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Douglas W. Smith

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Seller Alone Is Liable for Failure To Make 'Credit-Sale' Disclosures

In *Manning v. Princeton Consumer Discount Co.,*[1] the U.S. Court of Appeals for the Third Circuit held that in a credit sale, only the dealer is responsible for making the required credit sale disclosures, even though both a finance company and an automobile dealer are creditors under the Truth in Lending Act.[2]

Mrs. Manning, the plaintiff, agreed to purchase an automobile from Springfield Dodge, Inc., after it assured her that financing was available. The financing was a loan arranged by Springfield and extended by the Princeton Consumer Discount Company. Princeton sent Mrs. Manning a check payable to her, and she indorsed it to Springfield. Springfield received a commission from Princeton.

Mrs. Manning later sued for statutory penalties and injunctive relief against both Springfield and Princeton. She asserted that the defendants had failed to make certain disclosures required in credit sales by the Truth in Lending Act. She specifically complained of failure to disclose the cash price of the car, the amount of the loan payment and the unpaid balance of the cash price.

The district court held that only the dealer, Springfield, was liable for failing to make the disclosures required by 15 U.S.C.A. §1638,[3] which relates to credit sales. The court held that Princeton, as a lender, was not required to make disclosures other than those required by 15 U.S.C.A. §1639,[4] which relates to disclosures in consumer loan transactions.

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1. 533 F.2d 102 (3rd Cir. 1976).
2. Truth in Lending Act, 15 U.S.C.A. §1601-65 (1970) [herein cited as the Act].
3. Truth in Lending Act, 15 U.S.C.A. §1638, states that the "creditor" in a consumer credit sale shall disclose the following items:
   (1) the cash price;
   (2) amounts credited as down payment;
   (3) the difference between cash price and down payment;
   (4) all other items in amount of credit extended but not part of the finance charge;
   (5) the total amount to be financed;
   (6) the amount of the finance charge;
   (7) due dates of payments;
   (8) default charges in case of late payments;
   (9) a description of the security interest.
4. Truth in Lending Act, 15 U.S.C.A. §1639, states that any "creditor" in a consumer loan transaction (as opposed to a credit sale) shall disclose the following:
   (1) the amount of credit the obligor will have actual use of;
   (2) all charges in the credit extended but not in finance charge;
   (3) the total amount to be financed;
   (4) the amount of the finance charge;
   (5) the finance charge expressed as an annual percentage;
   (6) due dates of payments;

Mrs. Manning appealed. She contended that 15 U.S.C.A. §1631(a), the general disclosure provision in the Act,[5] requires both Springfield and Princeton, as creditors, to make the credit-sales disclosures and that their dual failure made them jointly and severally liable.

The Truth in Lending Act is a congressional response "to the American consumer's rapidly growing need for disclosure and standardization of credit information."[6] It is based on the premise that blind economic activity of the consumer is inconsistent with an efficient economic system.[7] The field of credit has become "such an impenetrable jungle of confusing terms and incomprehensible concepts for the average consumer"[8] that legislation was necessary. The Act embodies a broad, remedial scheme to insure meaningful disclosure of credit terms, which helps the consumer credit-shop and avoid uninformed and inefficient use of credit.[9] Each creditor is required by 15 U.S.C.A. §1631(a) to clearly disclose all required information to each credit recipient. Both Congress and the courts have urged a liberal, policy-oriented construction of this general disclosure provision. The historical philosophy of caveat emptor has been buried; the current theme is "let the seller disclose."[10] In *Thomas v. Meyers-Dickson Furniture Co.*,[11] the court, supporting what seemed to be an unfair decision against a creditor, said the Act's implied goal was to create a system of "private attorney generals" to aid in the enforcement of the Act. In other words, the disclosure requirements of 15 U.S.C.A. §1631(a) are necessarily broad and encourage a liberal consruction to deal with a myriad of complex circumstances found in credit transactions.[12]

The case law reflects this liberal spirit in allotting creditor liability between a dealer and a third-party finance company to which commercial paper has been assigned or from which loans have been extended. Most of the controversy has centered around the question of who qualifies as a creditor. Congress defined creditors as all who "regularly extend, or ar-

(7) default charges for late payments;

(8) a description of the security interest.

Cash price and down payment, necessary in credit sales, do not exist in consumer loan transactions.

5. Truth in Lending Act, 15 U.S.C.A. §1631(a), reads: "Each *creditor* shall disclose clearly and conspicuously, in accordance with the regulations of the Board, to each person to whom consumer credit is exended and upon whom a finance charge is or may be imposed, the information required under this part." (Emphasis added.)

