Comments

CONSUMER PROTECTION UNDER THE UCCC AND THE NCA—A COMPARISON AND RECOMMENDATIONS

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In a nation where the consumer debt in 1968 was $95 billion and interest and finance charges were $13 billion,[1] it is imperative that the laws and practices governing the extension of credit and repayment of indebtedness protect the rights and interests of all concerned. While the balance has traditionally been in favor of the lenders, two recent efforts have been made to draft comprehensive laws to even the odds. The *Uniform Consumer Credit Code* (UCCC) was written to assure adequate protection for consumers in credit transactions.[2] The success of the UCCC has been widely questioned,[3] however, and dissenting consumer forces drafted the *National Consumer Act* (NCA).[4]

The protection given the consumer under the UCCC is often inadequate. The NCA, on the other hand, frequently has gone too far in placing oppressive burdens on creditors. Although the substantive provisions

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[1] W. MAGNUSON & J. CARPER, THE DARK SIDE OF THE MARKET PLACE 91 (1968).

[2] The *Uniform Consumer Credit Code* was drafted by the National Conference of Commissioners on Uniform State Laws and approved by the American Bar Association in August, 1968. It has been enacted by two states. OKLA. STAT. ANN. tit. 14A, §§ 1-101 *et seq.* (Supp. 1969-70); UTAH CODE ANN. §§ 70B-1-101 *et seq.* (Supp. 1969).

As the name implies, the *Uniform Consumer Credit Code* is limited in scope to those credit transactions in which one of the parties is a consumer. Although "consumer" is not specifically defined, the sections of the code dealing with consumer credit transactions apply only where the debtor is "a person other than an organization" who acquires "goods, services, or interest in land . . . primarily for . . . personal, family, household, or agricultural [purposes]," and the credit received "does not exceed $25,000" as to the goods and services. UCCC § 2.104. *See generally* UCCC §§ 1.301(11), 2.104, 2.106, & 3.104.

[3] For criticisms of the UCCC, see Jordan & Warren, *The Uniform Consumer Credit Code*, 68 COLUM. L. REV. 387 (1968); Navin, *Waiver of Defense Clauses in Consumer Contracts*, 48 N.C.L. REV. 505 (1970); Comment, *Garnishment Under the Consumer Credit Protection Act and the Uniform Consumer Credit Code*, 38 U. CIN. L. REV. 338 (1969).

[4] NATIONAL CONSUMER LAW CENTER, NATIONAL CONSUMER ACT: A MODEL ACT FOR CONSUMER PROTECTION (1970) [hereinafter cited as NCA]. The NCA was drafted by the National Consumer Law Center, Boston College Law School, Brighton, Massachusetts and is presently being considered for enactment, in whole or in part, by several states.

The scope of the NCA is also limited to consumer credit transactions. The NCA definition of "consumer," however, is "a person other than an organization who seeks or acquires business equipment for use in his business, or real or personal property, services, money or credit for personal, family, household or agricultural purposes." NCA § 1.301(8). The NCA has a broader scope than does the UCCC and extends consumer protection to the sole proprietor who acquires business equipment. In addition, there is no dollar limit on a consumer transaction. *See generally* NCA §§ 1.301(8)-(13) & (25).

of these codes differ drastically in several areas, they are procedurally similar in that both depend upon an administrator and an administrative agency for enforcement.[5]

Debt collection practices, repossession, exemption from attachment, holder in due course status and waiver of defense clauses are the most important and controversial problems related to consumer credit transactions. The controversy is manifested in the divergent approaches the two codes have taken toward the resolution of these problem areas. This comment will analyze and compare the treatment of these five major areas under both the UCCC and the NCA. Criticisms and suggested improvements will be offered where appropriate. A complete comparative analysis of the two codes, however, is beyond the scope of this effort.

ABUSIVE COLLECTION PRACTICES

Perhaps because of the need for extrajudicial collection,[6] few states have attempted to regulate the practices of collection agencies.[7] This absence of regulation and the incentive for out-of-court settlements have encouraged creditors to forego their judicial remedies. When extrajudicial collection is zealously pursued, however, abusive practices frequently occur. Many collection agencies have employed tactics such as sending threatening letters, threatening to blacklist the debtor so that he loses his job, or calling him a liar and a deadbeat in the presence of his friends and family.[8]

In the absence of special legislation providing a remedy for abusive treatment, debtors generally have resorted to such common law remedies as intentional infliction of mental anguish, invasion of privacy, and defamation.[9] These remedies have several significant weaknesses, however, and the debtors subjected to abusive collection practices often do not seek judicial redress.[10] The cost of a court action may be prohibitive or the debtor may be afraid of the publicity accompanying a law suit based on abusive collection practices.[11] Probably the major drawback of common law remedies is that recovery by a single debtor will not induce col-

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5 UCCC §§ 6.101 *et seq.*; NCA §§ 6.101 *et seq.*

6 Comment, *Effectively Regulating Extrajudicial Collection of Debts*, 20 ME. L. REV. 261, 277 (1968) [hereinafter cited as *Extrajudicial Collection*]. *See, e.g.*, ARIZ. REV. STAT. ANN. §§ 32-1001 *et seq.* (Supp. 1969-70), which places only minimal restrictions on collection agencies.

7 *Extrajudicial Collection, supra* note 6, at 274 n.62.

8 Comment, *Recovery For Creditor Harassment*, 46 TEXAS L. REV. 950, 960 (1968). *See also* Graber v. International Creditors Corp., 39 U.S.L.W. 2051 (Pa. C.P. June 24, 1970); *Extrajudicial Collection, supra* note 6, at 262.

9 For a discussion of common law remedies and their weaknesses, see Note, *Debt Collection Practices: Remedies for Abuse*, 10 B.C. IND. & COM. L. REV. 698, 701 (1969); *Extrajudicial Collection, supra* note 6. *See also* American Credit Bureau v. Bel-Aire Interiors, Inc., 11 Ariz. App. 168, 462 P.2d 861 (1969).

10 Note, *Debt Collection Practices: Remedies for Abuse*, 10 B.C. IND. & COM. L. REV. 698, 701 (1969).

11 *Id.*

lection agencies to modify their practices. The financial loss attributable to a few law suits may be small in comparison with the profits derived from the use of abusive collection practices. Thus, the infrequency of lawsuits by debtors does not mean that objectionable collection practices are on the wane. Rather, it encourages the continuance of such practices.[12]

Because of the weaknesses of common law remedies, it would seem that the best solution would be comprehensive legislation proscribing certain practices and providing for recovery of damages to facilitate enforcement. The effectiveness of such measures would depend, of course, on whether the consumer knows of their availability. The publicity attendant to law suits and the possibility of a publicity campaign initiated by the administrator could achieve this end.[13]

Although the UCCC prohibits fraudulent or unconscionable conduct in the collection of debts,[14] its terminology and sanctions are inadequate. It does not create a remedy under which the debtor may recover damages, but merely allows the administrator[15] to seek an injunction against the unconscionable conduct.[16] The unavailability of money damages will probably inhibit the debtor's disclosure of all but the most flagrant violations to the administrator. Moreover, since the administrator's only remedy is to seek an order restraining the unconscionable conduct,[17] an offending creditor would have no incentive to cease abusive practices until he receives such an order. A comprehensive scheme of enforcement would thus necessitate a separate action against every creditor engaging in fraudulent or unconscionable conduct. The NCA, on the other hand, allows the administrators to bring a class action to recover damages to which consumers would be entitled under the act.[18] This weapon undoubtedly would be a greater deterrent to abusive collection practices than the possibility of a restraining order.

