession of the collateral. *See id.* § 5.110(1).

258. *See* NCA, *supra* note 240, § 5.207; A. LAFRANCE, *supra* note 172, § 125, at 87.

259. *See* Boyd, *supra* note 7, at 669, 674.

260. *See* Jefferson Credit Corp. v. Marcano, 60 Misc. 2d 138, 142-43, 302 N.Y.S.2d 390, 395-96 (N.Y. City Ct. 1969); Imperial Discount Corp. v. Aiken, 38 Misc. 2d 187, 238 N.Y.S.2d 269 (N.Y. City Civ. Ct. 1963); A. LAFRANCE, *supra* note 172, at § 125.

261. *See* Street v. Commercial Credit Co., 35 Ariz. 479, 485-88, 281 P. 46, 48-49 (1929) (interpreting the Uniform Conditional Sales Act).

262. A. LAFRANCE, *supra* note 172, § 125, at 87.

263. U3C §§ 5.110(1), .111(1) (1974).

264. *See* text & notes 246-47 *supra*.

265. *Cf.* U3C § 5.109, Comment 2 (1974). The creditor's right to cure is not similarly limited to defaults which can be liquidated monetarily. *See* UCC § 2-508; J. WHITE & R. SUMMERS, *supra* note 160, at § 8-4. *See also* UCC § 2-609 (conferring a right to demand assurance of performance on sellers and buyers); J. WHITE & R. SUMMERS, *supra*, § 6-2, at 169-70.

266. *See* authorities cited note 265 *supra*.

of the omission may be minimal. Most defaults result from nonpayment, and most abuses by way of "hair trigger" collection activity are precipitated by nonpayment.<sup>267</sup> Therefore, even the limited cure provisions when coupled with the default limitations, substantially improve the lot of consumer debtors, thus representing a significant and progressive contribution to existing law in Arizona.

### *Repossession*

Of the remedies available to creditors when consumers default, among the most notorious is repossession.<sup>268</sup> Under existing commercial law—which in most jurisdictions, including Arizona,<sup>269</sup> is the UCC—a creditor has the right to take from a defaulting consumer any goods in which a security interest exists.<sup>270</sup> The taking need not be preceded by legal process of any kind,<sup>271</sup> leaving the self-help remedy open to much abuse.<sup>272</sup> Not surprisingly, consumer opposition to repossession has been widespread,<sup>273</sup> with opponents arguing that the device is inappropriate in the consumer context.<sup>274</sup> Special objection has been made to the practice of forcible entry to effect a repossession.<sup>275</sup>

Serious doubts as to the continuing validity of repossession laws were raised by a 1972 United States Supreme Court decision requiring notice and a hearing prior to depriving a debtor of any significant property interest.<sup>276</sup> However, predictions made at that time regarding the demise of the remedy<sup>277</sup> were premature. Most courts have now concluded that repossession is legal since, as a self-help remedy, it

267. Cf. 1 D. CAPLOVITZ, *supra* note 243, at 4-1 to -13.

268. See 2 *id.* at 10-1 to -43 (1971).

269. See ARIZ. REV. STAT. ANN. §§ 44-2201 to -3202 (1967), *as amended*, (Supp. 1975-76).

270. ARIZ. REV. STAT. ANN. § 44-3149 (1967); UCC § 9-503 (1972); see Note, *Self-Help Repossession: The Constitutional Attack, the Legislative Response, and the Economic Implications*, 62 GEO. L.J. 273, 274-81 (1973).

271. UCC § 9-503 (1972); see NCCF REPORT, *supra* note 4, at 27; Note, *supra* note 270, at 275. Legal process is necessary only if the debtor resists or a breach of the peace is otherwise threatened. UCC § 9-503 (1972); see J. WHITE & R. SUMMERS, *supra* note 160, § 26-6, at 966-69.

272. See, e.g., 2 D. CAPLOVITZ, *supra* note 243, 10-1 to -43 (1971); Note, *Installment Sales: Plight of the Low-Income Buyer*, 2 COLUM. J.L. & Soc. PROB. 1, 9 (1966); Note, *supra* note 270, at 276-80.

273. See NCA, *supra* note 240, §§ 5.203, .208 & Comments.

274. See Boyd, *supra* note 4, at 402.

275. See A. LAFRANCE, *supra* note 172, § 122, at 77 & n.41. See text & notes 282-88 *infra*.

276. *Fuentes v. Shevin*, 407 U.S. 67 (1972); see Note, *supra* note 270, at 273-74. *Fuentes* invalidated laws authorizing the summary seizure of personal property under a writ of replevin. See also *North Georgia Finishing, Inc. v. Di-Chem, Inc.*, 419 U.S. 601 (1975) (garnishment); *Sniadach v. Family Finance Corp.*, 395 U.S. 337 (1969) (garnishment). But see *Mitchell v. W.T. Grant Co.*, 416 U.S. 600 (1974) (sequestration).

277. See A. LAFRANCE, *supra* note 172, § 124, at 83; Comment, *Creditors' Prehearing Remedies and Due Process*, 14 ARIZ. L. REV. 834 (1972).

involved no state action such as would invoke the due process objection.<sup>278</sup>

The original U3C, although cognizant of the due process considerations,<sup>279</sup> did not address this problem in the context of repossession.<sup>280</sup> Similarly, the revised U3C assumes the constitutional validity of the device and imposes no procedural constraints on its use.<sup>281</sup> The revision does respond, however, to some of the consumer objections by limiting the conditions under which the self-help remedy is available. Under the revised U3C, unless a consumer voluntarily surrenders the item, a creditor may take possession without judicial process "only if possession can be taken without entry into a dwelling and without the use of force or other breach of the peace."<sup>282</sup>

The breach of the peace limitation is not new to commercial law, being essentially the only limitation on self-help repossession contained in the UCC.<sup>283</sup> The UCC provision has been subject to definitional problems,<sup>284</sup> particularly in regard to whether entry into a debtor's dwelling constitutes a breach of the peace.<sup>285</sup> The revised U3C resolves this issue by specifically providing that entry into a dwelling without judicial supervision is never permitted.<sup>286</sup> The use of force in repossessions, another definitional problem under existing law, also appears resolved by the U3C revision flatly proscribing the use of force.<sup>287</sup>

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278. See *Burke, More Decisions on the Constitutionality of Self-Help Repossessions*, 27 PERS. FINANCE L.Q. REP. 115 (1973). The requirements of the due process clause of the fourteenth amendment apply only to states; thus, an action can be invalidated on this ground only if there is a sufficient level of state involvement. The question of due process applicability to self-help repossession is not closed, however, as the Supreme Court has so far avoided ruling on the question. See *Gonzalez v. Automatic Employees Credit Union*, 419 U.S. 90 (1974) (denying jurisdiction to review). Moreover, the Supreme Court recently has reaffirmed the due process stance taken in *Fuentes*. See *North Georgia Finishing, Inc. v. Di-Chem, Inc.*, 419 U.S. 601 (1975). Neither this case nor those previously decided, see *Fuentes v. Shevin*, 407 U.S. 67 (1972); *Sniadach v. Family Finance Corp.*, 395 U.S. 337 (1969), raised the state action issue, however, since garnishment and replevin procedures both involve some form of judicial action prior to the taking. The possibility of a successful due process challenge in Arizona may have been heightened by an Arizona supreme court decision holding that there is no common law right of replevin as to chattels the possession of which was lawfully obtained. *First Nat'l Bank v. Superior Court*, 112 Ariz. 292, 541 P.2d 392 (1975). It might be argued, based on this decision, that UCC § 9-503 (1972) in fact broadens rights available under the common law and hence constitutes the necessary element of state action. The difficulty with this argument is that the common law in many jurisdictions recognized a contractual right to recover chattels present in the conditional sales context. See *W. PROSSER, LAW OF TORTS* § 22 (4th ed. 1971).

279. For example, the original version did prohibit prejudgment garnishment. See U3C § 5.104 (1968).

280. See *NCA*, *supra* note 240, § 5.203, Comment.

281. See U3C § 5.112, Comment 2 (1974); *Miller & Warren*, *supra* note 3, at 15 & n.105.

282. U3C § 5.112 (1974).

283. See *ARIZ. REV. STAT. ANN.* § 44-3149 (1967); UCC § 9-503 (1972).

284. See *J. WHITE & R. SUMMERS*, *supra* note 160, § 26-6, at 966-69.

285. See *A. LAFRANCE*, *supra* note 172, § 122, at 77.

286. U3C § 5.112 (1974).

287. *Id.* It is not clear whether the revised U3C would go as far as the decision in

Under the UCC breach of peace prohibition, it was clear that physical force directed against a resisting debtor was forbidden,<sup>288</sup> but the permissibility of forced entry into automobiles, garages, and other non-dwellings was unsettled. The U3C apparently prohibits this form of force as well.

The revised U3C provisions on repossession seem quite progressive when compared with existing Arizona law. In Arizona the UCC provision governs,<sup>289</sup> and, therefore, the definitional problems associated with the breach of the peace limitation are present.<sup>290</sup> To the extent that the revised U3C resolves these problems at all, it is an improvement; to the extent that it resolves them in the direction of eliminating some of the more objectionable practices associated with repossession, its adoption in Arizona would be of clear benefit to consumers. As for the due process issue, the unwillingness of the U3C drafters to forge novel constraints is understandable. The trend in court decisions clearly vindicates self-help remedies against charges that they violate due process,<sup>291</sup> although their rejection of due process challenges probably reflects more a judgment of practical necessity than one based on consistent and persuasive reasoning.<sup>292</sup> Such practical demands would seem to call for modification of the repossession remedy rather than its total abolition.<sup>293</sup> This is, of course, precisely the approach taken by the revised U3C in retaining the remedy while placing limits on its availability.

### Deficiency Judgments

Discussions of repossession invariably turn to the problem of deficiency judgments.<sup>294</sup> Recent proposals for reform have made the creditor's right to recovery of a judgment dependent upon whether or not he

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Stone Machinery Co. v. Kessler, 1 Wash. App. 750, 463 P.2d 651 (1970), finding "constructive force" in violation of the breach of peace limitation where a sheriff, acting at the request of the creditor but not pursuant to legal process, accompanied the creditor and announced that he was assisting in retaking collateral. *Id.* at 757, 463 P.2d at 655. The revised U3C's apparent attempt to distinguish voluntary surrender from other recovery of collateral suggests that such an interpretation might be made. See U3C §§ 5.110, .112 (1974).

288. See, e.g., *Besner v. Smith*, 178 A.2d 924, 926 (D.C. Mun. Ct. App. 1962); *Willis v. Whittle*, 82 S.C. 500, 64 S.E. 410 (1909); cf. RESTATEMENT (SECOND) OF TORTS § 116 (1965).

289. See ARIZ. REV. STAT. ANN. § 44-3149 (1967); *Boyd*, *supra* note 4, at 396-97.

290. See text & notes 284-88 *supra*.

291. See text & note 278 *supra*.

292. See *Turner v. Impala Motors*, 503 F.2d 607 (6th Cir. 1974) (refusing to follow *Reitman v. Mulkey*, 387 U.S. 369 (1967), an important state action case, on the ground that *Reitman* was a "race" case. *Id.* at 610-11). See also discussion note 278 *supra*.

293. But see *Krahmer, Clifford & Lasley, Fuentes v. Shevin: Due Process and the Consumer, A Legal and Empirical Study*, 4 TEX. TECH. L. REV. 23 (1972), wherein the authors question the necessity of repossession in the consumer context. *Id.* at 61-62.

294. See NCCF REPORT, *supra* note 4, at 28.

elects to repossess the collateral.<sup>295</sup> The concept of deficiency by definition assumes a repossession and resale, the proceeds of which fail to satisfy the debt.<sup>296</sup> There exists a realistic concern that the resale of many consumer goods will not significantly reduce the debt. The value of the goods to the debtor may be significantly greater than their value on the market;<sup>297</sup> to permit both repossession and a deficiency judgment in such cases is to rub salt in the debtor's wound.<sup>298</sup> As a result it has been proposed that creditors be forced to elect remedies—either repossession or suit on the entire debt, but not both.<sup>299</sup>

The original U3C partially adopted this proposal. For consumer credit sales of goods with cash prices of \$1000 or less an election of remedies was required.<sup>300</sup> The creditor could either repossess the goods and consider the debt paid, or forego repossession and sue the debtor on the entire debt owing.<sup>301</sup> Although such a provision was desirable in principle, it had the serious shortcoming of being inapplicable to lenders, even where the loan effectively was prearranged by the seller to avoid the election rule.<sup>302</sup> Not surprisingly, this shortcoming prompted considerable criticism.<sup>303</sup>

The revised U3C responds to this criticism and more. A consumer is no longer liable for a deficiency unless the creditor has disposed of the goods in good faith and in a commercially reasonable manner.<sup>304</sup> In this respect the revised U3C has adopted the approach found in a line of decisions denying creditors a deficiency for failure to comply with the UCC conditions on disposition of collateral.<sup>305</sup> Moreover, pursuant to a

295. See *id.* at 29; 2 D. CAPLOVITZ, *supra* note 243, at 15-10 (1971).

296. Cf. UCC § 9-504(2) (1972).

297. See 2 D. CAPLOVITZ, *supra* note 243, at 15-8 to -9 (1971); Jordan & Warren, *supra* note 2, at 441.

298. The unfairness of the existing remedial situation is heightened by the creditor's ability under present law to purchase the goods himself for a low price at the resale, leaving the large deficiency for the debtor to bear. See UCC § 9-504 (1972); Jordan & Warren, *supra* note 2, at 441. Moreover, the creditor may add to the deficiency the reasonable expenses of retaking and selling the goods, plus attorneys' fees and legal expenses. UCC § 9-504 (1972).

299. See authorities cited note 295 *supra*. Under the UCC the secured party may repossess upon default, sell the collateral, and obtain a judgment against the debtor for any deficiency. UCC §§ 9-503 to -504 (1972). Under pre-UCC law a creditor electing to sue on the debt was held to be foreclosed from subsequent repossession. See J. WHITE & R. SUMMERS, *supra* note 160, § 26-4, at 964-65. For the present UCC provision regarding election, see UCC § 9-501(5) (1972).