6. McCormick, *Truth in Lending Act Legislation: Concurrent Recourse to Rescission and the Civil Penalty*, 43 GEO. WASH. L. REV. 840 (1975).

7. *See* Mourning v. Family Publications Serv., 411 U.S. 356, 363-364 (1973).

8. H.R. 1040, 90th Cong., 2d Sess. (1968).

9. 15 U.S.C.A. §1601 (1970).

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

11. 479 F.2d 740, 748 (5th Cir. 1973) (failure to include cost of credit life insurance as part of "finance charge").

12. See Peyton v. Rowe, 391 U.S. 54 (1967); N. C. Freed Co. v. Board of Governors of Federal Res. Sys., 473 F.2d 1210 (2d Cir. 1973).

range for the extension of credit for which the payment of a finance charge is required."[13] The Act thus contemplates both "arrangers"[14] and "extenders"[15] who perform their respective functions on a regular basis in credit sales.[16]

Guided by these definitions, many courts quickly developed a pattern in which both the dealer and the finance company are jointly responsible for making the disclosures required by the general disclosure clause, §1631(a), if both were classified as creditors. The determination that both the finance company and the dealer were creditors was based on the policy-oriented "conduit theory"—a theory used to depict the close, systematic relationship between a dealer and a finance company through which the dealer has arranged credit. In other words, most courts believe that after continuous dealings with a particular dealer, the finance company should be viewed as a credit extender (creditor) since the conduit of the seller (also a creditor) has arranged for the credit. The first articulation of the conduit theory appeared in *Garza v. Chicago Health Club, Inc.*[17] The Chicago Health Club, after enlisting new members, immediately assigned to a finance company the individual membership installment contracts. The members were then obligated to pay their dues directly to the finance company. The district court rejected the finance company's argument that it was merely an assignee of the club's membership dues and held that assignees of consumer installment contracts are credit extenders if they regularly extend credit through assignors. The assignees become liable as creditors under the Act. The court declared that "lenders may not escape TIL [Truth in Lending] status as creditors by using sales companies as 'front men'."[18]

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13. 15 U.S.C.A. §1602(f) (1970). Regulation Z, 12 C.F.R. §226.2(s) (1971), states: "'Creditor' means a person who in the ordinary course of business regularly extends or arranges for the extension of consumer credit, or offers to extend or arrange for the extension of such credit, which is payable by agreement in more than four installments, or for which the payment of a finance charge is or may be required, whether in connection with loans, sales of property or services, or otherwise."

Regulations Z is a body of regulations designed by the Board of Governors of the Federal Reserve System to carry out the purposes of the Truth in Lending Act. The Board's authority to prescribe regulations is in 15 U.S.C.A. §1604 (1970).

14. Regulation Z, 12 C.F.R. §226.2(h), states: "'Arrange for the extension of credit' means to provide or offer to provide consumer credit which is or will be extended by another person under a business or other relationship pursuant to which the person arranging such credit (1) receives or will receive a fee, compensation or other consideration for such service, or (2) has knowledge of the credit terms and participates in the preparation of the contract documents required in connection with the extension of credit."

15. Regulation Z provides no definition for "extender." *See* Eby v. Reb Realty, Inc., 495 F.2d 646 (9th Cir. 1974).

16. In 12 C.F.R. §226.2(t), a credit sale is defined as "any sale with respect to which consumer credit is extended or arranged by the seller."

17. 347 F. Supp. 955 (N.D. Ill. 1972).

18. *Id.* at 964.

It thus became accepted law that when "a finance company becomes an integral part of the seller's financing program, the finance company must bear the full responsibility for all disclosures required under the Truth in Lending Act."[19] As recently as 1976, the conduit theory was offered in *Meyers v. Clearview Dodge Sales, Inc.*,[20] in which the Fifth Circuit deduced that the existence of a credit arranger necessarily implied the existence of an extender and held both parties liable as creditors under the Act. The court characterized the finance company as an extender because it alone assumed the risks normally associated with the extension of credit. As confirmation of the entrenchment of the conduit theory, the Eighth Circuit in *Joseph v. Norman's Health Club, Inc.*[21] declared, "We find, as have all but one of the courts faced with similar facts, that where the third party financer becomes intimately involved in the relevant credit transactions it may become liable as an extender of credit."[22]