Under the UCCC, an injunction may not issue unless the "conduct of the [creditor] has caused or is likely to cause injury to consumers."[19] This requirement leaves the court with the problem of determining the degree and type of injury necessary to render the practice unconscionable. Too narrow an interpretation of injury may further undermine the effectiveness of this remedy. The UCCC standard, "a course of . . . fraudulent or unconscionable conduct,"[20] is likewise inadequate to guide the ad-

12 *Id.*
13 *Cf.* UCCC § 6.104; NCA § 6.104.
14 UCCC § 6.111: "(1) The Administrator may bring a civil action to restrain a creditor or a person acting in his behalf from engaging in a course of . . . (c) fraudulent or unconscionable conduct in the collection of debts arising from consumer credit sales, consumer leases, or consumer loans."
15 *Id.* §§ 6.101 *et seq.*
16 *Id.* § 6.111.
17 *Id.*
18 NCA § 6.111.
19 UCCC § 6.111.
20 *Id.*

ministrator, creditor or debtor. Such a broad standard may be interpreted in a variety of ways.[21] Consequently, creditors will be unable to determine which practices are permissible, and debtors will be unable to decide which practices should be reported.

The administrative approach of both the UCCC and the NCA requires a vigorous administrator and sufficient funds to carry out the program.[22] If costs are significant, the administrator may be forced to limit the number of cases he prosecutes. This problem could be greatly alleviated if the administrator were allowed to recover his costs of litigation when he prevails. Neither the UCCC nor the NCA provide for such a recovery.

In contrast to the UCCC's general proscription of "unconscionable conduct in the collection of debts,"[23] the NCA has specifically banned certain collection practices[24] as well as prohibiting "unfair or unconscionable means to collect or attempt to collect any claim."[25] The NCA's specific proscriptions include the practice of law by debt collectors; threatening violence or harm against a person, his reputation, or his property; and falsely accusing or threatening to accuse the debtor of crimes or conduct which disgrace him.[26] These provisions and others found in the act[27] would eliminate the majority if not all of the current abusive practices.

The NCA also requires the administrator to "promulgate regulations declaring specific practices in consumer transactions or collection of debts arising therefrom to be unconscionable and prohibiting the use thereof."[28] The inclusion of a standard such as "unfair or unconscionable means"[29] gives the administrator a flexible guideline for the promulgation of regulations proscribing specific practices. By using an indefinite standard such as unconscionability to establish guidelines for the creditor and administrator, the NCA is open to the same criticism as the UCCC. There is sufficient specificity in the NCA's prohibitions, however, to provide a clear indication of which practices are unconscionable under section 7.206.

In addition to lending specificity and flexibility to the determination of what actions are to be circumscribed, the NCA also creates three private remedies. Under section 7.301, the debtor is given a complete defense to his obligation if the creditor is guilty of any of the prohibited collection practices. Section 7.302 allows compensatory damages for emotional

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21 *Extrajudicial Collection, supra* note 6, at 276-77.
22 *Id.* at 276.
23 UCCC § 6.111(1)(c).
24 NCA § 7.201-205.
25 *Id.* § 7.206.
26 *Id.* §§ 7.201-205.
27 *Id.*
28 *Id.* § 6.109.
29 *Id.* § 7.206.

distress or mental anguish caused by these practices, and section 7.303 provides that punitive damages may be at the discretion of the court. The debtor's ability to raise violations of the act as a defense in an action by the creditor should give some assurance that the debtor will use his remedy. Moreover, the availability of compensatory and punitive damages acts as a deterrent to abusive collection practices and gives the debtor a remedy in addition to any defense he might have to an action by the creditor on the obligation.

The remedies the NCA affords the debtor are adequate if they are utilized. Without the advice of counsel, however, these remedies may go unused. Similarly, the debtor may presume that he is legally liable for his original obligation and, thus, may allow himself to fall prey to abusive collection practices. The enactment of consumer protection legislation such as the NCA and the prosecution of actions under it should, however, give rise to sufficient publicity to make debtors more aware of their rights.

The NCA and the UCCC both provide that the administrator is to investigate abusive practices.[30] Under the UCCC, the administrator first must establish "probable cause" to believe that there has been a violation before he may commence an investigation.[31] The UCCC does not explain how probable cause is to be established without an investigation, although consumer complaints presumably would be sufficient. Nevertheless, the requirement for probable cause is an obstacle to any administrative investigation. The NCA administrator, on the other hand, does not have to establish probable cause[32] and is compelled to investigate upon the filing of complaints by ten or more consumers.[33]

Although the NCA provides for the recovery of investigatory expenses if the administrator prevails in subsequent litigation,[34] there would be more incentive to the administrator and the consumer if the expenses of litigation and compensatory and punitive damages for the complainants could also be recovered. The specter of this increased potential liability would deter the creditor's abusive practices.

Neither the UCCC nor the NCA treat the problem of the "deadbeat" who runs up a small bill and fails to respond to any fair collection practices. In such cases, it may be uneconomical for the creditor to sue. If the creditor were to resort to more abusive or unconscionable collection

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30 *Id.* § 6.106; UCCC § 6.106(1).

31 UCCC § 6.106(1) states in part: "If the Administrator has probable cause to believe that a person has engaged in an act which is subject to action by the Administrator, he may make an investigation to determine if the act has been committed . . . ." The code does not explain what amount of proof is necessary to establish probable cause.

32 NCA § 6.106, Comment.

33 *Id.* § 6.106(2): "If 10 or more consumers file a signed complaint with the Administrator alleging that a person has engaged in an act which is subject to action by the Administrator, he shall immediately commence an investigation pursuant to subsection (1) of this section."

34 *Id.* § 6.106(1).

practices, he may either be restrained under the UCCC or have his claim defeated and possibly suffer damages under the NCA. Thus, both codes improve the position of the deadbeat. Nevertheless, abusive collection practices are so unconscionable that even the true deadbeat, who represents a small minority of consumers,[35] should be protected from their use. The practical effect of the UCCC and the NCA will be to make lenders more cautious in extending credit to marginal debtors.

By prohibiting specific practices and by empowering the administrator to proscribe others, the NCA has created guidelines for the prosecution of offenders. The UCCC, on the other hand, only offers a standard of fraudulent or unconscionable conduct and then limits the means by which the administrator can combat those practices which fall within it. By failing to include a specific enumeration, the UCCC has potentially weakened the protection extended to consumers in that it creates the possibility of inconsistent interpretation as well as interpretations which favor the more powerful lobbying group, the creditors.

REPOSSESSION

One would expect that a credit institution's profit would come from interest charges and not from the repossession of the collateral after default. A recent study of automobile repossession practices in Connecticut, however, indicates that part of the motivation for quick defaults and repossessions is the high profits realized from the resale of the automobiles.[36] Extrajudicial repossession may be justifiable[37] because litigation only increases the expenses of a lender who is seeking to recoup his loss.[38] A legal system which allows a creditor to realize a profit from repossession is in need of revision, however.