300. U3C § 5.103 (1968). The \$1000 limitation was imposed for the purpose of restricting the election provision to those goods subject to excessive depreciation, and those as to which the expenses of sale are likely to be disproportionate to the amount due. See Jordan & Warren, *supra* note 2, at 441. See discussion note 298 *supra*.

301. To avoid circumvention of the election requirement the original U3C also prohibited execution on the collateral. U3C § 5.103(6)(b) & Comment 6 (1968).

302. See *id.* § 5.103(1) & Comment 2.

303. See Boyd, *supra* note 7, at 670.

304. See U3C § 5.103(1) (1974).

305. See *Skeels v. Universal CIT Credit Corp.*, 222 F. Supp. 696 (W.D. Pa. 1963),

suggestion by the National Commission on Consumer Finance<sup>306</sup> the revised U3C raises the ceiling for the applicability of the election of remedies requirement to \$1750.<sup>307</sup> In response to the criticism that loans should be covered, the U3C now provides that lenders who are so tied to a seller that they would be subject to claims and defenses arising out of the sale<sup>308</sup> must also make an election.<sup>309</sup> In so doing, the revised U3C closes this loophole in such a way as to render the deficiency provisions consistent with those governing the holder in due course.<sup>310</sup>

Evaluating existing Arizona law in light of the revised U3C provisions on deficiency liability is simple<sup>311</sup>—the U3C is generally far superior. Although Arizona has adopted a statute forcing an election of creditor remedies,<sup>312</sup> the Arizona law fails to cover loans.<sup>313</sup> It also applies only to goods having a \$1000 or less sale price, whereas the U3C ceiling is stated in terms of cash price.<sup>314</sup> Contrary to the revised U3C, the Arizona provision does not extend the deficiency limitation to goods which are not themselves the subject of a sale, but are taken as security for a sale.<sup>315</sup> The Arizona law does nothing with regard to failures to comply with the UCC provisions on disposition. As is true of the original and revised U3C, the Arizona law does contain provisions prohibiting execution on goods that could not be repossessed to satisfy a deficiency, and hence prevents circumvention of the election provision in that manner.<sup>316</sup> Although there are minor differences which appear to render the Arizona law superior to the revised U3C in certain par-

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*modified on other grounds*, 335 F.2d 846 (3d Cir. 1964); *Leasco Data Processing Equipment Co. v. Atlas Shirt Co., Inc.*, 66 Misc. 2d 1089, 323 N.Y.S.2d 13 (N.Y. City Civ. Ct. 1971); J. WHITE & R. SUMMERS, *supra* note 160, at § 26-15.

306. NCCF REPORT, *supra* note 4, at 29; *see* U3C, Prefatory Note, at 93 (1974).

307. U3C §§ 5.103(1)-(2) (1974). The concept of a "commercial unit" is borrowed from section 2-105(6) of the UCC and is included to eliminate doubts that subsection (2) may be inapplicable to a consumer credit sale of several items, where the total cash price is more than \$1750, but each item (commercial unit) does not separately cost more than \$1750. *Id.* § 5.103, Comment 3.

308. *See id.* § 3.405. *See* text & notes 172-77 *supra*.

309. U3C § 5.103(4) (1974).

310. *See* text & notes 159-71 *supra*.

311. *But see* discussion note 323 *infra*.

312. ARIZ. REV. STAT. ANN. § 44-5501 (Supp. 1975-76).

313. *See id.* § 44-5501(A); Boyd & Balentine, *supra* note 5, at 653-54.

314. *Compare* ARIZ. REV. STAT. ANN. § 44-5501 (Supp. 1975-76) with U3C § 5.103(2) (1974). Thus, if a finance charge raised the sales price, but not the cash price, above \$1000, the U3C would apply but the Arizona law would not. *See* Boyd & Balentine, *supra* note 5, at 653. Considering that the ceiling has been raised to \$1750 under the revised U3C, it is clear that the Arizona law suffers by comparison.

315. *See* Boyd & Balentine, *supra* note 5, at 653. *Compare* ARIZ. REV. STAT. ANN. § 44-5501(A) (Supp. 1975-76) with U3C § 5.103(3) (1974).

316. *See* ARIZ. REV. STAT. ANN. § 44-5501(C) (Supp. 1975-76). Also, under both existing Arizona law and the revised U3C, a consumer may be held liable in damages if the consumer wrongfully damages collateral or if, after default and demand, the consumer wrongfully fails to make the collateral available. *See id.* § 44-5501(B); U3C § 5.103(6) (1974).

ticulars,<sup>317</sup> these are hardly important enough to weigh the scales in favor of existing Arizona law.

There is one significant improvement incorporated in the Arizona law, however, which cannot be so easily ignored. Under the Arizona statute a consumer is entitled to any cash surplus when the fair market value of repossessed goods exceeds the debt plus expenses.<sup>318</sup> While the surplus provision by itself is an important advance, use of the fair market formula is an even greater improvement. The usual practice is to determine surpluses—and deficiencies—in regard to resale proceeds.<sup>319</sup> Since the Arizona statute makes no reference to resale, it could be interpreted to require the payment of a surplus to the consumer even where no resale takes place, thus at least partially avoiding the effects of strict foreclosure.<sup>320</sup> A proposed Federal Trade Commission rule, requiring that debtors be given credit for the fair market value of the collateral,<sup>321</sup> would accomplish the same results as the Arizona statute. In fact, the proposed rule would go even further to require that all deficiencies, whether or not in an election-of-remedy situation, be determined according to fair market value of collateral rather than resale price.<sup>322</sup> If the revised U3C is adopted, it should be amended to incorporate the fair market value features of the Arizona statute and the proposed Federal Trade Commission rule.<sup>323</sup>

### JUDGMENTS AND COLLECTION

When self-help methods fail to provide relief, creditors are likely to involve the courts in the collection process. Creditors may file suits even when they have little expectation of ever collecting subsequent to a favorable judgment.<sup>324</sup>

317. The Arizona law prohibits repossession by the creditor once an action is brought for the unpaid balance, regardless of whether the suit reaches judgment. *See* ARIZ. REV. STAT. ANN. § 44-5501(C) (Supp. 1975-76). The U3C prohibition is limited to judgments. *See* U3C § 5.103(7)(b) (1974). Furthermore, the Arizona provision regarding execution is not qualified by price as is that of the revised U3C. *See* ARIZ. REV. STAT. ANN. § 44-5501(C) (Supp. 1975-76). Arguably, therefore, a seller who brings an action cannot later retake the goods, and if he obtains a judgment cannot levy on the goods. The U3C, on the other hand, permits either levies or recovery of the goods unless the action is one in which the seller "would not be entitled to a deficiency judgment if he repossessed the collateral . . ." thus restricting the limitation to goods with a sale price under \$1750. U3C § 5.103(7) (1974); *see* Boyd & Balentine, *supra* note 5, at 653.

318. ARIZ. REV. STAT. ANN. § 44-5501(B) (Supp. 1975-76).

319. *See* J. WHITE & R. SUMMERS, *supra* note 160, at § 26-15; Boyd, *supra* note 7, at 670.

320. *See* J. WHITE & R. SUMMERS, *supra* note 160, at § 26-8. *See also* Boyd & Balentine, *supra* note 5, at 651-52.

321. FTC Credit Practices Rule, *supra* note 12, at § 444.2(7).

322. *Id.* *See also* Boyd, *supra* note 7, at 670.

323. A recent study of automobile deficiency judgments in California led the investigator to recommend the fair market value measure to control claims for deficiency. Note, *I Can Get It For You Wholesale: The Lingering Problems of Automobile Deficiency Judgments*, 27 STAN. L. REV. 1081, 1104-07 (1975).

324. Creditors sue debtors in hopes of collecting the debt by invoking the power of

## Judgments

Consumer representatives have been especially concerned with problems arising at the judgment stage of a consumer transaction.<sup>325</sup> The high rate of default judgments entered,<sup>326</sup> especially against low-income debtors,<sup>327</sup> reflects serious deficiencies in the legal system, and is not necessarily evidence that most debtors are in fact in default.<sup>328</sup> This viewpoint is supported by the existence of skimpy pleading requirements,<sup>329</sup> practices such as venue agreements which virtually assure nonappearance of debtors,<sup>330</sup> confession of judgment and cognovit note laws,<sup>331</sup> and even the practice of falsified, or "sewer," service,<sup>332</sup> all of which facilitate and probably promote default judgments.

While the original U3C failed to address most of these problems, the revised version includes a number of new provisions aimed at

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the court. However, even if they never collect a judgment against the debtor, the judgment is still available for tax purposes. See 2 D. CAPLOVITZ, *supra* note 243, at 11-1 (1971).

325. See *id.* at 11-1 to -75.

326. Studies show the default rate to be as high as 90 percent in some urban areas. U3C § 5.114, Comment (1974).

327. See 2 D. CAPLOVITZ, *supra* note 243, at 11-66 (1971).

328. *Id.* at 11-73 to -75; see Note, *The Persecution and Intimidation of the Low-Income Litigant as Performed by the Small Claims Court in California*, 21 STAN. L. REV. 1657 (1969).

329. See U3C § 5.114, Comment (1974) (pointing out that current procedural rules requiring that a complaint contain "only the barest of facts" are geared towards contested litigation).

330. Cf. H. KRIPKE, CONSUMER CREDIT 305-06 (1970). See also 2 D. CAPLOVITZ, *supra* note 243, at 11-38 to -40 (1971). This problem is exacerbated by general venue provisions allowing an action to be filed where either the plaintiff or the defendant resides. U3C § 5.113, Comment (1974); see H. KRIPKE, *supra*.

331. See, e.g., Countryman, *supra* note 160, at 13-15; Hobson, *Cognovit Judgments: An Ignored Problem of Due Process and Full Faith and Credit*, 29 U. CHI. L. REV. 111, 126 n.92 (1961); Note, *Confessions of Judgment*, 102 U. PA. L. REV. 524, 524 n.5 (1954). Under a cognovit clause or warrant of attorney, a debtor authorizes the seller or his assignee to enter an appearance for and confess judgment against him. See Countryman, *supra* at 13; Hobson, *supra* at 111 & n.2. This consent is given prior to the occurrence of any actual default. Confession of judgment, while originally distinguishable as occurring before the court subsequent to the alleged default, now means essentially the same thing as a cognovit clause. See Note, *supra* at 524.

It is important to distinguish contract clauses that authorize the creditor to confess judgment against the debtor, often without notice, from consent judgments. Judgments entered with the consent of the debtor after default on the contract are universally permitted. See 1 CCH CONSUMER CREDIT GUIDE ¶ 4070, at 4036 (1972). Confession devices, however, have been successfully attacked in the courts on due process grounds. See *Swarb v. Lennox*, 405 U.S. 191 (1972); *Atlas Credit Corp. v. Ezrine*, 25 N.Y.2d 219, 250 N.E.2d 474, 303 N.Y.S.2d 382 (1969). But see *Overmeyer Co., Inc. v. Frick*, 405 U.S. 174 (1972) (upholding a cognovit clause in a commercial context, but stating, "[W]here the contract is one of adhesion, where there is great disparity in bargaining power, and where the debtor receives nothing for the cognovit provision, other legal consequences may ensue." *Id.* at 188).

332. See U3C § 5.115, Comment (1974); 2 D. CAPLOVITZ, *supra* note 243, at 11-2 to -7 (1971); Note, *supra* note 272, at 9-12. See generally A. LAFRANCE, *supra* note 172, at § 126. "Sewer service" is used to describe situations where summonses are thrown away (down the sewer) rather than served, and affidavits of service are falsified by unscrupulous private process servers and firms. See 2 D. CAPLOVITZ, *supra* at 11-5; Note, *A Possible Solution to the Problem of "Sewer Service" in Consumer Credit Actions*, 51 N.C.L. REV. 1517 (1973). This practice, while more prevalent in jurisdictions employing private process servers, is not restricted to these areas. U3C § 5.115, Comment (1974); A. LAFRANCE, *supra*, § 126, at 88.

alleviating if not eliminating them. To begin with, no default judgment may be entered against a debtor unless the creditor's complaint is verified by sworn testimony, affidavit, or otherwise, showing the propriety of the relief sought.<sup>333</sup> Moreover, under the revised U3C a complaint must specifically allege the facts constituting the consumer's default, the amount to which the creditor is entitled, and an indication of how this amount was determined.<sup>334</sup> These requirements have a dual impact. The provision requiring the creditor to set forth the facts of the claimed default rather than mere conclusions facilitates a response from the debtor, and thus increases the likelihood of its being filed.<sup>335</sup> Even if no response is filed, however, the requirements governing the amount due and the manner of its calculation provide some limitations on the award to be entered against the defaulting debtor.<sup>336</sup>

In an effort to deal with the venue problem,<sup>337</sup> the revised U3C requires that an action by a creditor arising from a consumer credit transaction be brought where the consumer resides, except in cases involving interests in land which may be brought where the land is located.<sup>338</sup> The venue limitation does not affect existing requirements for service of legal process.<sup>339</sup> However, the revised U3C does address the sewer-service problem by giving courts broad discretion to stay the enforcement of judgments and reexamine the claim upon which the judgment rests.<sup>340</sup> Thus, an unnoticed debtor can reopen the case and have his defenses heard by the court even after judgment has been rendered. As was true under the original U3C,<sup>341</sup> the revised U3C also prohibits the use of confession-of-judgment provisions and cognovit clauses.<sup>342</sup>

The revised U3C provisions on judgments represent a marked improvement over existing Arizona law. Arizona's notice pleading rules permit the skimpy complaints that invite default.<sup>343</sup> Although

333. U3C § 5.114(2) (1974).

334. *Id.* § 5.114(1).

335. The requirements should eliminate the tailoring of complaints, particularly by use of the so-called common counts, to foreclose defenses. *Cf.* Note, *supra* note 109, at 890 nn.47, 52.

336. *See* U3C § 5.114, Comment (1974). *But see* Note, *supra* note 109, at 889-90. The information available to the court from the usual notice pleadings provides an insufficient basis for an accurate award. U3C § 5.114, Comment (1974).

337. *See* text & note 330 *supra*.