Initially, the court in *Manning* followed the conduit analysis found in the line of cases from *Garza* to *Meyers*. There was not a direct assignment of Mrs. Manning's loan to a finance company; instead, a Springfield employee drove the plaintiff to the Princeton office, where the loan was extended. The court nevertheless determined that both Springfield (as arranger) and Princeton (as extender) were creditors under the Act. That determination would, under the conduit theory, lead automatically to liability of both "creditors" for failure to disclose under §1631(a). The Third Circuit, however, departed at this point from the conduit theory and refused to impose automatic liability on both creditors. Viewing the transaction as a multiple-creditor situation, the court disregarded §1631(a) and relied on Regulation Z, 12 C.F.R. §226.6(d), which deals specifically with multiple creditor transactions:

> If two or more creditors make a joint disclosure, each creditor shall be clearly identified. The disclosures required under paragraphs (b) and (c) of §226.8[23] *shall be made by the seller* if he extends or arranges for the extension of credit. Otherwise disclosures shall be made as required under paragraphs (b) and (d) of §226.8. [Emphasis added.]

19. Joseph v. Norman's Health Club, Inc., 532 F.2d 86, 92 (8th Cir. 1976).
20. 539 F.2d 511 (5th Cir. 1976).
21. 532 F.2d 86 (8th Cir. 1976).
22. *Id.* at 91. *See* Kriger v. European Health Spa, Inc., 363 F. Supp. 334 (E.D. Wis. 1973); Glaire v. LaLanne-Paris Health Spa, Inc., 12 Cal. 3d 915, 117 Cal. Rptr. 541, 528 P.2d 357 (1974); Starks v. Orleans Motors, Inc., 372 F. Supp. 928 (E.D. La. 1974), *aff'd mem.*, 500 F.2d 1182 (5th Cir. 1976); Philbeck v. Timmers Chevrolet, Inc., 361 F. Supp. 1255 (N.D. Ga. 1973); *rev'd on other grounds*, 499 F.2d 971 (5th Cir. 1974); Stefanski v. Mainway Budget Plan, Inc., 326 F. Supp. 138 (S.D. Fla. 1971).
23. Regulation Z, 12 C.F.R. §228 (1971), lists the specific disclosures required by Regulation Z and the Act. Section (a) is a general disclosure clause which tracks 15 U.S.C.A. §1631 in the Act. Section (b) lists disclosures required in both credit sales and consumer loans. Section (c) lists disclosures required only in credit sales and tracks 15 U.S.C.A. §1638 in the Act. Section (d) lists disclosures required only in loans and tracks 15 U.S.C.A. §1639 in the Act.

The court then noted that subparagraphs (b) of §226.8 lists the disclosures required in both credit sales and consumer loans. Subparagraph (c) of §226.8 lists disclosures required in credit sales by 15 U.S.C.A. §1638; subparagraph (d) pertains only to disclosures required in consumer loans by §1639. Interpreting the second sentence of §226.6(d), the court held that if the transaction was one in which the seller arranges credit, the obligation of disclosure fell solely upon him. According to the Court,

> [w]hether both or only one of them is responsible for making the statutory disclosures is not specified in the statute. While §121, 15 U.S.C. §1631 says that each creditor shall disclose to each person the information required, the Board [of Governors of the Federal Reserve System] has not considered that section as being applicable to the multiple creditor transaction. Practical considerations lead to the conclusion that needless duplication . . . is neither necessary to the Act's purpose nor justifiable in terms of expense.[24]

Since the burden of disclosure fell on the car dealer that arranged Mrs. Manning's credit, the Princeton finance company was absolved of all liability for failing to make the credit-sale disclosures. The Third Circuit acknowledged that its holding in *Manning* was opposite to results reached in the earlier conduit cases, but it distinguished those cases by simply stating their unexplained failure to consider or discuss §226.6(d). Indeed, both the conduit cases and *Manning* agree that both the dealer and the finance company are creditors under the Act in such situations. The conduit cases, however then abruptly halted their analysis and imposed automatic liability on both creditors. The Third Circuit proceeded one step further and, under a detailed application of the multiple-creditor section in Regulation Z, imposed singular liability on the automobile dealer and not on the finance company.[25]

The *Manning* decision is a classic example of sound statutory construction coupled with adequate adherence to the public policy notions behind the Truth in Lending Act. The conduit theory cases from *Garza* to *Meyers*, in their effort to promote the best interests of the consumer, perfunctorily ignored a specific regulation, §226.6(d), which specifically deals with multiple-creditor transactions. In *Manning*, the court, through a well-structured reading of the regulation, has sacrificed little if any consumer protection, and at the same time has provided a logical answer to multiple-creditor liability that seems to coincide with the intent of Congress:

> The plaintiff's position that both seller and lender must supply the same information appears to be based on a "fail safe" theory, i.e., it is

24. 533 F.2d at 105.