In recognizing the right to repossess, the *Uniform Commercial Code* states, "Unless otherwise agreed a secured party has on default the right to take possession of the collateral. In taking possession a secured party may proceed without judicial process if this can be done without breach of the peace or may proceed by action."[39] The UCCC predicates the right of repossession upon default[40] but leaves this term and the critical

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35 Less than one percent of all debts are uncollectable and only a fractional part of those are attributable to the true deadbeat. MAGNUSON & CARPER, *supra* note 1, at 91.

36 Comment, *Non-Judicial Repossession—Reprisal In Need of Reform*, 11 B.C. IND. & COM. L. REV. 435, 439 n.30 (1970) [hereinafter cited as *Non-Judicial Repossession*], *citing* Shuchman, *Profit on Default: An Archival Study of Automobile Repossession and Resale*, 22 STAN. L. REV. 20, 42 (1969).

37 *Non-Judicial Repossession, supra* note 36.

38 Hogan, *The Secured Party & Default Proceedings Under the U.C.C.*, 47 MINN. L. REV. 205, 211 (1962).

39 UNIFORM COMMERCIAL CODE § 9-503 (1962 Official Draft) [ARIZ. REV. STAT. ANN. § 44-3149 (1967)]. Hereinafter, all citations to Code sections are to the particular section number of the *Uniform Commercial Code* (1962 Official Text), followed by the *Arizona Revised Statutes Annotated* section number in parentheses.

40 UCC § 9-503 (44-3149).

phrase "breach of the peace" undefined. In the absence of a statutory definition, default has generally been considered to be whatever the parties have agreed upon in their contract.[41] Thus, default could be the noncompliance with any condition regardless of its materiality to the performance of the contract. The UCC's failure to define default leaves the court with the problem of determining whether a secured party may enforce his security interest merely because of a technical default which may be no more than the failure of an irrelevant condition.[42] Another problem is that the UCC does not define what constitutes a breach of the peace, thus creating another element of uncertainty in the default-repossession process.[43]

The most significant problem with non-judicial repossession, however, is its questionable constitutionality. In *Laprease v. Raymours Furniture Co.*,[44] New York's repossession statute,[45] which allowed prehearing seizure of chattels, was held to be violative of the fourth and fourteenth amendments. Analogizing from the fourth amendment law of searches and seizures, the court reasoned that a sheriff's prehearing repossession was as repugnant to the Constitution as the invasion of the privacy of a home without a warrant in a criminal matter.[46] Relying upon *Sniadach v. Family Finance Corp.*,[47] the court also held that "[i]nsofar as [the statute] permits a prehearing seizure, without notice to the defendant, it violates due process."[48]

In *Sniadach* the Supreme Court was faced with the question of "whether the interim freezing of . . . wages [under Wisconsin's prejudgment garnishment statute] without a chance [for the debtor] to be heard violates procedural due process."[49] The Court held that "[w]here the taking of one's property is so obvious . . . absent notice and a prior hear-

41 *Non-Judicial Repossession, supra* note 36, at 437. *See, e.g.*, Borochoff Properties, Inc. v. Howard Lumber Co., 115 Ga. App. 691, 695, 155 S.E.2d 651, 654 (1967); UCC § 9-501(3) (44-3147(c)).

42 W. WILLIER & F. HART, FORMS AND PROCEDURES UNDER THE UNIFORM COMMERCIAL CODE ¶ 92.46 (1969).

43 Hogan, *supra* note 38, at 211.

44 315 F. Supp. 716 (N.D.N.Y. 1970).

45 N.Y. CIV. PRAC. LAW §§ 7101 *et seq.* (McKinney 1963).

46 Arizona's corresponding statutes, ARIZ. REV. STAT. ANN. §§ 12-1301 *et seq.* (1956), which provide for a prehearing sheriff's replevin upon the plaintiff's affidavit that he is lawfully entitled to possession of the chattel, could similarly be attacked on fourth amendment grounds. In addition, Arizona, by adopting the UCC, has given statutory authorization to a creditor's non-judicial repossession so long as he does not breach the peace. UCC § 9-503 (44-3149). This state authorization of a creditor's private repossession without a prior hearing could also be said to be as repugnant to the Constitution as the invasion of the privacy of a home without a warrant in a criminal matter.

47 395 U.S. 337 (1969).

48 315 F. Supp. 716, 722 (N.D.N.Y. 1970). *But see* Lawson v. Mantell, 62 Misc. 2d 307, 306 N.Y.S.2d 317 (1969), where the court, citing *Sniadach*, held that N.Y. CIV. PRAC. LAW §§ 7101 *et seq.* (McKinney 1963) did not violate the fourteenth amendment requirement of due process. *See also* Termplan, Inc. v. Superior Court, 105 Ariz. 270, 463 P.2d 68 (1969), *noted in* 12 ARIZ. L. REV. 202 (1970), which restricted the application of *Sniadach* to prejudgment wage garnishment.

49 395 U.S. at 340.

ing . . . prejudgment garnishment procedure violates the fundamental principles of due process."[50] The logic of extending *Sniadach* to prehearing repossessions becomes apparent when one considers that the debtor may lose the collateral even though he may have paid virtually all of the purchase price.[51]

One purpose of both the UCCC and the NCA was to resolve some of the problems of non-judicial repossession. The UCCC, however, does not define default, and, like the UCC, provides no standard for determining the materiality of default necessary for the creditor to use non-judicial methods of enforcing his security interest.[52] Once default has been established, the creditor's and debtor's rights under the UCCC are controlled by UCC sections 9-501 *et seq.*, except to the extent that such rights are changed by the UCCC.[53] Once such change is that, in the case of a sale for $1000 or less, the creditor who elects to forego his rights in the collateral and sue on the debt is prohibited from levying and executing on the collateral which was the subject of the consumer credit sale.[54] This creates an anamoly because the UCCC may force the creditor to execute on property which may be more vital to the consumer than the collateral of the credit sale. To avoid this problem, the debtor should be allowed to compel the creditor to levy and execute on any property which will reasonably satisfy the judgment.[55]

Considering the questionable constitutionality of nonjudicial repossessions[56] it might be better to prohibit them and allow creditors either to foreclose the security interest or to sue on the debt. If the creditor elects to sue on the debt, the debtor should have the right to compel the creditor to levy and execute on property which the debtor reasonably chooses. Under such a scheme the debtor could retain that property most vital to him.

After there has been a default and a repossession, the consumer's most important right is the right of redemption. The UCCC gives the consumer the same right that is provided by the UCC: "a right to redeem the collateral at any time before disposition of the collateral or satisfaction of the obligation, by tendering fulfillment of *all* obligations secured by

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[50] *Id.* at 342.

[51] *See, e.g.*, Larson v. Fetherson, 44 Wis. 2d 712, 172 N.W.2d 20 (1969). *But see* Bolthazar v. Mari Ltd., 301 F. Supp. 103 (N.D. Ill. 1969).

[52] W. WILLIER & F. HART, *supra* note 42, ¶ 92.46; *Non-Judicial Repossession, supra* note 36, at 438. *See* NCA § 5.103, Comment 1.

[53] UCCC § 5.103, Comment 1.

[54] *Id.* § 5.103(6).