338. U3C § 5.113 (1974). Suits against nonresident debtors may be brought in the county where the sale, lease, or loan was made. *Id.*

339. *Id.* § 5.113, Comment.

340. *Id.* § 5.115 & Comment.

341. *See id.* § 2.415 (1968) (sales); *id.* § 3.407 (loans).

342. *Id.* § 3.306 (1974).

343. *See* C. SMITH, ARIZONA MANUAL FOR JUSTICE COURTS § 121 (1962). *Compare* Bates v. Bates, 1 Ariz. App. 165, 168, 400 P.2d 593, 596 (1965), and ARIZ. R. CIV. P. 8(a) with U3C § 5.114(1) (1974).

Arizona courts have stated that default judgments are not favored,<sup>344</sup> there are few limitations on the entry of default judgments in Arizona.<sup>345</sup> It appears that courts must conduct a hearing to determine the amount of damages when damages are unliquidated.<sup>346</sup> Only claims upon an open account need be verified,<sup>347</sup> however, and a verified claim, if not denied in writing under oath at least one day before trial, will be treated as prima facie correct.<sup>348</sup> The Arizona courts also seemingly have limited the setting aside of default judgments<sup>349</sup> to cases in which the party seeking relief is able to demonstrate the existence of a meritorious defense or excusable neglect.<sup>350</sup> The revised U3C appears to give relief in a broader range of cases.<sup>351</sup>

Under Arizona's venue statutes<sup>352</sup> creditors may sue in counties<sup>353</sup> or precincts<sup>354</sup> other than the consumer's residence.<sup>355</sup> Moreover, venue objections are waived if no objection is raised.<sup>356</sup> A defendant may request a change of venue where venue is improper,<sup>357</sup> but the court has no power to change venue sua sponte.<sup>358</sup> Thus, where the venue is so

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344. See *Cota v. Southern Arizona Bank & Trust Co.*, 17 Ariz. App. 326, 327, 497 P.2d 833, 834 (1972).

345. In Arizona a default may be entered when "a party against whom affirmative relief is sought has failed to plead or otherwise defend . . ." ARIZ. R. CIV. P. 55(a). Notice of an application for default judgment is required only when the defendant has made an earlier appearance in the action. *Id.* 55(b)(1); see *McClintock v. Serv-Us Bakers*, 103 Ariz. 72, 74, 436 P.2d 891, 893 (1968).

346. See *Mayhew v. McDougall*, 16 Ariz. App. 125, 130, 491 P.2d 848, 853 (1971); ARIZ. REV. STAT. ANN. § 22-218(2) (1975) (justice courts).

347. See ARIZ. REV. STAT. ANN. § 22-218(1) (1975) (justice courts); ARIZ. R. CIV. P. 8(c).

348. ARIZ. R. CIV. P. 8(c); see *Saylor v. Hawes*, 30 Ariz. 197, 200, 245 P. 354, 355 (1926).

349. See ARIZ. R. CIV. P. 55(c), 60(c).

350. See *Phillips v. Findlay*, 19 Ariz. App. 348, 353-54, 507 P.2d 687, 692-93 (1973).

351. The comment to section 5.115 of the revised U3C indicates that the broadly worded provision bestowing on inferior courts the jurisdiction to reopen default judgments is especially aimed at relief from sewer service. Arizona appears to allow relief at least in this particular situation. The Arizona supreme court has held that a trial court did not abuse its discretion in setting aside a default judgment on the ground that the defendant had not been served. *Eldridge v. Jagger*, 83 Ariz. 150, 153, 317 P.2d 942, 944 (1957). Although not a matter of statute, Arizona justice courts already have the power to set aside a default. See C. SMITH, *supra* note 343, at § 137.

352. ARIZ. REV. STAT. ANN. § 12-401 (Supp. 1975-76); *id.* § 22-202 (1975) (justice courts).

353. ARIZ. REV. STAT. ANN. §§ 12-401(4)-(6), (11) (Supp. 1975-76); see *Ellsworth v. Layton*, 97 Ariz. 115, 118-19, 397 P.2d 450, 452-53 (1964).

354. ARIZ. REV. STAT. ANN. §§ 22-202(C)-(D) (1975) (justice courts); see C. SMITH, *supra* note 343, at § 116.

355. Additionally, there is nothing in Arizona law to limit or prevent contract provisions setting venue in places other than the consumer's residence. For the problems such venue agreements create, see text & note 330 *supra*.

356. See *Sil-Flo Corp. v. Bowen*, 98 Ariz. 77, 83, 402 P.2d 22, 26 (1965); C. SMITH, *supra* note 343, at § 116.

357. See ARIZ. REV. STAT. ANN. § 12-404 (1956); *id.* § 22-204 (1975) (justice courts).

358. *Cf. Pride v. Superior Court*, 87 Ariz. 157, 161, 348 P.2d 924, 927 (1960) (if action brought in proper county, court has no jurisdiction to change venue). See generally *Butterfield v. Hatch*, 85 Idaho 527, 381 P.2d 285 (1963); *Bartell v. State Highway Comm'n*, 191 Kan. 539, 382 P.2d 334 (1963).

inconvenient as to prevent the debtor's presence, no objection can or will be raised. Arizona law does offer some protection in the area of confessed judgments.<sup>359</sup> In this regard, then, adoption of the revised U3C would preserve the Arizona position, which is consistent with the trend nationally.<sup>360</sup> However, the revised U3C provisions placing venue at the debtor's residence and requiring specificity in the complaint represent a marked improvement over current Arizona law.

### *Collections*

Horror stories associated with collection practices abound.<sup>361</sup> Although greater regulation of collection tactics has long been urged,<sup>362</sup> the original U3C did little to correct the problem. It did, however, attempt to facilitate prosecution<sup>363</sup> of persons violating the federal Extortionate Credit Transactions Act.<sup>364</sup> This was done by providing one of the elements required for a prima facie case of extortion under the federal law, namely, that repayment of credit extended under the proscribed conditions be unenforceable through civil judicial processes.<sup>365</sup> However, protections against abusive collection practices should not be limited to a federal law which is unique in its national character and its focus on organized crime.<sup>366</sup> The less exotic matter of local collection abuses also requires remedial measures. Under the original U3C there was a provision allowing public actions against creditors to restrain fraudulent or unconscionable conduct in the collection of debts.<sup>367</sup> However, no specific restrictions were placed on creditor conduct,<sup>368</sup>

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359. Arizona prohibits confessions of judgment prior to default on a debt. ARIZ. REV. STAT. ANN. § 44-143 (1956). Additionally, small loan licensees are prohibited from taking any confession of judgment or power of attorney. *Id.* § 6-629(1) (1974). These Arizona statutes apply broadly and, were the revised U3C adopted, they would continue to have effect outside the consumer context.

360. See FTC Credit Practices Rule, *supra* note 12, at § 444.2(l); NCCF REPORT, *supra* note 4, at 26.

361. See Note, *Mental Distress from Collection Activities*, 17 HASTINGS L.J. 369 (1965); Comment, *Collection Capers: Liability for Debt Collection Practices*, 24 U. CHI. L. REV. 572 (1957). See also Sherwin, *Locating the Missing Judgment Debtor*, 21 PRAC. LAW. 13 (1975).

362. The NCA included an entire article devoted to the subject of debt collection. NCA, *supra* note 240, §§ 7.101-.303. See generally Note, *supra* note 361.

363. U3C § 5.107 & Comments (1968).

364. 18 U.S.C. §§ 891-896 (1970).

365. See U3C § 5.107 & Comment 2 (1968). The proscribed conditions were an interest rate exceeding 45 percent and the creditor's reputation for the use of violence in collections. *Id.* § 5.107(2).

366. See *Perez v. United States*, 402 U.S. 146, 155-56 (1971); Boyd, *supra* note 47, at 173.

367. U3C § 6.111(1)(c) (1968).

368. Compare *id.* with NCA, *supra* note 240, § 7.201 (unauthorized practice); *id.* § 7.202 (threats of coercion); *id.* § 7.203 (harassment, abuse); *id.* § 7.204 (unreasonable publication); *id.* § 7.205 (fraudulent, deceptive, or misleading representations); and *id.* § 7.206 (unfair or unconscionable means). See also MCCA, *supra* note 240, §§ 6.101-207.

and no provision was made for private actions.<sup>369</sup> Even the provision for public actions was available only against a creditor engaging in an unconscionable course of conduct.<sup>370</sup>

To the credit of the drafters, the original U3C did address the problem of wage garnishment as a collection device. In line with the decision in *Sniadach v. Family Finance Corp.*,<sup>371</sup> prejudgment garnishment of wages was prohibited.<sup>372</sup> The U3C also placed a stricter limitation on the total amount of wages subject to postjudgment garnishment than is contained in federal law.<sup>373</sup> Finally, the discharge of employees due to wage garnishments stemming from a consumer transaction was prohibited.<sup>374</sup> The U3C thus improved upon federal efforts to alleviate the problem of garnishment.<sup>375</sup> However, neither the U3C nor the federal law provided for an effective enforcement scheme, nor came to grips with the burden-of-proof problem inherent in a proscription of firings "by reason of garnishment."<sup>376</sup>

The revised U3C retains and expands the protections provided in the original text,<sup>377</sup> especially with respect to wage garnishment. In addition to prohibiting prejudgment garnishment,<sup>378</sup> discharge of the garnishee,<sup>379</sup> and garnishments exceeding a certain amount,<sup>380</sup> the revised U3C contains a provision allowing special court relief from postjudgment wage garnishment.<sup>381</sup> This provision, added in response to a recommendation of the National Commission on Consumer Finance,<sup>382</sup> allows a court upon receipt of a verified application to exempt for an appropriate period of time such normally nonexempt earnings as are

369. See U3C § 6.111(1)(c) (1968); Spanogle, *The U3C—It May Look Pretty, But Is It Enforceable?*, 29 OHIO ST. L.J. 624 (1968).

370. Compare U3C § 6.111(1) (1968) with NCA, *supra* note 240, § 7.206.

371. 395 U.S. 337 (1969).

372. U3C § 5.104 (1968); see Johnson, *supra* note 209, at 1123; Robertson, *supra* note 202, at 70.

373. Compare U3C § 5.105 (1968) with 15 U.S.C. § 1673(a) (1970). See generally Boyd, *supra* note 47, at 192-93. See text & note 380 *infra*.

374. U3C § 5.106 (1968). Violation of this provision subjected the employer to civil liability for lost wages and reinstatement of the discharged employee. *Id.* § 5.202(6).

375. See 15 U.S.C. § 1674 (1970); Robertson, *supra* note 202, at 73-74.

376. See Boyd, *supra* note 47, at 194.

377. For instance, the protections against unconscionability are continued, U3C §§ 5.108, 6.111 (1974); see text & notes 367-70 *supra*, with the administrative protection still contingent on a course of conduct by the creditor. U3C §§ 6.111(1)-(2) (1974). However, a private right of action against unconscionable conduct has been added. See text & notes 447-56 *infra*; 369-70 *supra*.

378. U3C § 5.104 (1974).

379. *Id.* § 5.106.

380. *Id.* § 5.105. The amount is the same as that contained in the 1968 version; the lesser of 25 percent of the employee's disposable weekly earnings or the amount by which his weekly earnings exceed 40 times the federal minimum wage. *Id.*; *id.* § 5.105 (1968). The amount is increased from the federal figure of 30 times the minimum hourly wage, 15 U.S.C. § 1673(a)(2) (1970), "in the belief that the higher figure is justified in consumer credit transactions . . ." U3C § 5.105, Comment 1 (1974).

381. See U3C § 5.105(4) (1974).

382. *Id.* § 5.105, Comment 5; see NCCF REPORT, *supra* note 4, at 33.

necessary for the maintenance of the debtor or a family supported by his earnings.<sup>383</sup> This section goes beyond the minimum due process demands on which *Sniadach* rested to protect the minimum income essential to survival.

Following *Sniadach*, the Arizona supreme court held that Arizona's garnishment laws were deficient insofar as they permitted prejudgment wage garnishments without a hearing.<sup>384</sup> The decision was narrow, being expressly restricted to wage garnishment.<sup>385</sup> More troublesome yet, the opinion seemed to invite creditors to remedy the statute's due process deficiencies simply by alleging that a determination on the merits had been made.<sup>386</sup> To the extent that garnishment was permitted pursuant to such a showing, there resulted a rather remarkable degree of judicial and administrative amendment of the state's garnishment law.<sup>387</sup> The legislature has recently responded to these developments and has revised the Arizona wage garnishment laws.<sup>388</sup> The amended law adopts the U3C position and prohibits prejudgment garnishment of wages.<sup>389</sup> Given the special significance of wages and the severe impact of remedies that effect the economic lifeblood of the debtor,<sup>390</sup> the new Arizona position, one recommended by the National Commission on Consumer Finance,<sup>391</sup> is commendable.

The Arizona wage garnishment law also has been revised in other respects. Personal earnings are now exempt from garnishment to the

383. U3C § 5.105(4) (1974). The comment to this subsection indicates that this relief is intended for unusual circumstances, such as illness or an abnormally large number of dependents. See *id.* § 5.105, Comment 5.

384. *Termplan, Inc. v. Superior Court*, 105 Ariz. 270, 463 P.2d 68 (1969).

385. *Id.* at 272, 463 P.2d at 70; see *Roofing Wholesale Co. v. Palmer*, 108 Ariz. 508, 502 P.2d 1327 (1972) (upholding Arizona's replevin law). But see *Thornton v. Carson*, 111 Ariz. 490, 533 P.2d 657 (1975) (holding the Arizona replevin law invalid).

386. The opinion affirmed the superior court clerk's requirement that "some showing be made . . . that the writs were not to be levied on wages . . . prior to a determination of the alleged claim on the merits." *Termplan, Inc. v. Superior Court*, 105 Ariz. 270, 272, 463 P.2d 68, 70 (1969).

387. This was especially true since the Arizona statute not only failed to require a hearing, but also prohibited notice that a writ of garnishment had been issued until the writ was served. See Ariz. Rev. Stat. Ann. § 12-1575 (1956) (repealed, effective Sept. 1, 1976). See also *Termplan, Inc. v. Superior Court*, 105 Ariz. 270, 272, 463 P.2d 68, 70 (1969).

