Retail Credit: The Price Differential and Revolving Credit Carrying Charges

Michael S. Nolan
Retail Credit: The Time Price Differential and Revolving Credit Carrying Charges—Installment sales transactions have become a most significant element in today's retail merchandising operation. Quite naturally, recent legal developments in this area have attracted the attention as well as occasioned the concern of the retail business community. In particular, considerable interest has been generated by the recent series of decisions of the Nebraska Supreme Court touching upon the time price differential concept.1

The time price differential is simply the amount by which the time price of a particular item, the price at which a vendor will consent to sell it on credit, exceeds the price at which he would be willing to sell the identical item in return for immediate cash payment. The traditional view originating in the English case Beete v. Bidgood2 and adopted by the United States Supreme Court in Hogg v. Ruffner3 is that a seller enjoys complete freedom to set one price for a cash sale and a second and higher price in the case of a sale involving deferred payments.

The difference between the two prices constitutes compensation to the seller for the increased risk and expense involved in the credit transaction. It does not constitute interest, and consequently is not subject to the impact of the usury laws. “To constitute usury, there must be a loan and a taking of usurious interest, or the taking of more than legal interest for the forbearance of a debt or sum of money due.”4 A genuine conditional sale upon a deferred payment basis involves neither a loan nor the forbearance of a debt.5

Through the years this same attitude has been reflected in a multitude of state court decisions. Among the most recent opinions expressing the traditional viewpoint is that of the Minnesota Supreme Court in Van Asperen v. Darling Olds, Inc. which held that “a bona fide installment sale does not come within the purview of the usury statute.”6 The Supreme Court of Missouri held in Wyatt v. Commercial Credit Corporation that finance charges added to the cash price of a refrigerator purchased on an installment plan do not constitute interest.7 Within the past year two other courts8 have considered the installment sale, and have similarly decided that the transaction does not involve a loan or the forbearance of a debt and that the carrying charge, finance charge, or time price differential does not constitute interest.

---

4 Id. at 118.
7 Wyatt v. Commercial Credit Corporation, 341 S.W. 2d 348 (Mo. 1960).
The Nebraska Supreme Court in *Lloyd v. Gutgsell*\(^9\) dealt with an apparently similar installment sales agreement but came to an altogether contrary determination. The trial court had entered judgment in favor of the purchaser of a house trailer who had brought suit to cancel a conditional sales contract and a promissory note, to recover payments made, and to secure a certificate of title to the trailer without encumbrance. The majority of the court, with two justices concurring, affirmed the decision of the trial court, finding the transaction to be usurious. The cash price of the trailer was $5,000.00 which was reduced by a cash down payment and a trade-in allowance, leaving an unpaid balance of cash price in the amount of $3750.00. The conditional sales agreement specified a time price differential of $1229.00 and insurance charges of $340.00. The time price of the trailer under the contract was $6,569.00.\(^{10}\)

The majority opinion, in holding the challenged contract to be usurious, did not technically reject the traditional view that a true installment sale does not involve the charging of interest. The court did in fact carry out a previous determination “to look through the form and examine the substance” of any agreement in order to determine “whether such a transaction is a time sale made in good faith or a loan.”\(^{11}\)

The deciding factor in the supreme court’s determination that the transaction was in essence a loan was the undisputed testimony of the purchasers concerning their conversation with the salesman. The testimony indicated that a time price was never discussed with or even mentioned to the purchaser prior to the signing of the contract. The purchaser was given no choice between a cash and a credit price. Another factor considered by the court was that the contract form had itself been prepared by the finance company and contained a printed assignment to the company.\(^{12}\) The court concluded that the transaction was “merely a sale for a cash price, with the difference between the money the buyer has and what he needs being financed.”\(^{13}\) The court felt that “the expectation was that the defendant would finance the transaction and advance the balance of the cash price to the seller.”\(^{14}\) The time price differential was considered merely the charge for this advance and hence was interest. Since the amount of the differential exceeded nine per cent, simple interest, the transaction was held to be an usurious one.