[55] *Cf.* Blasingame v. Wallace, 32 Ariz. 580, 261 P. 42 (1927), where the court indicated that, pursuant to the predecessor of ARIZ. REV. STAT. ANN. § 12-1553 (1956), a judgment debtor has the right to require that an execution be satisfied out of personal property before executing upon the debtor's realty.

[56] In a case recently filed in the United States District Court for the District of Arizona, the plaintiff is seeking to have prehearing repossession declared unconstitutional. Cisernos v. Burr, Civil No. 70-149 TUC (D. Ariz., filed Oct. 20, 1970), in Daily Reporter, Oct. 21, 1970, at 1, col. 1.

the collateral as well as expenses of the creditor."[57]

The value of this right may be seriously undermined, however, through the application of an acceleration clause. In the absence of an acceleration clause, the amount necessary to redeem after a default in one payment would be only the overdue payment plus the creditor's expenses.[58] Thus, it would not be worthwhile for the creditor to repossess unless the default had become material.[59] Consequently, most security agreements contain acceleration clauses and the amount necessary to redeem is equal to the total amount due on the contract plus the creditor's expenses. If the low income debtor could not afford to make the monthly payment, he surely woud be unable to afford the total of the accelerated payments. The result is that the low income debtor's right to redeem cannot be exercised[60] unless the total of the payments is small.

The UCC states that acceleration clauses

> shall be construed to mean that [the creditor] shall have power to accelerate the payments only if he in good faith believes that the prospect of payment or performance is impaired. The burden of establishing lack of good faith is on the party against whom the power has been exercised.[61]

Since the UCCC is silent as to acceleration clauses, the UCC provisions would apply. The creditor probably would have no difficulty in satisfying the UCC's good faith requirement[62] for accelerating the payments where there has been an actual default in at least one payment,[63] and the burden of proving a lack of good faith is on the debtor. Thus, the debtor's failure to make one payment may subject his property to repossession without an effective right of redemption.

The NCA completely prohibits non-judicial repossession of the security interest[64] arising from a consumer transaction. Thus, it has limited the possibility of any questionable abusive practices which may accompany the over zealous creditor's private repossession. It also avoids the additional problem created by the UCC because there is no need to determine which practices constitute a breach of the peace. For the purpose of judicial repossession, the NCA has defined default as the failure to pay certain installments.[65] If the default is within this definition, the creditor may replevy the collateral. Prior to replevin and within five days af-

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57 UCCC § 5.103, Comment 1 (emphasis added). *See also* UCC § 9-506 (44-3152).
58 UCC § 9-506 (44-3152).
59 Hogan, *supra* note 38, at 210.
60 *Non-Judicial Repossession, supra* note 36, at 439 n.28.
61 UCC § 1-208 (44-2215).
62 *Id.*
63 *Cf.* Fort Knox Nat'l Bank v. Gustafson, 385 S.W.2d 196 (Ky. App. 1964), where the court considered default in payment as one of the necessary elements in directing a verdict for the creditor on the issue of good faith.
64 NCA § 5.204.
65 *Id.* § 5.103.

ter the service of complaint, the debtor may request a hearing on the issue of default.[66] In the absence of such a request the creditor may proceed without a hearing.[67] While the debtor's right to demand a hearing may be meaningless if he is unaware of it, it should satisfy the fourteenth amendment objection against prehearing seizures made in *Laprease v. Raymours Furniture Co.*[68]

The NCA definition of default may have gone too far, however, by requiring the creditor to wait for the debtor's failure to pay:

> (a) three successive installments within the period of time allowable by this Act, or
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> (b) any remaining balance within three months after the due date of the final installment, or
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> (c) an amount resulting from the total of unpaid delinquent installments constituting 30% of the amount financed.[69]

Although the consumer could have lost, destroyed, or completely consumed the collateral before he missed his first installment, the creditor may still have to wait up to three months to bring an action. A failure to pay one installment within 30 days of the due date should constitute default so long as there is a reasonable right to redeem.

Unlike the UCCC,[70] the NCA allows the creditor to elect either to "waive his security interest and pursue his claim to judgment as unsecured or foreclose or otherwise enforce the security interest by any available judicial procedure."[71] This procedure permits the creditor to levy and execute on any of the debtor's non-exempt property including the collateral which was the subject of the credit sale. The debtor should be given the right to compel the creditor to execute on property of the debtor's choice which will reasonably satisfy the judgment.[72] Notwithstanding the creditor's election to waive the security interest, the debtor may voluntarily surrender the collateral. The surrender automatically acts as the enforcement of the security interest by the creditor[73] prohibiting any further action on the debt.[74]

In the event the creditor elects to enforce the security interest, the debtor, within 15 days after the service of the complaint, may cure his default[75] by tendering fulfillment of his current obligation, all payments

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66 *Id.* § 5.208.
67 ARIZ. REV. STAT. ANN. §§ 12-1301, -1302 (1956).
68 315 F. Supp. 716 (N.D.N.Y. 1970).
69 NCA § 5.103.
70 UCCC § 5.103(6).
71 NCA § 5.203(2).
72 By allowing the debtor to choose, within reason, the property upon which the creditor should execute, the debtor will be able to preserve that which is most vital to himself and his family.
73 NCA § 5.205. Apparently the NCA would allow the debtor to surrender the collateral even though it has been severely damaged. The NCA at least should require the collateral to be in good condition.
74 *Id.* § 5.203.
75 *Id.* §§ 5.206, 207.

"scheduled to be due at the time of the tender, plus any unpaid delinquency or deferred charges."[76] If the default is not cured within the 15-day period, the debtor has 30 days following the issue of process to redeem the collateral "by tendering the amount constituting his current obligation [plus] a performance deposit, not to exceed the total of three installments, equivalent to one-third of the total obligation remaining with respect to the customer credit transaction."[77] This gives the debtor sufficient time to raise a reasonable amount of money which will redeem the collateral and allow continued performance of the contract.

EXEMPTION VERSUS ATTACHMENT

The problem of which of the debtor's property should be exempt from attachment is present in both prejudgment and postjudgment situations. The most controversial and undoubtedly the most vital problem to the low-income consumer in this general area is wage garnishment.[78] It is so feared that the mere threat of its use—or garnishment blackmail—is one of the creditor's most effective tools.[79] The debtor's basic problem is not so much that his wages may be withheld but that he may be discharged from employment.[80] Employers not only look upon garnishment as an indicator of an employee's fitness,[81] but they are also forced to incur significant expenses because of it.[82] A recent survey in Seattle, Washington, for example, indicated that 53 percent of the employers discharged employees because "bookkeeping and other related expenses render garnishment an unjustifiable nuisance." The remaining 47 percent answered that "frequent garnishments are such evidence of an employee's bad character and poor credit management as to make him a poor employment risk."[83]

The Boeing Company, Washington's largest employer, now employs five clerks and one supervisor in its Commercial Airplane Division to process more than 500 writs of garnishment each month at an annual cost of $200,000.[84] The company loses the time that the employee spends going to court or to the collector's office. Even if they fire the employee, the company loses the cost of training his replacement. It is easy to