388. Ch. 170, [1976] Ariz. Sess. Laws 786 (effective Sept. 1, 1976). In fact, the whole range of creditors' provisional remedies, defined to include attachment, garnishment, and replevin, *id.* § 1 (12-2401(3)), has been revised. See text & notes 411-25 *infra*.

389. Ch. 170, § 1 (12-2401(3)), 14 (12-571(A)), [1976] Ariz. Sess. Laws 786, 795. By specifically exempting garnishment of wages from the definition of provisional remedies, *id.* § 1 (12-2401(3)), wage garnishment remains available only "[w]hen any party in an action has been awarded a money judgment." *Id.* § 14 (12-1571(A)(2)).

390. "The idea of wage garnishment in advance of judgment, of trustee process, of wage attachment, or whatever it is called is a most inhuman doctrine. It compels the wage earner, trying to keep his family together, to be driven below the poverty line." *Sniadach v. Family Finance Corp.*, 395 U.S. 337, 340 (1969), quoting Representative Henry S. Reuss, 114 CONG. REC. 1832 (1968).

391. U3C § 5.104, Comment (1974).

same extent as wages are protected under federal law.<sup>392</sup> This revision represents a definite improvement over prior Arizona law which exempted only one-half of the debtor's earnings.<sup>393</sup> Nevertheless the amount of wages subject to garnishment still exceeds the protection recommended by the National Commission of Consumer Finance,<sup>394</sup> and this increased level of protection, afforded by the U3C,<sup>395</sup> would be preferable. The Arizona law remains inferior in certain other areas as well. There is no provision for postjudgment relief based on need. The Arizona act also contains no prohibition on discharges stemming from garnishment.<sup>396</sup> Although a recent circuit court of appeals decision will put some teeth into the federal prohibition of discharges based on a single garnishment,<sup>397</sup> there is still no federal protection against multiple-garnishment discharges.<sup>398</sup>

The revised U3C by and large does not address prejudgment collection problems other than those associated with wages. Decisions beginning with *Fuentes v. Shevin*<sup>399</sup> have left the validity of prejudg-

392. Compare ch. 170, § 24 (33-1131(B)), [1976] Ariz. Sess. Laws 800, with 15 U.S.C. § 1673(a) (1970) (both provisions limiting garnishment to the lesser amount of 25 percent of the employee's weekly disposable earnings or the amount by which his weekly earnings exceed 30 times the federal minimum hourly wage). See generally Boyd, *supra* note 47, at 192-93. It may be of interest to note that a Michigan court has recently held that the amount of wages that may be garnished under federal law must be reduced by the amount of any debt owed to the employer since the garnishee may claim a set off to the extent of the debt. *Sears, Roebuck & Co. v. A.T. & G. Co.*, 66 Mich. App. 359, 239 N.W.2d 614 (1976). Compare *id.* with *Sandra Dev. Corp. v. Allen*, 86 Ariz. 40, 340 P.2d 193 (1959).

393. Ch. 172, § 94, [1973] Ariz. Sess. Laws 1711, as amended, ch. 170, § 23 (33-1126), [1976] Ariz. Sess. Laws 799. See generally Jury, *Arizona's Exemption Statute Relative to Earnings for Personal Services: Time for Modernization*, 6 ARIZ. L. REV. 257 (1965). The revised exemption does not apply in the case of a court order for support for any person; in such cases, one-half of the disposable earnings are protected. Ch. 170, § 23 (33-1131(C)), [1976] Ariz. Sess. Laws 800.

A problem of statutory construction may well present itself with use of the revised exemption law. The increased protection for wages is contained in an amendment to the exemption laws. *Id.* § 23 (33-1131). Still codified in the wage garnishment section, however, is a provision exempting only one-half of the debtor's earnings. ARIZ. REV. STAT. ANN. § 12-1594 (1956).

394. U3C § 5.105, Comment 1 (1974).

395. *Id.* § 5.105. See discussion note 363 *supra*.

396. It is interesting to note that the law, as revised, deletes a qualification on the grounds for issuance of a writ of garnishment, namely "that the garnishment applied for is not sued out to injure . . . defendant . . ." Compare Ariz. Rev. Stat. Ann. § 12-1571 (1956) with ch. 170, § 14, [1976] Ariz. Sess. Laws 794.

397. In *Stewart v. Travelers Corp.*, 503 F.2d 108 (9th Cir. 1974), the court held that an employer discharged in violation of the Consumer Credit Protection Act single-garnishment discharge prohibition may bring a private action for reinstatement, back pay, and damages. See 15 U.S.C. § 1674 (1970).

398. The effects of multiple garnishment and the resultant creditor leverage are discussed in Jury, *supra* note 393, at 261, 265. To solidify the protection against severe disruption of a debtor's income, and to assure an opportunity for judicial determination of a debt before unpaid earnings are taken, the revised U3C also prohibits irrevocable wage assignments. U3C § 3.305 (1974). There is no such prohibition, however, in Arizona law. *But cf.* ARIZ. REV. STAT. ANN. § 6-631 (1974). It has been held that wage assignments are not affected by the federal limitations on wage garnishment. *Western v. Hodges*, 494 F.2d 379 (4th Cir. 1974).

399. 407 U.S. 67 (1972).

ment replevin and attachment laws in most jurisdictions in doubt.<sup>400</sup> A subsequent decision, *Mitchell v. W.T. Grant*,<sup>401</sup> added to the uncertainty by raising doubts about the continuing validity of *Fuentes*.<sup>402</sup> In Arizona the situation was even more confused because the Arizona supreme court refused to follow the *Fuentes* decision on the ground that the decision was rendered by less than a majority of the Supreme Court.<sup>403</sup> The Arizona court was vindicated temporarily by the Court's subsequent decision in *Mitchell*.<sup>404</sup> However, the United States Supreme Court has recently indicated that the *Mitchell* decision did not undermine *Fuentes* as much as had been suspected. In *North Georgia Finishing, Inc. v. Di-Chem, Inc.*,<sup>405</sup> the Supreme Court invalidated a Georgia garnishment law which permitted a writ to be issued prior to judgment in a suit against a corporation.<sup>406</sup> This time it was *Mitchell* that was distinguished,<sup>407</sup> leading Justice Stewart to remark, "It is gratifying to note that my report of the demise of *Fuentes v. Shevin* . . . seems to have been greatly exaggerated."<sup>408</sup> The Arizona court was now persuaded, and in *Thornton v. Carson*<sup>409</sup> it finally declared Arizona's replevin statute<sup>410</sup> unconstitutional for failure to meet the demands of *Mitchell* and *Di-Chem*.

The net result of this body of case law is that Arizona's attachment, garnishment, and replevin laws were constitutionally infirm, and filling the resulting gaps in the law of prejudgment remedies became a task for the state legislature. The Arizona legislature has recently performed this task by overhauling the so-called "provisional remedies" of attachment, garnishment, and replevin,<sup>411</sup> and adding a chapter providing for notice and an opportunity to be heard.<sup>412</sup> Except in limited circum-

400. See A. LaFRANCE, *supra* note 172, § 124, at 82, § 128, at 94.

401. 416 U.S. 600 (1974).

402. In *Mitchell* the Supreme Court upheld a Louisiana sequestration law which provided for issuance of a writ on petition and affidavit without notice or a hearing. Justice Powell, concurring, asserted "I think it fair to say that the *Fuentes* opinion is overruled." 416 U.S. at 623. Three dissenting Justices objected to "[a] basic change in the law upon a ground no firmer than a change in [the Court's] membership . . ." 416 U.S. at 636.

403. Roofing Wholesale Co. v. Palmer, 8 Ariz. 508, 502 P.2d 1327 (1972).

404. *But see* Manning v. Palmer, 381 F. Supp. 713 (D. Ariz. 1974), wherein a three-judge court declared Arizona's attachment and garnishment statutes, Ariz. Rev. Stat. Ann. §§ 12-1521 to -1539 (1956); *id.* §§ 12-1571 to -1604 (1956), as amended, (Supp. 1975-76) (partially repealed, effective Sept. 1, 1976), invalid despite *Mitchell*, and permanently enjoined the practice of issuing writs of garnishment and attachment prior to judgment.

405. 419 U.S. 601 (1975).

406. *Id.* at 606.

407. *Id.* at 606-07.

408. *Id.* at 608 (concurring opinion).

409. 111 Ariz. 490, 533 P.2d 657 (1975).

410. ARIZ. REV. STAT. ANN. §§ 12-1301 to -1314 (1956).

411. Ch. 170, § 1 (12-2401(3)), [1976] Ariz. Sess. Laws 786.

412. *Id.* § 1 (12-2401 to -2412). In certain limited situations, such as where the debtor is leaving the state without securing the debt or has secreted or disposed of

stances,<sup>413</sup> no provisional remedy may be issued until the creditor has made an application to the court setting forth under oath the factual and legal grounds for the claim;<sup>414</sup> the debtor is given notice of the creditor's claim and of the right to request a hearing within 10 days;<sup>415</sup> and such a hearing, held within 5 days of debtor's request for it,<sup>416</sup> concludes that there is "probable cause to believe the claim of the [creditor] is valid;"<sup>417</sup> or there is a failure of the debtor to request a hearing within the prescribed time.<sup>418</sup> This scheme, especially this last qualification regarding failures of debtors to request hearings, may tend to limit the positive effect of the hearing provision, particularly as to low-income

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property in order to defraud creditors, a provisional remedy may be issued without notice. *Id.* § 1 (12-2402(A)). Even in these circumstances, however, the creditor must "establish with particularity by affidavit to the court's satisfaction sufficient facts supporting [his] claim and establish that one of the [limited situations, delineated in section 12-2402(A)] has been met . . ." *Id.* § 1 (12-2402(B)). Further, a creditor must exercise reasonable diligence to serve notice on the debtor of the seizure, *id.* § 1 (12-2402(D)), and of the debtor's right to request an immediate hearing in order to quash the seizure order. *Id.* § 1 (12-2402(D)-(E)). The provision for an immediate hearing limits the hearing to the "probable validity" of the claim of the party seeking the provisional relief, "any defenses and claims of personal property exemptions of the party against whom such provisional remedy will operate," and the existence of any statutory requirement for issuance of the remedy. *Id.* § 1 (12-2402(C)). To avoid an argument that this hearing limitation is inconsistent with the demands of due process, and, in any event, to give the section its probable intended meaning, the word "defense" should be interpreted to include claims of the debtor asserted by way of recoupment. There are numerous decisions to the effect that a claim based upon a truth-in-lending violation is sufficiently related to the debt action to avoid the 1-year statute of limitations imposed by the federal law on such claims insofar as recoupment is concerned. *See Collector's, Inc. v. Atrisco Ass'n*, [1974-76 Transfer Binder] CCH POVERTY LAW REP. ¶ 19,211 (N.M. Dist. Ct. 1974); *First Nat'l Bank v. Drake*, [1969-73 Transfer Binder] CCH CONSUMER CREDIT GUIDE ¶ 98,939 (N.Y. Civ. Ct. 1973). *See also* text accompanying note 543 *infra*.

It should be noted, however, that the new chapter does specifically afford a provisional remedy in the nature of replevin without notice where the remedy is sought "to enforce a security interest in consumer goods which is . . . a purchase money security interest." *Id.* § 1 (12-2402(A)(2)). This exception may raise questions. In such cases there is a right to a post-seizure hearing on demand, *id.* § 1 (12-2402(D)-(E)), and notice is apparently required as to exempt property. *See* discussion note 435 *infra*.

413. *See* discussion note 412 *supra*.

414. Ch. 170, § 1 (12-2403(2), -2404), [1976] Ariz. Sess. Laws 788.

415. *Id.* § 1 (12-2403(2), -2405 to -2406). Further protection is afforded the debtor by the requirement that the actual notice of the creditor's claim be accompanied by additional notice proclaiming in English and Spanish: "Notice! A lawsuit has been filed against you. In order to protect your rights, please read carefully the other papers which were served upon you with this notice!" *Id.* § 1 (12-2406(C)).

416. *Id.* § 1 (12-2410(B)).

417. *Id.* § 1 (12-2410(D)). The hearing is limited to the issues of the "probable validity" of the applicant's claims and any defenses or exemption claims of the debtor, and the existence of any statutory requirements for issuance. *Id.* § 1 (12-2410(C)). For a discussion of the proper interpretation of "defenses," see discussion note 412 *supra*. The court's determination is based on a "probable cause" standard of proof. *Id.* § 1 (12-2410(D)).

It is interesting to note that in the proposed provision the second allowable issue was "[t]he probable existence of any statutory requirements for the issuance of any provisional remedies sought." S. 1243, 32d Ariz. Legis., 2d Reg. Sess. § 1 (12-2410(C)(2)) (1976). The deletion of "probable" in the enacted statute clearly sets out a more stringent test, but raises questions about certainty of proof.

418. *Id.* § 1 (12-2408). A remedy may be issued upon default only on determination by a judge or justice of the peace that the procedural requirements have been met and the creditor's claims are valid. *Id.* § 1 (12-2409).

debtors who rather routinely fail to take full advantage of their legal rights. However, any such tendency is somewhat offset by the provision allowing attorneys' fees to be awarded to parties who successfully challenge the issuance of a provisional remedy.<sup>419</sup>

Arizona's new provisional remedy scheme appears to meet the demands of due process. In particular, the fact that a judge or justice of the peace must make the final determinations on probable cause and the requirements of affidavits under oath stating facts sufficient to show a claim is valid satisfy the essential judicially imposed requirements.<sup>420</sup> The instances in which process may be issued under the new Arizona law without notice or a preissuance hearing seem within due process guidelines, given the provision for prompt judicial review by motion to quash.<sup>421</sup>

In matters other than wage garnishment, the prejudgment process problem transcends the consumer setting,<sup>422</sup> and the solution must be aimed at the general rather than the specific problem. To the extent that the solution affects consumers, the protection afforded must be weighed against the possibility that restrictions on remedies may increase finance charges and decrease the availability of credit.<sup>423</sup> The Arizona response appears satisfactory given these considerations and the constraints of due process. Since the revised U3C does not deal with the problem of provisional remedies except to limit wage garnishments,<sup>424</sup> adoption of the U3C would result in peaceful coexistence of the revised Arizona law on provisional remedies and the superior protec-

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419. Ch. 170, § 1 (12-2411), [1976] Ariz. Sess. Laws 791. There is some danger that the right of the creditor to claim attorneys' fees will inhibit debtors from asking for hearings. But paying attorneys' fees is already a risk borne by debtors, and statutory limitations on the amounts awarded will reduce the risk correspondingly. See text & notes 107-23 *supra*. Moreover, if the U3C option to bar attorneys' fees were to be adopted, U3C § 2.507 (Alt. A) (1974); see text accompanying notes 111-15 *supra*, the risk would be removed. Even if attorneys' fees are otherwise collectible it could be argued that the provision for an award to the party against whom the provisional remedy was issued or sought inferentially negatives an award of attorneys' fees to a creditor who is successful at the hearing.