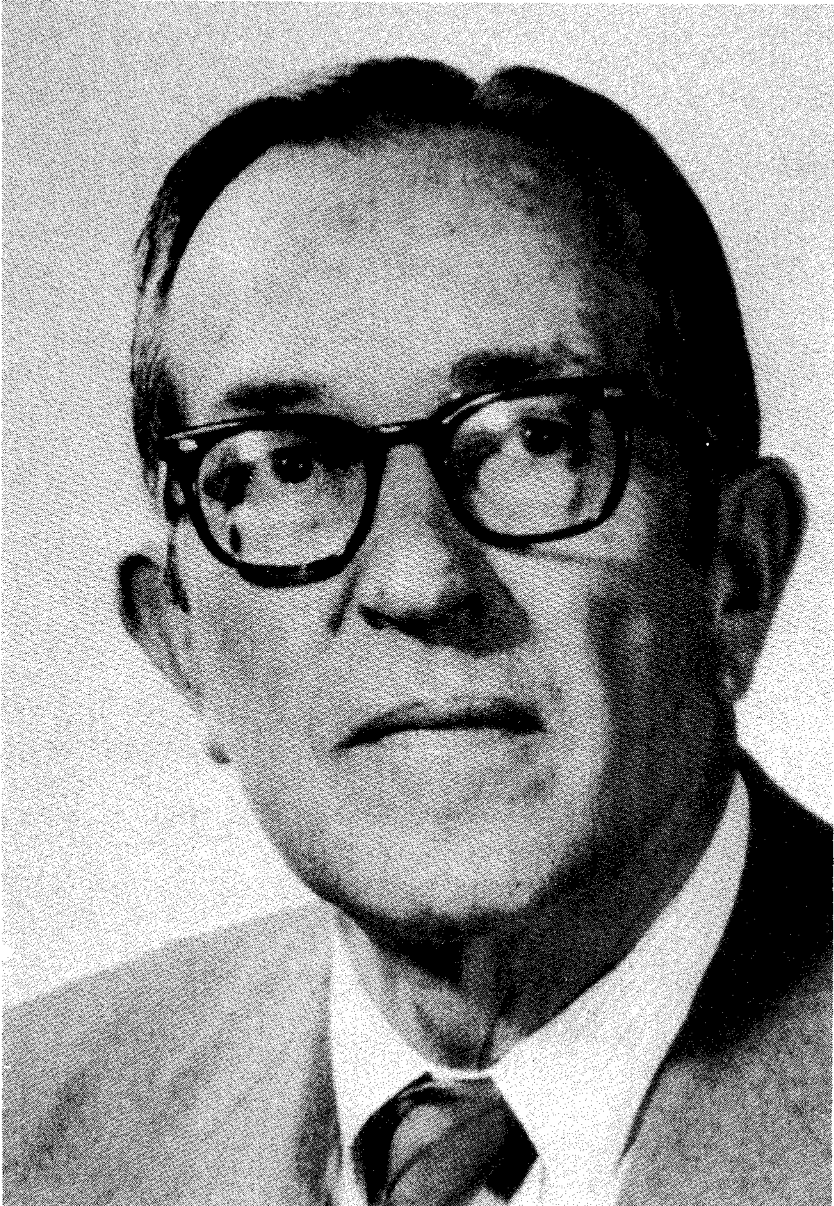
25. The *Manning* analysis also appeared in Boggan v. Euclid Nat'l Bank, Civil No. 75-1177 (6th Cir. 1975).

26. 533 F.2d at 106.

> unlikely that both would be remiss and, hence, it is more likely that the consumer would receive the information. But Congress evidently thought that in the single creditor situation the sanctions it provided were adequate to assure compliance. We see no reason why the same reasoning does not apply in a transaction in which one of two creditors has been singled out as the one required to meet the statutory mandate. Nor can we believe that the Act's purpose . . . is better served by giving [the consumer] two sheets of paper, rather than one, when both contain exactly the same data.[26]

Manning and the conduit theory coexist to the point of determining status as creditors. But as to the distinct question of liability, the *Manning* analysis provides adequate consumer protection plus a more legally justifiable result.

DOUGLAS W. SMITH



Attorney General Griffin B. Bell

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