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76 *Id.* § 5.207(2).
77 *Id.* § 5.209(1).
78 *See Project—Wage Garnishment in Washington—An Empirical Study*, 43 WASH. L. REV. 735 (1968) [hereinafter cited as *Project*].
79 *Id.* at 754.
80 Brunn, *Wage Garnishment in California: A Study and Recommendations*, 53 CALIF. L. REV. 1214, 1229 (1965); *Project, supra* note 78, at 754.
81 *Project, supra* note 78, at 756 n.78.
82 *Id.* at 755. ARIZ. REV. STAT. ANN. § 12-1583 (1956): "If a garnishee fails to answer within the time specified in the writ, the court may, after judgment has been rendered against defendant, render judgment by default *against the garnishee for the full amount of the judgment against defendant.*" (emphasis added).
83 *Project, supra* note 78, at 756 n.78. *But see* 15 U.S.C. § 1674 (Supp. V, 1970).
84 *Project, supra* note 78, at 755.

understand, therefore, why some companies will discharge an employee after a single garnishment.[85] It is such a nuisance that union contracts recognize an employer's right to discharge an employee whose wages are garnished more than a certain number of times within a given period.[86]

The fear of discharge has a harsh impact on the employee. When a debtor is faced with the choice of garnishment and the possible loss of employment or having the debt discharged in voluntary bankruptcy, he often selects the latter in order to preserve the steady flow of income.[87] When this occurs the creditor generally gains nothing by garnishment or the threat of it.[88]

In 1968, during House debates concerning the Consumer Credit Protection Act,[89] Congressman Henry B. Gonzales of Texas described one of the causes of consumer bankruptcies:

> For a poor man—and whoever heard of the wage of the affluent being attached?—to lose part of his salary often means his family will go without the essentials. No man sits by while his family goes hungry or without heat. He either files for consumer bankruptcy and tries to begin again, or just quits his job and goes on relief. Where is the equity, the common sense, in such a process?[90]

Personal debts cancelled by consumer bankruptcies, in 1967, reached approximately $1.5 billion.[91]

> In Pennsylvania and Texas, which prohibit the garnishment of wages, the number of nonbusiness bankruptcies per 100,000 population are nine and five respectively, while in those States having relatively harsh garnishment laws, the incidents of personal bankruptcies range between 200 to 300 per 100,000 population.[92]

Thus, there appears to be a direct relationship between the harshness of a state's garnishment law and the number of personal bankruptcies.[93]

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85 Brunn, *supra* note 80, at 1229.

86 Note, *Garnishment in Kentucky—Some Defects*, 45 KY. L.J. 322, 330 (1956-57).

87 For a study of the effects of garnishment on bankruptcy, see Brunn, *supra* note 80.

88 A 1964 survey showed that only 13 percent of personal bankruptcies had any assets available to creditors and out of these the most that was realized was eight cents on the dollar. Countryman, *The Bankruptcy Boom*, 77 HARV. L. REV. 1452, 1453-54 (1964). The main reason for such a low rate of collection is that the administration of the bankrupt's estate takes most of the money in the estate, leaving little or nothing for the creditors. W. HOGAN & W. WARREN, CREDITORS' RIGHTS AND SECURED TRANSACTIONS UNDER THE U.C.C.—CASES AND MATERIALS 2 (1967).

89 15 U.S.C. § 1674 (Supp. V, 1970). This recently enacted federal legislation offers substantial consumer protection in a limited number of areas. The UCCC and the NCA, on the other hand, have attempted complete coverage of the consumer's problems related to the extension of consumer credit.

90 114 CONG. REC. 1833 (1968).

91 H.R. REP. No. 1040, 90th Cong., 1st Sess. 20 (1967).

92 *Id.* at 21.

93 *Id. See also* Brunn, *supra* note 80, at 1229.

To meet the problem, both the UCCC and the NCA have included provisions concerning exemptions and wage garnishments.[94] The UCCC limits both pre- and post-judgment garnishment, allowing the garnishment of only 25 percent of the employee's disposable earnings[95] for the week or the excess earnings over forty times the federal minimum hourly wage,[96] whichever is less.[97] This protects a large portion of a low-income debtor's wages.

A major criticism of restricting the amount of a debtor's wages subject to garnishment as opposed to its complete prohibition is that the creditor will be forced to garnish more frequently to secure the same amount of payment available in a single garnishment before the UCC.[98] This repetitious garnishment puts the debtor's employment in jeopardy leaving him in the same dilemma which exists without the code. The debtor has three basic choices. First, he may petition for voluntary bankruptcy to avoid the garnishment of his wages. Second, if he has the money he may pay the claim to avoid garnishment even though the claim may be contestable. Finally, he may do nothing and allow his wages to be garnished with the risk that he be discharged from employment.

The fear of being fired for garnishment theoretically was dispelled by the *Consumer Credit Protection Act*[99] and the UCCC which states:

> No employer shall discharge an employee for the reason that a creditor of the employee has subjected or attempted to subject unpaid earnings of the employee to garnishment or like proceedings directed to the employer for the purpose of paying a judgment arising from a consumer credit sale, consumer lease, or consumer loan.[100]

This prohibition cannot prevent the harrassed employer from discharging the employee for reasons allegedly unrelated to the garnishment. At the very least, the garnished employee would be subjected to greater scrutiny than other employees. Therefore, even though garnishment firing is prohibited, where garnishment of wages is still permitted the fear of discharge for the slightest mistake and the desire to prevent discharge through bankruptcy will persist.

Section 5.105 of the NCA prohibits pre-judgment attachment of any property and, unlike the UCCC, is not limited to unpaid earnings.[101] In addition, the NCA provides that certain property shall be free from post-judgment attachment:

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94 UCCC §§ 5.104-196; NCA §§ 5.105, 106.

95 The UCCC defines disposable earnings as "that part of the earnings of an individual remaining after the deduction from those earnings of amounts required by law to be withheld." UCCC § 5.105(1)(a).

96 *See also* Fair Labor Standards Act of 1938, 29 U.S.C. § 206(a)(1) (1964).

97 UCCC § 5.105. *See also* 15 U.S.C. § 1673 (Supp. V, 1970); UCCC § 5.104.

98 Comment, *Arizona's Exemption Statute Relative to Earnings for Personal Services: Time for Modernization*, 6 ARIZ. L. REV. 256, 265 (1965).

99 15 U.S.C. § 1674 (Supp. V, 1970).

100 UCCC § 5.106.

101 *Id.* § 5.104.

> The following property of the consumer shall be exempt from levy, execution, sale, and other similar process in satisfaction of a judgment for an obligation arising from a consumer credit transaction:
>
> (a) unpaid earnings;
>
> (b) household furnishings—appliances and clothing of the consumer and his dependents;
>
> (c) real property used as the principal residence of the consumer or his dependents;
>
> (d) other property necessary for the maintenance of a moderate standard of living for the consumer and his dependents.[102]

NCA sections 5.105 and 5.106 clearly enable the consumer to retain his unpaid earnings free from attachment in satisfaction of a consumer obligation.[103] While the NCA's complete prohibition of wage garnishment avoids the UCCC's shortcomings, it may have gone too far in protecting the consumer from the attachment of other property. Section 5.106(1)(c) would allow a debtor to tie up a good deal of money in "real property used as the principal residence."[104] Section 5.106(1)(d), which provides for the exemption of other property necessary for a "moderate standard of living," is open to interpretation by the courts.