420. See *North Georgia Finishing, Inc. v. Di-Chem, Inc.*, 419 U.S. 601, 607 (1975); *Mitchell v. W.T. Grant*, 416 U.S. 600, 615-17 (1974); *Fuentes v. Shevin*, 407 U.S. 67, 92-93 (1972); *Thornton v. Carson*, 111 Ariz. 490, 492, 533 P.2d 657, 659 (1975). In *United States Gen., Inc. v. Arndt*, 45 U.S.L.W. 2081 (E.D. Wis. Aug. 4, 1976), the court in striking down a recently enacted Wisconsin attachment law specifically referred to the statute's failure to require the pleading of facts supporting conclusions contained in an affidavit.

421. Ch. 170, § 1 (12-2402(C)), [1976] Ariz. Sess. Laws 786. The demands of the Supreme Court decisions left some room for the issuance of process followed by an immediate postseizure hearing. See *North Georgia Finishing, Inc. v. Di-Chem, Inc.*, 419 U.S. 601, 606-07 (1975); *Mitchell v. W.T. Grant*, 416 U.S. 600, 618 (1974).

422. The debtor in *Di-Chem* was a corporation. Justice White, in his opinion for the Court, refused an invitation to distinguish consumer debtors from other debtors on the basis of the type and degree of injury suffered. See 419 U.S. at 608. The debtors in *Thornton v. Carson*, 111 Ariz. 490, 533 P.2d 657 (1975), were commercial buyers. See *id.* at 490, 533 P.2d at 657. See generally A. LAFRANCE, *supra* note 172, § 128, at 94.

423. See NCCF REPORT, *supra* note 4, at 34.

424. See text & notes 371-83 *supra*.

tion afforded by the U3C wage garnishment provisions, which would be understood to apply in the consumer context.<sup>425</sup>

The fact that the provisional remedies problem transcends the consumer context may explain the absence of U3C provisions directed to the problem beyond the matter of wage garnishment. There is less to be said, however, in defense of the U3C's failure to deal with the general problem of exemptions from execution. As noted, the original U3C exempted from garnishment all wages prior to judgment,<sup>426</sup> and certain amounts of wages after judgment.<sup>427</sup> The original U3C also denied execution insofar as necessary to preserve the requirement that a creditor must choose between repossession and a deficiency in consumer credit sales of items sold for \$1000 or less.<sup>428</sup> In contrast, the National Consumer Act, responding to demands for reform,<sup>429</sup> went much farther to exempt specifically household furnishings, appliances, clothing, and such other property as necessary for the maintenance of a moderate standard of living.<sup>430</sup> Despite this more advanced precedent, however, the revised U3C simply duplicates the exemption provisions of its predecessor,<sup>431</sup> otherwise accepting the exemption laws as they presently exist in the respective state.<sup>432</sup> This omission in the U3C is a serious one; however, the Arizona legislature has recently acted to revise its formerly antiquated exemption laws,<sup>433</sup> and that revision<sup>434</sup> will serve to mitigate what would otherwise be a serious objection to the adoption of the revised U3C. Very significant in the reform is the addition of a provision making waiver of exemption rights void.<sup>435</sup> Exemption laws

425. A legislature seeking to provide due process protection for all consumer credit transactions might consider employing section 5.116 of the revised U3C as a model. See text & notes 221-26 *supra*. Section 5.116 allows a supervised lender to reach certain collateral only after notice and a hearing. Its protection thus extends beyond the problem of legal process to limit self-help remedies. See U3C § 5.116 (1974).

426. U3C § 5.104 (1968) (no garnishment of wages before judgment). See also *id.* §§ 2.410, 3.403 (no assignment of earnings).

427. See *id.* § 5.105; text & notes 373, 380 *supra*.

428. See U3C § 5.103(6)(b) & Comment 6 (1968). See text & notes 300-01 *supra*.

429. See, e.g., Joslin, *Debtors Exemption Laws: Time for Modernization*, 34 IND. L.J. 355 (1959).

430. NCA, *supra* note 240, § 5.106 & Comment; see MCCA, *supra* note 240, § 7.110.

431. See U3C § 3.305 (1974) (no assignment of earnings); *id.* § 5.104 (no garnishment before judgment); *id.* § 5.105 (limitation on garnishment).

432. See *id.* § 5.116(1)(c) & Comment 1.

433. Ariz. Rev. Stat. Ann. §§ 33-1121 to -1129 (1974) (partially repealed 1976). Among those items formerly exempted were "[o]ne horse with vehicle or harness or other equipments . . . used by a surgeon, physician, constable or clergyman in the legitimate practice of his profession." *Id.* § 33-1124(11).

434. Ch. 170, §§ 21-24, [1976] Ariz. Sess. Laws 797-800.

435. *Id.* § 24 (33-1132). The concluding phrase of the enacted provision (here italicized) may cause some confusion: "Notwithstanding any agreement to the contrary, a waiver of the exemption rights provided by this article shall be void and unenforceable, except as specifically provided in section 33-1122 and when done with notice." This final phrase, "and when done with notice," was added in an amendment to the proposed bill. Compare S. 1243, 32d Ariz. Legis., 2d Reg. Sess. § 27 (33-1132) (1976), with ch. 170, § 24 (33-1132), [1976] Ariz. Sess. Laws 799. Since the intent of the originally proposed provision was to prohibit contractual waivers of afforded exemption rights, the

involve a number of difficult theoretical and practical problems.<sup>436</sup> The new Arizona provisions employ a combined specified assets and fair market value approach.<sup>437</sup> While one might quarrel with the amounts chosen, by and large the revisions are a welcome improvement.

### UNCONSCIONABILITY, REFERRAL SALES SCHEMES, AND HOME SOLICITATION SALES

Among the more significant changes made by the revised U3C are those directed to unconscionability, referral sales schemes, and home solicitation sales.

#### *Unconscionability*

The UCC expressly made unconscionability a limitation on commercial sales arrangements,<sup>438</sup> including consumer sales contracts.<sup>439</sup> Much litigation and commentary followed,<sup>440</sup> with a considerable amount of discussion being directed to the meaning of unconscionability,<sup>441</sup> which was undefined in the Code.<sup>442</sup> Although this lack of definition provided the courts with a needed flexibility, it also caused uncertainty<sup>443</sup> and may have made some courts hesitant to utilize the doctrine. The original U3C made unconscionability explicitly applica-

amendment of the provisions by the final phrase should not be read to reduce the intended protection. Indeed, a logical reading of the provision as enacted makes the waiver prohibition even more protective. Under such a reading one would conclude that since section 33-1122 declares all secured property nonexempt from process, thereby making such property subject to process with or without a waiver, section 33-1132's exception for secured property would be superfluous unless the phrase, "and when done with notice," qualifies the secured party's right to reach secured property. Thus, under section 33-1132, as enacted, secured parties may not be able to reach even secured property without having provided notice. It is not indicated what notice is required, but arguably notice as provided for in *id.* § 1 (12-2405 to -2406) is necessary.

Protection such as Arizona has afforded through prohibition of contractual waiver or limitation on exemption rights is the recommended trend. See FTC Credit Practices Rule, *supra* note 12, at § 444.2(2).

436. See, e.g., Countryman, *For a New Exemption Policy in Bankruptcy*, *RUTGERS L. REV.* 678 (1960); Joslin, *supra* note 429; Karlen, *Exemption from Execution*, 22 *BUS. LAW.* 1167 (1967).

437. See ch. 170, §§ 21-24, [1976] *Ariz. Sess. Laws* 797-800. Among the important improvements with respect to specified assets are the exemptions for motor vehicles, *id.* § 24 (33-1130(4), (7)), and a total of \$100 held in a single bank account. *Id.* § 23 (33-1126(7)).

438. UCC § 2-302.

439. *Id.*; see Boyd, *supra* note 4, at 374, 383-84.

440. See, e.g., Williams v. Walker-Thomas Furniture Co., 350 F.2d 445 (D.C. Cir. 1965); Henningsen v. Bloomfield Motors, Inc., 32 N.J. 358, 161 A.2d 69 (1960); W. HAWKLAND, *A TRANSACTIONAL GUIDE TO THE UNIFORM COMMERCIAL CODE* 44-47 (1964); A. LAFRANCE, *supra* note 172, at § 107.

441. See A. LAFRANCE, *supra* note 172, § 107, at 26-28. See generally J. WHITE & R. SUMMERS, *supra* note 160, at §§ 4-2 to -7.

442. Most courts applying the unconscionability doctrine have based their decisions on the criteria contained in the UCC comment: oppression and unfair surprise. See UCC § 2-302, Comment 1; A. LAFRANCE, *supra* note 172, § 107, at 27-30.

443. See A. LAFRANCE, *supra* note 172, § 107, at 26-31; J. WHITE & R. SUMMERS, *supra* note 160, at §§ 4-2 to -7.

ble to loans and leases as well as to sales;<sup>444</sup> however, in other respects it duplicated the UCC provision.<sup>445</sup> No elaboration was made on the meaning of unconscionability except in the context of relief through actions of the administrator.<sup>446</sup> The revised U3C significantly expands the availability of the unconscionability concept. For example, it provides for a private remedy for a consumer who was led unconscionably to believe a consumer credit transaction would arise,<sup>447</sup> and to a consumer induced to enter into a transaction by unconscionable conduct.<sup>448</sup> In effect, private relief is now available in cases of unconscionable conduct which were actionable under the original U3C only by the administrator,<sup>449</sup> but with the important improvement that no course of conduct is required.<sup>450</sup> Also, in a significant addition aimed at aiding courts and consumers in recognizing unconscionability, certain considerations that have been given weight by courts in finding contracts unconscionable are codified in the revised Code.<sup>451</sup>

As was true under the original U3C<sup>452</sup> the basic remedy available to consumers for unconscionability is nonenforcement of the contract.<sup>453</sup> However, actual damages may be recovered in cases of unconscionable debt collection practices.<sup>454</sup> As a further incentive to consumers, reasonable attorneys' fees may be recovered in any successful suit.<sup>455</sup>

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444. U3C § 5.108(1) (1968). Because the UCC provision is contained in the sales article, there has been some doubt regarding the use of the doctrine in loan transactions. See A. LAFRANCE, *supra* note 172, § 107, at 31.

445. Compare U3C § 5.108 (1968) with UCC § 2-302. The U3C provision could be viewed as tightening up the existing protection through its limitation that "a charge or practice expressly permitted by this Act is not in itself unconscionable." U3C § 5.108(3) (1968); cf. A. LAFRANCE, *supra* note 172, § 107, at 30-31.

446. Section 6.111, however, provided for administratively initiated relief against certain unconscionable behavior. See U3C § 6.111 (1968).

447. *Id.* § 5.108(1) (1974). Thus, for example, a seller could not bind a consumer to a short term sales contract payable in a lump sum, on the promise that financing could be secured, and then inform the consumer that financing was unavailable, keeping the downpayment or trade-in as a penalty for nonpayment. *Id.* § 5-108, Comment 1.

448. See *id.* § 5.108(1)(a) & Comment 1.

449. See *id.* § 5.108, Comment 2; *id.* § 6.111 (1968).

450. See *id.* § 5.108 & Comment 2 (1974).

451. *Id.* §§ 5.108(4)-(5) & Comments 3-5.

452. See *id.* § 5.108 (1968).

453. See *id.* § 5.108(1)(b) (1974). It might be advisable to revise this provision to instruct courts, while fashioning remedies, not to substitute reasonable terms for unconscionable terms in fashioning remedies for unconscionability: for instance, enforcing a reasonable price instead of the unconscionable price. If this type of remedy were utilized, creditors would have nothing to lose by using unconscionable terms. See *Frostifresh Corp. v. Reynoso*, 54 Misc. 2d 119, 281 N.Y.S.2d 964 (App. T. 1967); A. LAFRANCE, *supra* note 172, § 107, at 31-32; cf. U3C § 5.201, Comment 3 (1974).

454. U3C § 5.108(2) (1974). The availability of damages under the UCC provision, however, is uncertain. See *Vom Lehn v. Astor Art Galleries, Ltd.*, 18 UCC REP. SERV. 861 (N.Y. Sup. Ct. 1976) (rejecting a damage claim because section 2-302 makes no provision for damages, referring only to enforcement); *W.L. May Co. v. Philco-Ford Corp.*, 18 UCC REP. SERV. 599 (Ore. 1975) (reversing judgment for plaintiff without deciding damage claim issue).

455. See U3C § 5.108(6) (1974); cf. *Vom Lehn v. Astor Art Galleries, Ltd.*, 18 UCC REP. SERV. 861 (N.Y. Sup. Ct. 1976) (allowance of attorneys' fees in connection with a successful claim of rescission under the UCC's unconscionability provision).

However, to protect creditors against spurious litigation, attorneys' fees may be awarded to a creditor if a suit is determined to be knowingly groundless.<sup>456</sup>

Existing Arizona law on unconscionability stands where it was left by the UCC.<sup>457</sup> The adoption of the revised U3C, therefore, would further legitimize and clarify the doctrine and confirm its use in the consumer context, making unconscionability as defined by decisions in other jurisdictions and codified in the U3C clearly available to Arizona consumers. Moreover, the expanded consumer remedies would assist debtors wishing to raise the issue.