The majority opinions seems to indicate that a bona fide time sale would still escape the impact of the usury law. Justices Boslaugh and Brower in their separate concurring opinions, however, disclose the

---

10 Id., 124 N.W. 2d at 201.
12 Lloyd v. Gutgsell, *supra* note 9, 124 N.W. 2d at 203.
13 Id., 124 N.W. 2d at 204.
14 Id., 124 N.W. 2d at 203.
belief that the court's decision marks an absolute departure from the established view on the nature of the time price differential. Both justices were particularly disturbed by the fact that the decision was not made prospective in effect to safeguard the validity of numerous financial transactions which had been consummated in reliance upon the past decisions of the court.\textsuperscript{15}

Justice Boslaugh believes that "the effect of the language of the majority opinion is to destroy the validity of all time sales contracts which were made in good faith upon previous decisions of this court."\textsuperscript{16} Justice Brower interprets the present decision as creating "a new rule of law in conflict with our previous holdings."\textsuperscript{17} He evidently feels that the effect of the decision is to equate completely a time price differential with an interest charge. In addition, he clearly believes that the traditional distinction is an artificial one which disregards the facts of modern economic life. Justice Brower adopts a view similar to that advocated by some commentators that the position of an installment purchaser under a contract, whether or not assigned to a finance company, is not significantly different from that of the borrower who secures a loan from a finance company to purchase the identical item. Under current conditions the buyer has no greater freedom than the borrower. The effect of competition controls the installment seller to no greater extent than the lender who is in addition subject to the usury laws. It is in short the belief of Justice Brower that today the time price differential is "interest received for forbearance of the dealer to collect the cash price and that the same law of usury should be applied to the time differential as to interest on a loan."\textsuperscript{18}

If the Nebraska Supreme Court is not formulating a complete rejection of the established time price differential concept, but is merely looking through the form of the transaction to discover its real nature, the decision in Lloyd v. Gutgsell is not altogether novel nor unique. The judicial history of the installment sale and of the usurious bargain is replete with similar admonitions.\textsuperscript{19} During the past two decades, many courts have shown an inclination to disregard the form of the transaction and strike down as usurious contracts which purported to be ordinary installment sales agreements. The Minnesota Supreme Court led the way in Seebold v. Eusterman, acknowledging the traditional installment sales theory but holding the challenged contract a mere subterfuge to conceal a loan.\textsuperscript{20} The Michigan Supreme Court in Hillman's v. Em 'N Al's held an installment agreement for the sale of restaurant equipment usurious, but adhered to the view that "unless the sale and

\textsuperscript{15} Id., 124 N.W. 2d at 204-206.
\textsuperscript{16} Id., 124 N.W. 2d at 205.
\textsuperscript{17} Id., 124 N.W. 2d at 206.
\textsuperscript{18} Ibid.
\textsuperscript{19} Randall v. Home Loan & Investment Co., 244 Wis. 623, 12 N.W. 2d 915 (1944).
\textsuperscript{20} Seebold v. Eusterman, 216 Minn. 566, 13 N.W. 2d 739 (1944).
purchase of property is a mere pretense the seller may charge a greater price for goods bought on credit than for cash without rendering the transaction usurious.”

In the recent case of Elder v. Doerr, the Nebraska Supreme Court itself professed to adhere to the traditional view of the installment sale. The court also held, however, that a “transaction is not a valid time sale made in good faith unless the seller informs the buyer, at the time of the sale, of the cash and time prices and gives the buyer the opportunity to choose the one he will accept.”

Other courts have struck down conditional sales agreements for the same reasons which disturbed the Nebraska Supreme Court. In G.F.C. Corporation v. Williams, the court emphasized the absence of any price other than the cash sales price on the basis of which a finance charge was computed. In Bradford v. Mack, the same court again failed to find a genuine time sale because only a cash price had been quoted to the purchaser. In Daniel v. First National Bank of Birmingham and in Hare v. General Contract Purchase Corporation, the courts pointed to the excessive involvement of the bank and finance company in the transaction as an indication that the questionable transaction was in essence a loan. Only the Arkansas Supreme Court in Sloan v. Sears Roebuck & Co. has adopted the position apparently taken by the concurring opinions in Lloyd v. Gutgsell, that all time price differentials are interest charges and will be held usurious if in excess of the legal interest rates.

The Supreme Court of Wisconsin has not as yet been called upon to consider the applicability of the usury laws to installment sales agreements. In 1935, however, the time price differentials did receive a measure of statutory recognition under the Motor Vehicle Installment Sales Act which provided for licensing by the State Banking Department and prohibited “unconscionable” charges. In 1953 the Act was amended to establish maximum rates of charges for each of several categories of motor vehicles. At the same time the Banking Department was given power to make rules and regulations and to examine the records of licensees.

In 1959, a bill prepared by the Wisconsin Retail Merchants Association was introduced into the state senate. One purpose of this bill was to extend statutory recognition of the time price differential to include retail sales of items other than automobiles. The bill provided

---

26 Hare v. General Contract Purchase Corp., 220 Ark. 601, 249 S.W. 2d 973 (1952).
29 Wis. Laws 1953, ch. 302, §§1-4.
30 Bill No. 256, S., Wis. Legis. (1959).
for full disclosure of terms to the buyer and a differential not to exceed $12 per $100 of principal balance per year. An amended version of this bill\(^{31}\) was passed by the legislature but was vetoed by the governor on October 28, 1959. Among the reasons specified in the veto message, the governor emphasized the absence of provisions for licensing and supervision of installment sales corresponding to those already governing small loans and automobile financing.