> Where the standard 'necessity'—possibly moderate and adequate—is interpreted to vary according to what the debtor is accustomed to as is the case in some instances, it is possible for a debtor accustomed to the 'better things of life' to be protected in his possession of elegant and costly wearing apparel . . . and household furnishings, and [a] . . . large income as against the just claims of a creditor in circumstances far more modest.[105]

If one accepts the premise that prevention of bankruptcies is more important than the preservation of wage garnishment as a creditor's tool, the best solution is a complete prohibition against both pre-judgment and post-judgment wage garnishment. As long as wage garnishment is permitted, the fear of discharge and the desire to prevent that discharge through bankruptcy will persist.[106] A major criticism of the complete prohibition of wage garnishment is that the creditor will cease to extend credit to the low-income debtor. This argument loses its appeal, however,

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102 NCA § 5.106(1).

103 *Id.*, Comment 1.

104 The NCA definition of "consumer" includes a person who acquires real property for family purposes. NCA § 1.301(8). Therefore, section 5.106 which exempts a principal residence from "levy, execution, sale, and other similar process in satisfaction of a judgment for an obligation arising from a consumer credit transaction," could prevent a mortgagee from foreclosing a mortgage on a principal residence. Under these circumstances it is hard to imagine a creditor who would take a mortgage on a principal residence. Any state considering adoption of the NCA should certainly allow foreclosure in such instances.

105 Karlen, *Exemptions from Execution*, 22 BUS. LAW. 1167, 1168-69 (1967).

106 Brunn, *supra* note 80, at 1237.

when one considers the increasing rate of bankruptcies in those states which permit wage garnishment[107] with the likelihood that the creditor's claim will be discharged in bankruptcy. The possibility that a claim may be completely discharged surely offers as great an incentive for not extending credit to low-income debtors as a prohibition of wage garnishment.

If wage garnishment is allowed to continue it may leave the debtor a jobless charge on society. His potential for acquiring any property, paying other obligations, and paying the remainder of the garnishor's claim would be seriously impaired. In addition the debtor may be encouraged to have his debts discharged in bankruptcy so that any future employment would not be jeopardized by the threat of garnishment.

The NCA prohibits wage garnishments, but it gives the debtor too much protection from the attachment of his other property. The act should incorporate a limitation on the dollar value of the exempted "principal residence" in order to avoid the injustice of allowing the debtor to invest money in a costly residence at the expense of the creditor. In addition, the "moderate standard of living" exemption should be defined in terms of a community average standard of living. In the absence of such a definition the "moderate standard of living" could possibly be interpreted by a court as a standard to which the debtor has become accustomed.

TRANSFERABILITY VERSUS THE CONSUMER

Holder In Due Course

A creditor achieves the status of a holder in due course when he takes a negotiable instrument "(a) for value; and (b) in good faith; and (c) without notice that it is overdue or has beenn dishonored or of any defense against or claim to it on the part of any person."[108] The creditor who has not dealt with the obligor and who has attained HDC status can collect on the instrument free of the debtor's personal defenses or other claims against the seller.[109]

The potential injustice of permitting a creditor to beomce an HDC is shown by the following example. Suppose Mr. Doe, a consumer, makes a credit purchase of a stove from a local appliance dealer. When he makes the purchase, Doe signs a negotiable note which the dealer later sells to a finance company which takes as an HDC. The night after selling the note this particular dealer leaves town without delivering the stove. At this point Doe refuses to pay because he feels he should not have to pay for something he did not receive. In the creditor's suit to collect the note, the primary question is the allocation of loss between the innocent consumer and the innocent creditor.[110] On one hand, the court desires

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107 *Id.* at 1234-39. *Cf.* H.R. REP. No. 1040, 90th Cong., 1st Sess. 20-21 (1967).
108 UCC § 3-302(1) (44-2532(A)).
109 *Id.* § 3-305 (44-2535).
110 Comment, *Negotiable Instruments: Consumer Versus Financier In Con-*

to protect the consumer from the seller's abusive practices and, on the other hand, to preserve the free negotiability of commercial paper.[111] Under the present status of the law,[112] failure of consideration is not a defense against an HDC and Doe would have to pay the finance company the amount of the note even though he did not receive the stove. Such may be the injustice of the HDC doctrine.

The purpose of allowing HDC status is to preserve free negotiability of commercial paper by severely limiting the maker's defenses.[113] Free negotiability enables the dealer to acquire additional capital by selling the consumer notes. The argument in favor of preserving HDC status is that if the consumer's defenses were not cut off, the finance company would not purchase the dealer's notes. Therefore, the dealer would probably be unable to acquire new inventory or he would be forced to sell strictly on a cash basis and not extend credit to consumers.

On the other hand, without his personal defenses the unsophisticated consumer may very well find himself in the position of Mr. Doe. The proposals to date have treated the two goals as mutually exclusive and have attempted to shift the risk of loss to the party better able to bear it. Those who favor consumer protection feel that the finance company should bear this risk since it, rather than the unsophisticated consumer, has the means and the ability to investigate the dealer.[114]

The traditional methods of overcoming the HDC status through the doctrines of "good faith without notice," "close connection," and "original party"[115] are ineffective because they can be circumvented by a second or third transfer of the note so that the ultimate transferee is a holder in due course. The UCCC failed in its attempt to preserve the consumer's defenses by ineffectively limiting the availability of HDC status. The relevant portion states:

> In a consumer credit sale or consumer lease, other than a sale or lease primarily for an agricultural purpose, the seller or lessor may not take a negotiable instrument other than a check as evidence of the obligation of the buyer or lessee. A holder is not in good faith if he takes a negotiable instrument with notice that it is issued in violation of this section. A holder in due course is not subject to the liabilities set forth in the provisions on the effect of violations on rights of parties . . . and

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sumer Goods Financing—A Judicial Dilemma, 52 MARQ. L. REV. 285, 286 (1968) [hereinafter cited as *Negotiable Instruments*]. For a more comprehensive statement of the problem, see Littlefield, *Good Faith Purchase of Commercial Paper: The Failure of the Subjective Test*, 39 S. CAL. L. REV. 48 (1966).

111 *Negotiable Instruments, supra* note 110, at 286, *citing* Griffin v. Baltimore Fed. Sav. & Loan Ass'n, 204 Md. 154, 159, 102 A.2d 804, 806 (1954).

112 UCC §§ 3-302 *et seq.* (44-2532 *et seq.*).

113 *Negotiable Instruments, supra* note 110, at 286. *Cf.* UCC § 3-305(2) (44-2535(B)).

114 30 OHIO ST. L.J. 604, 608 (1969).

115 For a discussion of these doctrines, see *Negotiable Instruments, supra* note 110.

the provisions on civil actions by Administrator.[116]

The UCCC would have protected the consumer from HDC status if it had stopped with the prohibition against negotiable instruments in consumer credit sales. The remainder of the provision, however, effectually nullifies any consumer protection. The comment to this section states that "it is possible that in rare cases second or third takers may not know of an instrument's consumer origin; in this unusual situation the policy favoring negotiability is upheld in order not to cast a cloud over negotiable instruments generally."[117] This "unusual situation" could quickly become the ordinary occurrence, however, if it proves to be an effective method of achieving HDC status.