### *Referral Schemes*

Referral sale schemes have been the subject of increasing attack at the federal and state level.<sup>458</sup> Under these systems the seller offers a discount or rebate to the buyer contingent upon sales to prospective customers to whom the buyer has referred the seller.<sup>459</sup> The original U3C prohibited such schemes in the following terms:

With respect to a consumer credit sale or consumer lease the seller or lessor may not give or offer to give a rebate or discount or otherwise pay or offer to pay value to the buyer or lessee as an inducement for the sale or lease in consideration if [*sic*] his giving to the seller or lessor the names of prospective purchasers or lessees, or otherwise aiding the seller or lessor in making a sale or lease to another person, if the earning of the rebate, discount or other value is contingent upon the occurrence of an event subsequent to the time the buyer or lessee agrees to buy or lease.<sup>460</sup>

An agreement made in violation of this provision was unenforceable, and the consumer at his option could rescind the agreement or retain the goods or services without any obligation to pay for them.<sup>461</sup> This broadly stated protection and the uniquely dramatic remedy are retained in the revised U3C.<sup>462</sup> Moreover, the words "in consideration of" have

456. See U3C § 5.108(6) & Comment 5 (1974).

457. See ARIZ. REV. STAT. ANN. § 44-2319 (1967); Boyd, *supra* note 4, at 383-84. The only Arizona case interpreting this section involved a commercial rather than a consumer contract. See Raybond Electronics, Inc. v. Glen-Mar Door Mfg. Co., 22 Ariz. App. 409, 528 P.2d 160 (1974).

458. See A. LAFRANCE, *supra* note 172, § 103, at 11; Jordan & Warren, *supra* note 2, at 441-42; Comment, *Arizona's Home Solicitation and Referral Sales Act: An Evaluation and Suggestions for Reform*, 12 ARIZ. L. REV. 803, 815-16 (1970) [hereinafter cited as Comment, *Arizona's Home Solicitation and Referral Sales Act*]; Comment, *Let the "Seller" Beware—Another Approach to the Referral Sales Scheme*, 22 U. MIAMI L. REV. 861 (1968).

459. U3C § 2.411 & Comment 1 (1968); Boyd & Balentine, *supra* note 5, at 631-32.

460. U3C § 2.411 (1968).

461. *Id.*; see *id.*, Comment 3; Boyd & Balentine, *supra* note 5, at 632; Johnson, *supra* note 209, at 1125.

462. U3C § 3.309 (1974).

been omitted in the revised version to bring within the prohibition referral arrangements not specifically bargained for in a contract sense.<sup>463</sup> Further protection of consumers is accomplished through extension of the provision to preclude arrangements where the goods or services are to be paid for in whole or in part by the use of a credit card or financed by a lender subject to claims and defenses arising out of the sale or lease.<sup>464</sup> In such cases, the consumer has the same rights against the card issuer or lender that are available against the seller or lessor.<sup>465</sup> Finally, use of a referral scheme subjects a creditor to a penalty action.<sup>466</sup>

The treatment of referral arrangements by the U3C, especially by the revised U3C, is far superior to that contained in existing Arizona law. Arizona law prohibits referral arrangements defined in much the same terms as in the U3C;<sup>467</sup> however, there the similarity ends. The Arizona prohibition is limited to home solicitation sales of goods or services,<sup>468</sup> whereas the U3C provision applies to consumer credit sales and consumer leases generally.<sup>469</sup> The Arizona law does not by its terms preclude evasion of the proscription through the use of credit cards or consumer loans. Furthermore, the Arizona provision retains the "in consideration of" language deleted from the revised U3C, thus leaving open the possibility that it applies only to referral agreements specifically bargained for.<sup>470</sup> Also unclear is the consumer's remedy under this statute. Section 44-5003 makes a sale involving a referral scheme voidable, but it is not clear what action must be taken to void the sale.<sup>471</sup> Under the U3C the agreement is simply unenforceable and the consumer may secure a refund of any money paid or retain the goods or services without obligation.<sup>472</sup> The right to sue for a penalty as allowed in the revised U3C would further enhance the remedies available to Arizona consumers, as the Arizona statute grants no such right. Neither the U3C nor the Arizona law requires that a consumer be given notice of the referral sale prohibition or his rights in relation thereto.<sup>473</sup> If the protection against such schemes is to be effective, a notice requirement should be added in any adoption of the U3C.<sup>474</sup>

463. See *id.*; *id.*, Prefatory Note, at 92.

464. See *id.* §§ 3.309 & Comment 3, 3.405; *id.*, Prefatory Note, at 92.

465. See *id.* § 3.309 & Comment 3.

466. See *id.* § 5.201.

467. Compare ARIZ. REV. STAT. ANN. § 44-5003 (Supp. 1975-76) with U3C § 3.309 (1974).

468. See ARIZ. REV. STAT. ANN. §§ 44-5001(1), -5003 (Supp. 1975-76).

469. See U3C § 3.309 (1974); *cf.* Boyd & Balentine, *supra* note 5, at 631-32.

470. Compare ARIZ. REV. STAT. ANN. § 44-5003 (Supp. 1975-76) with U3C § 3.309 (1974) and *id.*, Prefatory Note, at 85.

471. See Boyd & Balentine, *supra* note 5, at 632.

472. See U3C § 3.309 (1974); Robertson, *supra* note 202, at 65.

473. See Boyd & Balentine, *supra* note 5, at 632; Comment, *Arizona's Home Solicitation and Referral Sales Act*, *supra* note 458, at 816.

474. *Cf.* U3C §§ 3.503, 5.116(2) (1974).

### *Home Solicitation Transactions*

As noted, the Arizona referral scheme prohibition applies only to home solicitation sales.<sup>475</sup> This limitation is illustrative of the recent trend toward subjecting home solicitation sales to special regulation on the theory that abuses are more likely to occur when the consumer is a captive in his home and the seller has no fixed local place of business.<sup>476</sup> Many such regulations have been modeled after the provisions contained in the original U3C,<sup>477</sup> the central feature of which is the "cooling-off period."<sup>478</sup> Under the original U3C the purchaser in a home solicitation sale<sup>479</sup> could cancel the sale agreement without cause within 3 days following the sale.<sup>480</sup> The seller was obligated to notify the buyer of the right to cancel, and any sale made without proper notice was ineffective.<sup>481</sup> Any written notice of cancellation by the purchaser sent to the address indicated in the creditor's agreement was sufficient if it expressed the consumer's intent not to be bound by the sale.<sup>482</sup>

The original U3C provisions were subject to several criticisms. For instance, the right of cancellation could be abrogated in emergency situations.<sup>483</sup> While the idea behind this exception was sound,<sup>484</sup> the provision itself was stated so broadly as to allow circumvention of the right.<sup>485</sup> Additionally, the right of cancellation was subject to a cancellation fee,<sup>486</sup> which could be viewed as penalizing and hence inhibiting exercise of the right conferred.<sup>487</sup> Other areas of criticism in-

475. See text accompanying note 468 *supra*.

476. See, e.g., LoPucki, *supra* note 5, at 342-43; Sher, *The "Cooling off" Period in Door-to-Door Sales*, 15 U.C.L.A.L. REV. 717 (1968); Comment, *Arizona's Home Solicitation and Referral Sales Act*, *supra* note 458, at 804 n.7.

477. See Miller & Warren, *1974 Uniform Consumer Credit Code*, 23 KAN. L. REV. 619, 644 (1975); cf. A. LA FRANCE, *supra* note 172, § 119, at 69.

478. See, e.g., A. LA FRANCE, *supra* note 172, § 119, at 69; Boyd & Balentine, *supra* note 5, at 629-30; Robertson, *supra* note 202, at 60-61; Comment, *Arizona's Home Solicitation and Referral Sales Act*, *supra* note 458, at 812-13.

479. For the definition of home solicitation sale, see U3C § 2.501 (1968). See also Comment, *Arizona's Home Solicitation and Referral Sales Act*, *supra* note 458, at 806-12.

480. U3C § 2.502(1) (1968); see LoPucki, *supra* note 5, at 343-44; Robertson, *supra* note 202, at 60.

481. U3C § 2.503 (1968); see Jordan & Warren, *supra* note 3, at 442-43; Robertson, *supra* note 202, at 61.

482. U3C §§ 2.502(2), (4) (1968); see Robertson, *supra* note 202, at 60.

483. See U3C § 2.502(5) (1968). Examples given of emergency situations included "emergency repairs to broken water pipes, furnaces, appliances and the like." *Id.*, Comment 3.

484. The exception appears intended primarily to protect repairmen of various types who perform their work in the home and whose transactions might therefore come within the definition of home solicitation sales. See *id.*

485. See U3C, Prefatory Note, at 93 (1974); Miller & Warren, *supra* note 3, at 14.

486. See U3C § 2.504(3) (1968). The fee was 5 percent of the cash price, but could not exceed the amount of the cash down payment. Thus, if there was no down payment, no fee was available to the seller. It was thought by the drafters that this limitation would lead to down-payment requirements by sellers, the existence of which would make consumers more hesitant to yield to high-pressure sales tactics. *Id.*, Comment 3.

487. Comment, *Arizona's Home Solicitation and Referral Sales Act*, *supra* note 458, at 825; cf. U3C, Prefatory Note, at 93 (1974).

involved uncertainty as to what use of the goods by a buyer would foreclose cancellation,<sup>488</sup> the narrowly defined scope of the right,<sup>489</sup> and the adequacy of the notice requirement.<sup>490</sup> Finally, the original U3C scheme was criticized for not expressly precluding the seller from including in the agreement a clause whereby the buyer waived his cancellation rights.<sup>491</sup>

The revised U3C continues the same basic home solicitation regulatory scheme,<sup>492</sup> but makes a number of improvements in the protection offered. To begin with, the scope of application is expanded to cover consumer credit sales at any residence, not just that of the buyer.<sup>493</sup> More importantly, coverage is extended to sales involving credit cards or consumer loans as to which the lender is subject to claims and defenses.<sup>494</sup> Possible jurisdictional confusion between the U3C and the federal law providing a right of rescission<sup>495</sup> is avoided by excluding sales subject to the federal rescission provision.<sup>496</sup> In other areas where there may be an overlap with federal law,<sup>497</sup> the federal rule will prevail and the administrator is empowered to promulgate rules bringing the U3C into compliance.<sup>498</sup>

Less justified, perhaps, is the Code's exclusion from coverage of sales conducted and consummated entirely by mail or telephone.<sup>499</sup> The rationale for this exception undoubtedly is that the prospects for untoward pressure that underlie the cooling-off-period notion are absent from sales by mail or over the telephone.<sup>500</sup> Such a conclusion, however, is at least debatable.<sup>501</sup>

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488. See U3C § 2.505 (1968) (imposing upon the cancelling buyer the duty to take reasonable care of the goods in his possession before cancellation and for a reasonable time thereafter); Miller & Warren, *supra* note 3, at 14.

489. See U3C § 2.501 (1968) (limiting home solicitation sales to those taking place at the buyer's own residence); Miller & Warren, *supra* note 3, at 14.

490. "Whereas the notice might be adequate to inform a middle class consumer of his rights, an uneducated low income buyer, who probably needs protection from door-to-door salesmen most of all, will probably not understand the notice." Robertson, *supra* note 202, at 61.

491. See Boyd & Balentine, *supra* note 5, at 630.

492. See U3C §§ 3.501-.505 (1974).

493. See *id.* § 3.501 & Comment 2.

494. See *id.* §§ 3.405, .501 & Comment 4.

495. 15 U.S.C. § 1635 (1970), *as amended*, (Supp. IV, 1974) (granting a right of rescission in any consumer credit transaction creating a security interest in real property used or to be used as the debtor's residence); see Boyd, *supra* note 47, at 188-92.

496. See U3C § 3.501 (1974).

497. See 16 C.F.R. § 429.1 (1976) (Federal Trade Commission rule), *discussed in* Boyd & Balentine, *supra* note 5, at 630-31.

498. See U3C §§ 3.501 & Comment 5, 6.104(1)(e) (1974); Miller & Warren, *supra* note 477, at 644.

499. See U3C § 3.501 (1974).

500. See *id.*, Comment 2.

501. Cf. Herbert, *Creditors Beware: Telephone Harassment May Be a Crime*, 29 PERS. FINANCE L.Q. REP. 42 (1975). Some of the concerns prompting home solicitation laws apply equally to telephone and mail solicitations: for instance, the seller's lessened need to maintain consumer good will, the consumer's limited knowledge about the seller

The revised U3C attempts to limit potential abuse of the emergency provision by requiring a separate, nonform statement signed by the buyer describing the emergency and requesting the seller to provide the goods or services without delay in order to safeguard the health, safety, or welfare of natural persons or to prevent damage to property.<sup>502</sup> Further protection to the buyer is afforded by the elimination of the cancellation fee,<sup>503</sup> the addition of a requirement that the buyer be given a copy of the notice of his right to cancel at the time the agreement is signed,<sup>504</sup> and by a new provision making it clear that "ordinary wear and tear or consumption of goods contemplated by the transaction" does not preclude cancellation.<sup>505</sup> The possibility that sellers will require buyers to waive their rights has not been addressed directly. It may be that the U3C home solicitation scheme, with an express exception only for emergencies, does not permit waivers. However, because actual use is being made of such waivers,<sup>506</sup> some express prohibition is needed, such as that contained in the Federal Trade Commission rules.<sup>507</sup> Therefore, if the U3C is adopted in Arizona, an explicit prohibition of these waivers should be added.

The revised U3C provisions regarding home solicitation sales would dramatically enhance protections currently available in Arizona. Rescission in Arizona continues to be governed primarily by the UCC<sup>508</sup> or common law.<sup>509</sup> Arizona has enacted a home solicitation sales law<sup>510</sup> modelled roughly after the original U3C, but the protection afforded pales by contrast to the original and especially the revised U3C.<sup>511</sup> The scope of the transactions covered by the Arizona law generally is comparable to that of the U3C,<sup>512</sup> and there is even an attempt to limit circumvention of cancellation rights by use of specially

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and product, and the consumer's susceptibility to impulse buying when approached in the home. See Comment, *Arizona's Home Solicitation and Referral Sales Act*, *supra* note 458, at 804 n.7.