By means of this same bill an attempt was made to solve another retail credit problem, the validity of the revolving credit or budget charge account. The revolving account functions like the standard charge account, but payments may be spread out over a period of several months. The plans have several variations including fixed monthly payments and limitations on credit. The store applies a carrying or service charge to the unpaid balance at the end of the month. The usual charge among Wisconsin department stores is 1\(\frac{1}{2}\) percent per month which amounts to an annual rate of 18 per cent. Retail merchants have attempted to cloak these charges in time price terminology, but it is difficult to conceive of them as anything but interest for the forbearance of existing debts. The charge is computed as a percentage of the unpaid balance, and no attempt is made to set individual time prices for each item. It would seem that a revolving credit charge exceeding 10 percent per annum is in violation of the small loan law\(^{32}\) and that the debt is uncollectable. The bill vetoed by the governor because of the failure to provide for licensing and supervision would have legalized revolving credit charges of up to 1\(\frac{1}{2}\) percent per month.

Another attempt to solve these credit problems was made in the state assembly in 1959 by means of two separate bills which attacked the problems on an individual basis.\(^{33}\) Both bills were indefinitely postponed. Versions of these bills are currently being held in the assembly committee on Insurance and Banking for disposal in the April session, 1964. One bill would authorize monthly revolving credit charges not to exceed 1\(\frac{1}{2}\) percent on balances up to $300. A monthly charge of 1 percent would be allowed on that part of the balance in excess of $300.\(^{34}\) The companion bill extends the statutory time price differential to apply to the sales of goods other than automobiles, the allowed rate varying with the size of the principal balance.\(^{35}\) In addition both bills provide for licensing and supervision.\(^{36}\)

The possible effect of the much publicized decision of the Nebraska Supreme Court in *Lloyd v. Gutgsell* upon Wisconsin judicial thought

---

\(^{31}\) Substitute Amendment No. 1, S., to Bill No. 256, S., Wis. Legis. (1959).
\(^{34}\) Bill No. 796, A., Wis. Legis. (1959).
\(^{36}\) Bill No. 171, S., Wis. Legis. (1963), which has been killed in the state senate, dealt with both revolving credit charges and the time price differential.
is a matter of speculation, but it is clear that this decision has served to re-emphasize the need for statutory clarification and stabilization of the retail credit picture. In light of the recent decisions of the Nebraska Supreme Court, it is obvious that such legislative action cannot fail to benefit the retail seller as well as the installment purchaser.

MICHAEL S. NOLAN

Legal Ethics: Attorney Disciplined for Unprofessional Conduct
—Defendant-attorney was found guilty of unprofessional conduct in an action instigated upon complaint of the Board of State Bar Commissioners. This finding was based upon two grounds. The first related to the maintenance of a neon “Income Tax” sign in the defendant’s window, and the second concerned the allowance in his office of an income tax service conducted by his wife, a nonprofessional. Noting that this was a “test” case involving somewhat common practices, the court merely reprimanded the defendant and ordered him to pay costs not to exceed $200.¹

In its opinion the court pointed out that the placement of the “Income Tax” sign called attention to the defendant’s law office as the place where such service could be obtained. This, it felt, was a form of advertising, which amounted to solicitation of business, thus being unprofessional conduct. The court rejected defendant’s argument that because nonprofessionals are permitted to engage in such service, his performance, within narrow, nonlegal limits, was engagement in a business in which he was free to advertise. The court concluded that the public interest would not be best served by allowing advertisement on the part of attorneys who render tax services.

The court looked at the problem of office sharing as a permissive practice, but only in certain instances. In the Willenson case the court held that the arrangement amounted to unprofessional conduct. There must be evidence of a physical separation which indicates the independence of the parties such that patrons of the other enterprise will be apprised of the lack of supervisory control by the attorney.

The refusal of the defendant-attorney to remove the sign upon request subjected him to possible disbarment or a substantial period of suspension. However, it is questionable whether the court would have imposed such stringent sanctions even absent the nature of the case as a “test” case.

An attorney may be disciplined for actions that contravene the ethics of his profession even though his conduct is neither criminal nor calculated to obstruct justice.... It has also been said that unprofessional conduct that will justify disbarment

¹ State v. Willenson, 20 Wis. 2d 519, 123 N.W. 2d 452 (1963).