The injustice of the HDC doctrine arises only when the seller is unavailable or unable to satisfy the buyer's claim. An unscrupulous seller probably would not hesitate to take a negotiable instrument in a consumer transaction, yet this is precisely the type of seller from whom the consumer must be protected. If the instrument is negotiated to a true HDC, the UCCC's protection of the consumer against HDC status would be rendered completely ineffective.

The NCA, on the other hand, has abolished the HDC concept in the consumer context:

> (1) No lender, seller or lessor shall take or otherwise arrange for the consumer to sign an instrument payable 'to order or to bearer' as evidence of the credit obligation of the consumer in a consumer credit transaction or a consumer lease.
>
> (2) Any holder of an instrument, contract or other writing evidencing an obligation of the consumer takes it subject to all claims and defenses of the consumer up to and including the total amount of the transaction total arising out of the transaction whether or not it is payable 'to order or to bearer.'[118]

The NCA has effectively prohibited the creation of a negotiable instrument where the proceeds of the instrument are used by a consumer for the acquisition of consumer goods.[119] In addition, it has provided that any holder of an instrument evidencing a consumer obligation is subject to the consumer's defenses arising out of the transaction.[120] These defenses appear to include the defenses the consumer may have against the seller of the consumer goods, even though the instrument arose out of a direct loan to the consumer, the proceeds of which were used to purchase consumer goods.[121]

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116 UCCC § 2.403.

117 *Id.* Comment.

118 NCA § 2.405. Arizona has recently enacted legislation which abolishes negotiable instruments and nullifies waiver of defense clauses in instruments made by a buyer in a "home solicitation sale." ARIZ. REV. STAT. ANN. § 44-5005 (Supp. July 1970).

119 *Compare* NCA §§ 1.301(8), (10), (12), (19), (23), *with* 2.405.

120 *Id.* § 2.405(2).

121 The inference that the NCA would subject the creditor who makes a

Nevertheless, the drafters of the NCA found it necessary to codify the "original party" doctrine[122] under which the lender who supplies the seller with the negotiable instrument forms is considered to be an original party to the sales contract and subject to the consumer's defenses arising out of the sale. The relevant part of the NCA states:

> The creditor in consumer loan transactions shall be subject to all of the claims and defenses of the consumer up to the total amount financed, arising from the consumer sale or lease for which the proceeds of the loan are used, if the creditor participated in or was connected with the consumer sale or lease transaction.[123]

The codification of the "original party" doctrine would be superfluous if the creditor who makes a direct loan would be subject to the consumer's defenses arising from the purchase of consumer goods with the proceeds of that loan. Perhaps the drafters of the NCA did not intend to subject the financier who makes a direct loan to the consumer's defenses. Nevertheless, the NCA can be construed to subject the financier who makes a direct loan to the consumer's defenses. If the NCA is so construed it has gone too far. The creditor who makes a fully secured loan without any inquiry as to the use of the loan proceeds may find his claim for repayment defeated by the consumer's defenses when the proceeds are used to purchase consumer goods. The NCA needs to define precisely which loans will be subject to defenses arising out of the purchase of consumer goods with the loan proceeds.

Opposition to abolishing HDC status is based on the sincere fear that credit institutions would cease to purchase negotiable instruments from small dealers and consequently, credit would be denied to many consu-

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direct loan to the consumer to the consumer's defenses arising out of the purchase of consumer goods with the loan proceeds comes from a careful analysis of the following sections of the NCA. Only the relevant portions of the sections are set out.

NCA § 2.405:

> (1) No lender . . . shall take or otherwise arrange for the consumer to sign an instrument payable "to order or to bearer" as evidence of the credit obligation of the consumer in a consumer credit transaction or a consumer lease.
>
> (2) Any holder of an instrument, contract or other writing evidencing an obligation of the consumer takes it subject to all claims and defenses of the consumer . . . arising out of the transaction whether or not it is payable to "order or to bearer".

NCA § 1.301(19): " 'Lender' means a merchant regularly engaged in the business of making consumer loans."

NCA § 1.301(23): " 'Merchant' means a person who regularly advertises, distributes, offers, supplies or deals in . . . credit in a manner which directly or indirectly results in or is intended or designed to result in, lead to or induce a consumer transaction."

NCA § 1.301(12): " 'Consumer loan' means a loan made by a lender to a consumer. . . ."

NCA § 1.301(8): " 'Consumer' means a person other than an organization who seeks or acquires . . . credit for personal, family, household or agricultural purposes."

122 *Negotiable Instruments, supra* note 110.

123 NCA § 2.407(1).

mers. Although finance companies probably would continue to purchase instruments from reputable dealers to whom they could always look for reimbursement, the abolition of HDC may be fatal to the new businessman who has not yet established his good name.

The protection of negotiability on the one hand and the preservation of the consumer's personal defenses on the other have been treated by both the UCCC and the NCA as if they were mutually exclusive. This need not be so. One possible method for simultaneously preserving the HDC status and protecting the consumer would be to require the seller of consumer goods to post a bond with the Consumer Protection Agency[124] to hold the consumer harmless. If the consumer could join the seller as a third party defendant to an HDC's action on the debt or foreclosure action, the consumer's claim against the seller could be adjudicated in the same action. The seller could be joined by serving the Consumer Protection Agency as statutory agent where the seller is no longer available. In any event, once the consumer's claim has been adjudicated he could satisfy any favorable judgment first against the seller or, if he is unavailable, against the bond which has been posted with the Consumer Protection Agency. The HDC could obtain his judgment free from the consumers defenses and the consumer would have his protection either by initiating his own action against the seller or by joining him as a third party defendant in an action initiated by the HDC.

The Waiver Of Defense Clause

The effect and purpose of waiver of defense clauses is to give conditional and installment sales contracts characteristics similar to those of negotiable instruments,[125] *i.e.*, the consumer's defenses do not run with the contract. It follows, therefore, that the problems resulting from the HDC doctrine also confront the consumer where a waiver of defense clause is used. Indeed, the status of an assignee free from the consumer's defenses may be easier to achieve than that of an HDC.

> For example, a holder in due course must take a negotiable instrument without notice that it is overdue, while there is no such requirement for an assignee; the value which the holder in due course must give is defined in [UCC] Section 3-303 more restrictively than the general definition of 'value' in [UCC] Section 1-201(44) which is all that is required of the assignee.[126]

Prior to the adoption of the UCC, waiver of defense clauses were

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[124] The Consumer Protection Agency referred to here would be the one contemplated by both the UCCC and the NCA. UCCC §§ 6.101 *et seq.*; NCA §§ 6.101 *et seq.*

[125] For a more complete discussion of how and why the waiver of defense clause came into being, see Navin, *supra* note 3.

[126] W. WILLIER & F. HART, *supra* note 42, ¶ 92.43.

validated or invalidated on the basis of public policy.[127] The UCC has recognized such clauses, however, "[s]ubject to any statute or decision which establishes a different rule."[128] Arizona has a statute which has been construed to invalidate waiver of defense clauses insofar as they attempt to reach defenses which exist against the seller at the time the assignee of the sales contract notifies the consumer of the assignment.[129] Therefore, any defenses which arise after the transfer—such as a subsequent discovery that the consumer item is defective—could still be cut off as to an assignee of the contract by the use of a waiver of defense clause.