502. U3C § 3.502(5) (1974).

503. *Id.* § 3.504.

504. *Id.* § 3.503(1).

505. *Id.* § 3.505(1); see Miller & Warren, *supra* note 3, at 14.

506. Boyd & Balentine, *supra* note 5, at 630 n.29 (use of waiver clauses in Arizona).

507. 16 C.F.R. § 429.1(d) (1976). Until recently there was doubt as to the authority of the Federal Trade Commission to promulgate such substantive rules. The doubts were resolved in favor of the Commission in *National Petroleum Refiners Ass'n v. FTC*, 482 F.2d 672 (D.C. Cir. 1973), *cert. denied*, 415 U.S. 951 (1974). Doubts also existed as to the import of the rules on intrastate sales. See Boyd & Balentine, *supra* note 5, at 630 n.31. The Federal Trade Commission Improvements Act of 1975 extends the Commission's jurisdiction to practices "affecting" commerce as well as those "in commerce." See 15 U.S.C. §§ 45(a)-(b) (Supp. V, 1975).

508. See Boyd & Ballantine, *supra* note 5, at 629.

509. See UCC § 2-721; A. LaFRANCE, *supra* note 172, at § 102; Boyd, *supra* note 4, at 375.

510. ARIZ. REV. STAT. ANN. §§ 44-5001 to -5008 (Supp. 1975-76).

511. See Boyd & Balentine, *supra* note 5, at 629-32.

512. Compare ARIZ. REV. STAT. ANN. § 44-5001(1) (Supp. 1975-76) with U3C § 3.501 (1974).

arranged loans.<sup>513</sup> However, proper notice is narrowly confined under Arizona law to "registered mail, return receipt requested" or ordinary mail evidenced by a postal receipt.<sup>514</sup> Those criticisms leveled against the original U3C, to which the revised version responded in large part, also apply to the Arizona statute.<sup>515</sup> Specifically, under the Arizona law cancellation fees are allowed,<sup>516</sup> the emergency exception is too broad,<sup>517</sup> and it is unclear to what extent reasonable use or consumption precludes cancellation.<sup>518</sup> No provision is made regarding contractual waivers of cancellation rights,<sup>519</sup> nor have possible overlaps between federal law and the Arizona statute been anticipated.<sup>520</sup>

The Arizona statute might seem to go beyond the U3C provisions on home solicitation sales with its prohibitions on the use of negotiable instruments in home solicitation sales<sup>521</sup> and on referral schemes in the door-to-door sales context.<sup>522</sup> However, as previously indicated, these protections are available under other provisions of the U3C. The revised U3C prohibits the use of negotiable instruments in all consumer credit transactions<sup>523</sup> and invalidates all referral schemes.<sup>524</sup> These general U3C provisions are stronger than any similar Arizona provisions. Adoption of the revised U3C, therefore, would mean a substantial improvement in protection of consumers from ill-advised home solicitation purchases.

### ENFORCEMENT

Reforms aimed at eliminating or alleviating abuses are only as effective as the enforcement scheme that accompanies the proscriptions.<sup>525</sup> The original U3C was severely criticized because it largely overlooked

513. See ARIZ. REV. STAT. ANN. § 44-5001(1) (Supp. 1975-76).

514. *Id.* § 44-5002(B).

515. See Boyd & Balentine, *supra* note 5, at 630. Compare ARIZ. REV. STAT. ANN. §§ 44-5001 to -5008 (Supp. 1975-76) and U3C §§ 2.501-.505 (1968) with *id.* §§ 3.501-.505 (1974).

516. See ARIZ. REV. STAT. ANN. § 44-5007(C) (Supp. 1975-76).

517. See *id.* § 44-5007(D). The emergency exception, in fact, is not defined at all, the statute merely stating, "The buyer may not cancel a home solicitation sale if he requests the seller to provide goods or services without delay because of an emergency and the seller in good faith makes a substantial beginning of performance before notice of cancellation, and the goods cannot be returned to the seller in substantially as good condition as when the buyer received them." *Id.*

518. See *id.* § 44-5006(B); Comment, *Arizona's Home Solicitation and Referral Sales Act*, *supra* note 458, at 824.

519. See Boyd & Balentine, *supra* note 5, at 630.

520. Cf. *id.* at 631; Comment, *Arizona's Home Solicitation and Referral Sales Act*, *supra* note 458, at 803 n.4.

521. ARIZ. REV. STAT. ANN. § 44-5005 (Supp. 1975-76).

522. *Id.* § 44-5003.

523. See U3C § 3.307 (1974); text & notes 160-76 *supra*.

524. See U3C § 3.309 (1974); text & notes 467-69 *supra*.

525. Cf. Spanogle, *supra* note 369.

the potential inherent in private enforcement devices.<sup>526</sup> Apart from a few sections offering private remedies<sup>527</sup> and another giving consumers the right to recover overcharges,<sup>528</sup> the original U3C offered minimal affirmative private relief.<sup>529</sup> Enforcement instead was left primarily in the hands of the administrator<sup>530</sup> and criminal law enforcement authorities.<sup>531</sup>

The revised U3C dramatically alters this imbalance in favor of public enforcement. There is still heavy reliance on the administrator, whose powers have been increased correspondingly.<sup>532</sup> However, consumers are given an added right of action to recover actual damages and a penalty for the violation of any provision not containing a built-in sanction.<sup>533</sup> Where an added measure of deterrence to potential violators and incentive to consumer actions is deemed desirable, a private right of damages and a penalty is granted even though an express or implied sanction is contained in the section itself.<sup>534</sup>

The revised U3C also provides a penalty where a creditor fails to refund an excess charge within a reasonable time following demand by the debtor.<sup>535</sup> The original version allowed recovery only of the excess charge.<sup>536</sup> The addition of a penalty in the revision was motivated by the belief that a creditor subject only to deprivation of the excess charge would have nothing to lose by imposing such a charge.<sup>537</sup>

526. See Boyd, *supra* note 7, at 672-73; Spanogle, *Why Does the Proposed Uniform Consumer Credit Code Eschew Private Enforcement?*, 23 BUS. LAW. 1039 (1968).

527. See U3C § 2.403 (1968) (prohibition on the use of negotiable instruments); *id.* § 2.411 (prohibition on use of referral sales).

528. *Id.* §§ 5.202(2)-(3).

529. Consumers were given a right to sue for a penalty not in excess of three times the finance charge for violations of the prohibition on using negotiable instruments, or of the limitations on the schedule of payments or loan terms for regulated loans. See *id.* §§ 3.511, 5.202(1).

530. See *id.* §§ 6.401-415.

531. See *id.* §§ 5.301-302.

532. See U3C, Prefatory Note, at 94 (1974). See also Miller & Warren, *supra* note 3, at 16-17; discussion at note 141 *supra*.

533. U3C § 5.201(1) (1974); see *id.*, Prefatory Note, at 93-94; Miller & Warren, *supra* note 3, at 16.

534. See U3C, §§ 5.201(1) & Comments 1-2 (1974); *id.*, Prefatory Note, at 94. Rights that are accompanied by inadequate remedies or no remedy at all and limitations on agreements and practices that do not provide for sufficient penalties or for any penalty at all are generally ineffective to accomplish the desired result. They become little more than exhortatory, easily ignored, and meaningless proclamations.

*Id.* § 5.201, Comment 1.

The penalty provisions do not apply to employers who violate the prohibition against garnishment discharges. See *id.* § 5.106. See text & note 374 *supra*. However, an employee discharged in violation of the provision may bring a civil action for recovery of income lost, not to exceed 6 weeks' wages, and an order requiring reinstatement. U3C § 5.201(5) & Comment 5 (1974). Disclosure violations also are outside the penalty provisions and are given independent treatment. See *id.* § 5.203.

535. U3C § 5.201(3) (1974). Any refund not made within 30 days is presumed not to have been made within a reasonable time. *Id.*

536. See *id.* § 5.202(3) (1968).

537. *Id.* § 5.201, Comment 3 (1974).

The same reasoning supports the provision granting a right to recover a penalty where excess charges have been contracted for even if not paid.<sup>538</sup>

The penalty recoverable in any situation where such remedy is allowed is to be determined by the court, but is limited to no more than \$1000 nor less than \$100.<sup>539</sup> In this respect the revised U3C basically tends to track federal law, although the basic federal penalty formula is twice the amount of the finance charge.<sup>540</sup> The U3C penalty, however, is not tied to the amount of the excess charge because the excess may be small, thus providing an inadequate incentive to seek recovery of a penalty.<sup>541</sup> Additionally, flexibility in fixing penalties was desired in order that the amount might be varied according to the seriousness of the offense and the surrounding circumstances.<sup>542</sup> The damages and penalties recoverable under these sections may be set off against the consumer's debt and may be raised as a defense to an action on the debt regardless of the prescribed time limits.<sup>543</sup>

As a final concession to the need for private remedies, the revised U3C directs the courts to award costs and reasonable attorneys' fees whenever the consumer is successful.<sup>544</sup> The provision appears to contemplate an award of attorneys' fees whether the case is tried or settled,<sup>545</sup> and the size of such award is not limited by the amount recovered by the consumer.<sup>546</sup>

A creditor may escape liability for a penalty by notifying the consumer of the violation, before the consumer gives written notice or files suit, and correcting the violation within 45 days thereafter.<sup>547</sup> Liability also may be avoided by the creditor's showing that the violation was not intentional but resulted from a bona fide error despite reasonable attempts to avert it.<sup>548</sup> These reasonable defenses provided creditors

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538. See *id.* § 5.201(3) & Comment 3.

539. *Id.* § 5.201(1).

540. See 15 U.S.C. § 1640(a)(2)(A) (Supp. IV, 1974) (providing penalties for violation of the credit transaction and credit billing provisions of the federal Truth-in-Lending Act).

541. Miller & Warren, *supra* note 3, at 16.

542. U3C § 5.201, Comment 2 (1974). The federal penalty provision does not apply to as wide a variety of conduct as does that of the U3C. See 15 U.S.C. §§ 1631-1645 (1970), *as amended*, (Supp. IV, 1974); 15 U.S.C. §§ 1666-1666j (Supp. IV, 1974).

543. U3C § 5.202 (1974).

544. *Id.* § 5.201(8). This provision would be compatible with the new Arizona statute providing for attorneys' fees in actions arising out of contract and in successful efforts to avoid the issuance of a provisional remedy. Ch. 170, §§ 1 (12-2411), 2 (12-341.01), [1976] Ariz. Sess. Laws 786, 791. See text & notes 107-23 *supra*; discussion note 419 *supra*.

545. See U3C § 5.201, Comment 6 (1974).

546. *Id.* § 5.201(8).

547. *Id.* § 5.201(6).

548. *Id.* § 5.201(7).

in the revised U3C were adopted from the federal truth-in-lending law,<sup>549</sup> which has been interpreted to mean that errors of law are outside the bona fide error exception.<sup>550</sup>

The expansion in the revised U3C of the opportunity for private recourse is to be applauded,<sup>551</sup> as exclusive reliance on public enforcement simply is unrealistic. Unfortunately, however, the revised U3C enforcement scheme is not without its shortcomings. For one thing, the provision making supervised loans by unlicensed lenders void has been deleted.<sup>552</sup> The only explanation offered is that the voidness sanction has proved unworkable in the past.<sup>553</sup> It is not apparent why this should be so. A legal conclusion that a contract is void is a very effective weapon for consumers, as it diminishes the possibility that relief will be forfeited inadvertently.<sup>554</sup> A more likely explanation is that voidness was considered too severe a penalty and hence inappropriate; however, this rationale is not totally persuasive either.

Even more troublesome is the posture of the revised U3C regarding class actions. Recovery of a penalty in a class suit is totally precluded,<sup>555</sup> ostensibly because case law has disfavored class suits where recovery is in the form of a penalty.<sup>556</sup> The difficulty with this position is that it too readily accedes to the complaints of a few courts and numerous creditors that permitting such recovery in class suits for "technical violations" punishes unfairly the great majority of creditors who are well-meaning and law-abiding.<sup>557</sup> This argument fails to take into account the fact that penalties are essentially legislated liquidated damages provided to insure that violations will not go unchallenged.<sup>558</sup> It further fails to recognize that individual consumer actions are not likely to result with sufficient frequency or effect to assure the effective enforcement which is the objective of the entire scheme of private remedies.<sup>559</sup> The mere existence of the penalty, the fact that it is not

549. See 15 U.S.C. §§ 1640(b)-(c) (Supp. IV, 1974).

550. See *Buford v. American Finance Co.*, 333 F. Supp. 1243, 1247-48 (N.D. Cal. 1971). The Texas Court of Civil Appeals has held that the burden is on the creditor to establish the existence of bona fide error under both the Texas Consumer Credit Code and the federal truth-in-lending law. See *McDonald v. Savoy*, 501 S.W.2d 400, 407 (Tex. Civ. App. 1973).

551. The revised U3C provides for other remedies in addition to those set forth in section 5.201. See U3C § 5.201, Comment 7 (1974).

552. *Id.*, Prefatory Note, at 94. A penalty, however, is retained. See *id.* § 5.201(1).

553. See *id.*, Prefatory Note, at 94; Miller, *Enforcement of the Uniform Consumer Credit Code: Observations from the Oklahoma and Federal Experience*, 51 N.C.L. REV. 1229, 1240-45 (1973).

554. See *Boyd*, *supra* note 47, at 183. Inadvertent forfeiture may occur, for example, where the relief available is in the nature of rescission.

555. U3C §§ 5.201(1), (3) (1974).

556. See Miller & Warren, *supra* note 3, at 16. See also Hale, *The Direction of Litigation in the Consumer Credit Field*, 28 BUS. LAW. 639, 653-61 (1973).

557. See *Redhouse v. Quality Ford Sales, Inc.*, 511 F.2d 230, 236 (10th Cir. 1975).

558. Cf. U3C § 5.201 & Comment 1 (1974).

559. See *Boyd*, *supra* note 47, at 184 & n.105; Dole, *supra* note 147, at 81.

tied to the finance charge, and the liberalized attorneys' fee provisions are not alone likely to alter this reality inherent in consumer-initiated legal actions.<sup>560</sup>

In other respects the revised U3C, following the original version,<sup>561</sup> leaves the availability of class suits to the law of the respective state.<sup>562</sup> This, too, is unfortunate. It is unfortunate because the procedures in many states either do not address the problem of class actions at all or fail to do so in ways that reflect the contemporary importance of such actions.<sup>563</sup> If the considerable discussion by courts of the propriety of class actions has revealed anything, it is that the question should be resolved by the legislatures.<sup>564</sup> The revised U3C, by deferring to local law, which frequently means court decision,<sup>565</sup> has missed an opportunity to deal definitively and rationally with an issue that has become the subject of obtuse and emotional reaction.<sup>566</sup> The experience in federal courts clearly illustrates the problem. Although the class action provisions in the federal rules are quite liberal,<sup>567</sup> the courts have strained to devise limits on their effectiveness.<sup>568</sup> The federal consumer protection laws also have seemed to invite class suits,<sup>569</sup> yet the courts have acted in such a way as to force congressional clarification of the right if it is to be recognized.<sup>570</sup>

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560. See Boyd, *supra* note 47, at 183. Indeed, unless the creditors themselves believed that consumers who would join in class actions would not file individual suits, it would not be in their interest to oppose class actions, since separate attorneys' fees and costs could be charged in each individually filed action.

Congress has recently amended the truth-in-lending laws expressly to allow recovery of civil penalties in class actions. Pub. L. No. 93-495, § 408(a), 88 Stat. 1518, amending 15 U.S.C. § 1640(a) (1970) (codified at 15 U.S.C. § 1640(a) (Supp. IV, 1974)) (providing for the recovery of actual damages and "in the case of a class action, such amount as the court may allow . . ."); see Evans, *supra* note 151, at 12-13.

561. See Spanogle, *supra* note 369, at 640-51.

562. See Miller & Warren, *supra* note 3, at 16.

563. See Dole, *supra* note 147, at 80-81; Kalven & Rosenfield, *The Contemporary Function of the Class Suit*, 8 U. CHI. L. REV. 684 (1941).

564. See generally Dole, *supra* note 147.

565. See *id.* at 90-97. A few jurisdictions have authorized class suits by consumers. See 1 CCH POVERTY L. RPT. ¶ 3450, at 4429-30 (1972). Congress, after struggling to enact class action legislation for years, see Boyd, *supra* note 47, at 184 n.106, finally produced a law governing class suits in truth-in-lending disputes. See 15 U.S.C. § 1640(a) (Supp. IV, 1974); Evans, *supra* note 151, at 12-13.

566. See, e.g., Redhouse v. Quality Ford Sales, Inc., 511 F.2d 230, 236 (10th Cir. 1975).

567. See FED. R. CIV. P. 23; cf. Dole, *supra* note 147, at 109-14.

568. See, e.g., Eisen v. Carlisle & Jacquelin, 417 U.S. 156 (1974) (holding that rule 23 requires notice to every member of the class with plaintiffs' bearing the cost).

569. Actions for violations of the Consumer Credit Protection Act may be brought in any federal district court without regard to the amount in controversy. See 15 U.S.C. § 1640(e) (1970); R. JOHNSON, *supra* note 148. In the absence of such authorization, class suits will fail due to the requirement that each class member's claim exceed the \$10,000 amount. See, e.g., Snyder v. Harris, 394 U.S. 332 (1969); Troy Bank v. Whitehead & Co., 222 U.S. 39 (1911); Alvarez v. Pan Am. Life Ins. Co., 375 F.2d 992 (5th Cir.), cert. denied, 389 U.S. 827 (1967). But see 28 U.S.C. § 1337 (1970).

570. See, e.g., Redhouse v. Quality Ford Sales, Inc., 511 F.2d 230 (10th Cir. 1975); Rodriguez v. Family Publications Servs., Inc., 57 F.R.D. 189 (C.D. Cal. 1972); Ratner

Arizona's experience is comparable. Arizona adopted the federal rules as its procedural model,<sup>571</sup> including the class action rules.<sup>572</sup> Nevertheless, the Arizona courts have moved to limit the availability of class suits in ways which charitably may be described as curious.<sup>573</sup> A definitive statement by the legislature that class suits are virtually indispensable in the consumer context is in order. Any enactment of the revised U3C should be accompanied by such a legislative statement so as to correct this serious deficiency in an otherwise laudable document. A statement modelled after the recent amendment to the federal truth-in-lending law authorizing class actions for penalties as well as actual damages<sup>574</sup> and imposing reasonable limits on recovery<sup>575</sup> would appropriately accomplish this objective.<sup>576</sup>

### CONCLUSION

The revised U3C should be adopted in Arizona. It is a comprehensive code which recognizes the need for a body of law paralleling the commercial law generally, yet diverging from commercial doctrine where special considerations—such as disparities in bargaining power—require that doctrine be replaced or modified in the context of consumer transactions.<sup>577</sup> However, there are deficiencies in the revised U3C, with respect to both its coverage and its substantive rules, which are serious enough to warrant modification prior to adoption. The device of incorporating by reference federal consumer protection laws is a necessary concession to the ever-expanding role of the federal government in this area. This is particularly true of the disclosure laws but not

v. Chemical Bank New York Trust Co., 54 F.R.D. 412 (S.D.N.Y. 1972). *But see* Haynes v. Logan Furniture Mart, Inc., 503 F.2d 1161 (7th Cir. 1974). Recent amendments to 15 U.S.C. § 1640(a) (Supp. IV, 1974) do limit recovery in class actions. See discussion note 148 *supra*.

571. See ARIZ. R. CIV. P. 1, Reviser's Note.

572. ARIZ. R. CIV. P. 23; see Lennon v. First Nat'l Bank, 21 Ariz. App. 306, 518 P.2d 1230 (1974).

573. See Reader v. Magma-Superior Copper Co., 110 Ariz. 115, 117, 515 P.2d 860, 862 (1973). *But see* "Aggregation in Class Actions in Arizona," 15 ARIZ. L. REV. 593, 615, 619-20 (1973) (arguing that Arizona courts take a more liberal view regarding aggregation to meet jurisdictional amounts than does the United States Supreme Court).

574. See 15 U.S.C. § 1640(a) (Supp. IV, 1974). See discussion note 560 *supra*.

575. See discussion note 148 *supra*.

576. In other respects Arizona's consumer laws share many of the same remedial deficiencies found in the original U3C. See text & notes 526-31 *supra*. See, e.g., Motor Vehicle Time Sales Disclosure Act, ARIZ. REV. STAT. ANN. §§ 44-281 to -295 (1967), as amended, (Supp. 1975-76); Consumer Fraud Act, *id.* §§ 44-1521 to -1534; *id.* § 44-1223 (Supp. 1975-76) (fraud perpetrated by changing odometers). *But see id.* § 44-1222 (unordered merchandise); *id.* §§ 44-1691, -1695 (consumer credit reporting). However, the Arizona courts are beginning to acknowledge the advantages of private enforcement which underlie the revised U3C enforcement scheme. Thus, the Arizona supreme court has held recently that a violation of the Arizona consumer fraud statute, see *id.* §§ 44-1521 to -1533 (1967), as amended, (Supp. 1975-76), gives rise to a private action. See Sellinger v. Freeway Mobil Home Sales, Inc., 110 Ariz. 573, 576, 521 P.2d 1119, 1122 (1974).

577. See Boyd, *supra* note 4, at 372-74, 379.

exclusively so. It therefore may be necessary to alter the U3C to reflect federal laws enacted since the revised version was approved for adoption.<sup>578</sup> The essentially negative posture of the U3C towards class actions should be replaced with authorization for such suits, appropriate safeguards being added to discourage spurious claims and unrealistic recoveries.<sup>579</sup> Provision should be made for giving consumers notice of their rights where the absence of such notice may render the rights illusory.<sup>580</sup> Similarly, the Code should be modified to protect against waivers of rights.<sup>581</sup> Where there is a possibility that courts may interpret a remedy so as to undermine its effectiveness, such an interpretation must be expressly negated.<sup>582</sup>

To the extent that Arizona law is superior to the revised U3C, modifications should be made to reaffirm the present Arizona position. Thus, the requirement of a free period presently contained in the Arizona statute governing revolving charge accounts should be added to the U3C.<sup>583</sup> Likewise, where the U3C provides a choice, the option should be adopted which best preserves Arizona's position.<sup>584</sup>

Certain deficiencies in the revised U3C are such that mere modification will not alleviate them. For example, there is a need for sweeping reform in the area of warranties.<sup>585</sup> The same may be said of the laws relating to debt collection<sup>586</sup> and credit reporting;<sup>587</sup> however, one

578. Since the revised U3C was approved for adoption, Congress has expanded the truth-in-lending laws by amending the credit advertising provisions, 15 U.S.C. § 1665a (Supp. IV, 1974), and has enacted the Fair Credit Reporting Act. *Id.* §§ 1681-1681t (1970). There also has been other legislation added of considerable import: the Real Estate Settlement Procedures Act, 12 U.S.C. §§ 2601-2616 (Supp. IV, 1974); the Equal Credit Opportunity Act, 15 U.S.C. §§ 1691-1691e (Supp. IV, 1974); the Consumer Product Warranties Act, *id.* §§ 2301-2312 (Supp. IV, 1974); see discussion note 589 *infra*; and the Consumer Leasing Act of 1976. Pub. L. No. 94-240, 90 Stat. 257 (effective Mar. 3, 1977). See generally discussion text & notes 137-40 *supra*.

579. See text & notes 555-74 *supra*.

580. See Boyd & Balentine, *supra* note 5, at 632; Comment, *Arizona's Home Solicitation and Referral Sales Act*, *supra* note 458, at 816.

581. Compare text & note 435 *supra* with text & notes 506-07 *supra*.

582. See text & note 453 *supra*.

583. See discussion note 98 *supra*. Another example is the provision for payment of a surplus in cases where the creditor repossesses goods the fair market value of which exceeds the debt owing plus expenses. See text & notes 318-20 *supra*. This change is supported by the proposed FTC Credit Practices Rule. See discussion note 12 *supra*. In fact, it would be prudent to revise the U3C to whatever extent necessary in anticipation of possible changes in the Federal Trade Commission rules. See text & notes 56, 123, 226, 321, 360, 435 *supra*. See also text & note 586 *infra*.

584. See text accompanying notes 97-98 *supra*.

585. See Boyd, *supra* note 4, at 385-88, 394; MCCA, *supra* note 240, §§ 2.502-.504.

586. See A. LAFRANCE, *supra* note 172, at § 130. The U3C does offer some increased protection against abusive debt collection practices. See text & note 377 *supra*. Once again the contrast with other proposed legislation is rather dramatic. See MCCA, *supra* note 240, §§ 6.101-303. See also FTC Credit Practices Rule, *supra* note 12, at § 444.2(10).

587. See A. LAFRANCE, *supra* note 172, at 24; MCCA, *supra* note 240, § 5.101-305.

There is significant federal and state legislation governing credit reporting in Arizona. On the federal level there is the Fair Credit Reporting Act, 15 U.S.C. §§ 1681-1681t (1970). See generally A. LAFRANCE, *supra* note 172, at § 106. At the state

may argue that these matters warrant independent consideration. Moreover, as to warranties, reform measures have been recently enacted at the federal level.<sup>588</sup> It may be prudent, therefore, to await an evaluation of such federal laws before further action is taken at the state level.<sup>589</sup> The suggestion is not that the deficiencies in the U3C should go unattended.<sup>590</sup> The point is rather that these deficiencies, however important they may be, are not of such magnitude as to justify rejecting the revised U3C entirely.

In total the revised U3C represents a rather impressive response to most of the criticisms of the original version which made the latter unacceptable to most states. This writer earlier suggested, in an essentially negative evaluation of the U3C, that the proposed National Consumer Act, even though too consumer-oriented, should serve as a model against which to test future consumer protection legislation.<sup>591</sup> The drafters of the revised U3C seem to have heeded this suggestion to a rather remarkable degree.<sup>592</sup> The existing Arizona law, although improved by recent legislation,<sup>593</sup> is still inferior to the revised U3C. There is, of course, the risk that enactment of an exhaustive statutory scheme such as the U3C will stifle that continuing review necessary to maintain viable legislation in the dynamic area of consumer law.<sup>594</sup> On balance, however, the risks inherent in enacting this comprehensive piece of legislation are far outweighed by the gains when it is considered in light of the current piecemeal legislative efforts that characterize Arizona consumer law.<sup>595</sup>

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level there is the Consumer Reporting Agencies Act. ARIZ. REV. STAT. ANN. §§ 44-1691 to -1696 (Supp. 1975-76); cf. A. LAFRANCE, *supra* note 172, § 106, at 25. See also MCCA, *supra* note 240, §§ 5.101-305.

588. Consumer Product Warranties Act [Magnuson-Moss Warranty—Federal Trade Commission Improvement Act], Pub. L. No. 93-637, 88 Stat. 2183 (codified at 15 U.S.C. §§ 2301-2312 (Supp. IV, 1974)). See generally D. EPSTEIN, CONSUMER PROTECTION 218-23 (1976); Leete, *A Look at the Consumer Warranty Problems—The Federal Solution*, 6 U. TOL. L. REV. 351 (1975).

589. An area to watch is that concerned with alternative models of consumer dispute settlement mechanisms. The new federal warranty law, see text & note 588 *supra*, encourages the formation of informal dispute settlement procedures. See 15 U.S.C. §§ 2310(a)(1)-(3) (Supp. IV, 1974); 16 C.F.R. §§ 703.1-8 (1976). The American Bar Association Section on Antitrust Law is studying arbitration as a mechanism for the resolution of consumer-merchant grievances. Consumer controversies resolution legislation has been proposed at the federal level. See Brandel, *The Consumer Controversies Resolution Act*, 28 PERS. FINANCE L.Q. 107 (1974).

590. See text & notes 426-32 *supra*.

591. See Boyd, *supra* note 7, at 674.

592. Compare U3C (1974) with NCA, *supra* note 240.

593. See text & notes 388-93, 411-21 *supra*.

594. See Boyd & Balentine, *supra* note 5, at 658.

595. See *id.* at 657-58.