The UCCC has provided two alternative treatments for waiver of defense clauses.[130] Alternative A subjects the seller's assignee[131] to the claims and defenses of the buyer or lessee notwithstanding any agreement to the contrary.[132] Alternative B presents a compromise between complete negotiability and Alternative A.[133] It allows the assignee to enforce the waiver of defense clause as to any defenses or claims which arise prior to three months after notice of the assignment so long as the buyer does not give notice prior to that time.[134]

A New York statute goes beyond Alternative B by allowing the good faith assignee to take free of defenses if the consumer is notified of the assignment, invited to notify the assignee of any defenses, and fails to do so within ten days after the notice was mailed to the consumer at the address shown on the contract.[135] These notice statutes, which have been criticized as being more beneficial to the creditor than the consumer,[136] are subject to four significant weaknesses. First, if the consumer has a defense and does not notify the assignee, the assignee has a strong negotiating position with the consumer by telling him that he can no longer complain.[137] Another fault is the necessity for affirmative and quick action on the part of the consumer.[138] Similarly, the notice may be ineffective to the unsophisticated consumer who may find it tucked away among his junk mail or on the inside cover of his payment book where it appears to be only information relating to his payments. Finally, such a statute gives the consumer the impression that all his defenses are waived

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127 Navin, *supra* note 3, at 508.
128 UCC § 9-206 (44-3119).
129 San Francisco Sec. Corp. v. Phoenix Motor Co., Inc., 25 Ariz. 531, 220 P. 229 (1923); ARIZ. REV. STAT. ANN. § 44-144 (1967).
130 UCCC § 2.404.
131 It should be noted that section 2.404 of the UCCC does not pertain to the assignee of the rights of a lender who makes a consumer loan. *Compare* UCCC § 3.104, *with* §§ 2.104 *and* 2.106.
132 *Id.* § 2.404 (Alternative A).
133 Jordan & Warren, *supra* note 3, at 436.
134 UCCC § 2.404 (Alternative B).
135 N.Y. PERS. PROP. LAW §§ 302.9, 403.3 (McKinney Supp. 1970).
136 Jordan & Warren, *supra* note 3, at 435.
137 *Id.*
138 The three-month period under the UCCC would not require quick action on the part of the consumer, but it may still be criticized for requiring an affirmative action by the consumer. *See* UCCC § 2.404.

by specific statutory mandate, even though there may be other grounds to challenge the assignee's status such as the requirement of good faith.[139] An additional criticism of the New York statute is that it allows only ten days from the date that notice of the assignment was mailed for the debtor to respond. Such a short period of time may possibly elapse while the letter is in transit. Even a diligent debtor may take more than ten days to respond to the notice of assignment.

The corresponding NCA section, on the other hand, states: "Notwithstanding any term or agreement to the contrary, an assignee of the rights of the creditor is subject to all claims and defenses of the consumer arising out of a consumer credit transaction or consumer lease."[140] This prohibition against waiver of defense clauses would have the same effect as UCCC section 2.404, Alternative A ,except that the UCCC treats consumer credit sales and consumer loans separately.[141] The UCCC prohibitions against negotiable instruments[142] and waiver of defense clauses,[143] to the extent they are effective, do not apply to consumer loans.

The separate treatment of consumer sales and consumer loans under the UCCC may to a large extent nullify any protection that the UCCC attempted to give the consumer. For example, if a consumer took out a loan from a finance company and used it to purchase a consumer item he would be unable to raise any defenses or claims he may have pursuant to the sale against the finance company. But if he purchased the same item from the same seller on an installment sales contract which was later assigned to the finance company, he could raise his defenses or claims, to the extent that UCCC section 2.404 is effective, despite a waiver of defense clause. Thus, under the UCCC, the seller of consumer goods theoretically could utilize waiver of defense clauses merely by drafting the contract so that the intended assignee becomes instead the lender.

The NCA, on the other hand, by making its prohibitions against negotiable instruments[144] and waiver of defense clauses[145] applicable to consumer credit transactions,[146] has abolished negotiability and invalidated waiver of defense clauses in consumer loans.[147] In addition, any future assignees of the contract are subject to the consumer's defenses.[148] The NCA has gone too far by subjecting the lender who has made a direct loan to the consumer on a nonnegotiable contract to the consumer's defenses arising out of the purchase of consumer goods with the

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139 Jordan & Warren, *supra* note 3, at 435 & n.139.
140 NCA § 2.406.
141 *Compare* UCCC § 2.104, *with* § 3.104.
142 *Id.* § 2.403.
143 *Id.* § 2.404.
144 NCA § 2.405.
145 *Id.* § 2.406.
146 *Id.* § 1.301(10).
147 *Id.* § 2.405(1), (2). *See also* note 121 *supra.*
148 NCA § 2.406.

loan proceeds.[149]

Legislation which purports to prohibit negotiable instruments in consumer sales[150] without a complete prohibition against waiver of defense clauses as well,[151] is ineffective. The reason for waiver of defense clauses was to circumvent possible defects in the negotiable instruments.[152] For a sanction against negotiable instruments to be effective there must also be a prohibition against waiver of defense clauses. Even if HDC status is retained under certain conditions,[153] however, the very existence of a waiver of defense clause could convince the unsophisticated consumer that he has waived his defenses. Therefore, the waiver of defense clause should be expressly prohibited.

CONCLUSION

Although both the UCCC and the NCA were drafted to combat some of the evils confronting consumers, only the latter proposal approximates that goal. The NCA is sometimes overly protective of the consumer at the expense of the creditor.[154] But the NCA proposals to abolish nonjudicial repossession,[155] wage garnishment,[156] and waiver of defense clauses,[157] if modified as has been suggested appear to be in the best interests of both the consumer and the honest and diligent creditor and should be seriously considered for adoption. Adequate consumer protection is imperative in the problem areas of debt collection practices, repossessions, exemptions from attachment, holder in due course status, and waiver of defense clauses.

The controversy surrounding abolishing the holder in due course doctrine as it now exists under the UCC is one of the most important issues confronting consumer protection interests as well as the entire credit structure. Neither the UCCC or the NCA have offered a proposal which protects both the creditor and the consumer, but it is submitted that the protection of both is possible. By placing the risk of loss upon the party who gave rise to the consumer's claim or defense—the seller of the consumer goods—through the requirement of a bond to hold the consumer harmless, the "free flow of credit" can be essentially preserved.

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149 *See* note 121 and accompanying text *supra*. A further illustration of the differences between the NCA and the UCCC is their application to the waiver clauses found on the typical bank credit card agreements. Since extension of credit on a bank card is a loan, Jordan & Warren, *supra* note 3, at 437, the waiver would be effective under the UCCC but of no effect under the NCA. *See id.* at 438.

150 *E.g.*, UCCC § 2.404 (Alternative A).

151 *E.g.*, *id.* (Alternative B).

152 Navin, *supra* note 3, at 509.

153 *See* text accompanying note 124 *supra*.

154 *See* text accompanying note 69 *supra*.

155 *See* text accompanying notes 58-60, 64 *supra*.

156 *See* text accompanying notes 78-107 *supra*.

157 *See* text accompanying notes 125-146 *supra*.