insurance, not being able to get adequate coverage against loss or accident, not getting claims settled fairly and not getting insurance claims paid promptly. The most important and surprising finding in this section is that relatively few people attach a major share of the blame for higher insurance costs to insurers or suggest that the increase has been caused by the desire of the insurance companies to increase their profits. The most frequently mentioned reason is inflation and cost of living. The public on questions of product liability, is significantly less demanding than consumer activists on what the number and size of awards made in courts in recent years would suggest. Essentially, they believe that accidents resulting from the negligence of the victim rather than from the negligence of the manufacturer, should not result in claims against the manufacturer.

Consumerism is, indeed, at the crossroads. The movement will certainly continue, even grow, in strength and influence. All of us business, education, government have a unique opportunity to help direct that growth, and consequently discover as we have at Sentry, that good consumerism can be good business. The question for today is: Will we be wise and agressive enough to grasp the opportunity confronting us and help steer the consumer movement down the roadway most advantageous to both ourselves and the customers we serve?

THE USDA ROLE IN CONSUMER PROTECTION

Ms. Carol Tucker Foreman

Serious consideration should be given to a comprehensive food policy at the national level. The policy should include:

1. determination of nutritional needs,
2. the U.S. role in feeding the world,
3. stimulation of adequate production,
4. reasonable food costs,
5. safe and high quality food,
6. domestic food assistance.

Concern about prices and profits is reasonable, however, we cannot ignore our basic responsibility to safeguard the nutrition and health of our citizens.

Through most of history, the human struggle for food has been directed primarily at simply getting enough to eat. This has led to government food policies that have focused mainly on increased production, better means of food preservation, and improved systems for the transportation and distribution of food. Now we have achieved a high degree of success in satisfying our domestic needs for adequate production, preservation, and distribution. Yet out of our very successes, new and troubling issues arise. Today, production in this country is so large and reliable that we are able to feed ourselves and a large portion of the rest of the world and use food sales to help balance trade deficits. Yet this has also meant that we have recurring surpluses and that producers have trouble surviving. Moreover, although millions of americans are unable to get enough to eat without assistance, for millions of others nutritional problems are a result of consuming too much food. We have been so successful in using chemicals to increase production, retard spoilage and preserve foods that we must now be concerned with the health effects of chemicals themselves. We have become so dependent upon food processing and upon nationwide food distribution systems that the farm value of production bears little relationship to final costs of food. And finally, because domestic population growth is leveling off and urbanization has slowed down, the rate of increase in domestic demand for food--which has been growing dramatically for years--may be slowing down.

We need to begin giving the most serious consideration to forging a new food policy--a policy that responds to the dilemmas facing us today in a changed world. The goal of this new policy should be to make available an adequate supply of safe, nutritious food at stable, reasonable prices--while providing a fair return on investment to farmers, processors and retailers, and decent wages to workers in the industry. The new policy should also be designed to provide for assistance to those at home and abroad who cannot afford the cost of a nutritious diet.

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A new food policy would involve change--including change in some of our existing programs and policies. It is important that if such changes are made, the resulting burdens should be spread across the population to the greatest extent possible. It is unreasonable to assume that farmers or processors or any other segment of the population should have to carry all the burden of change. At a minimum, change may require some adjustment assistance to those who will have to modify their traditional way of doing business. Further, consumer prices may increase as the costs of changes in processing and retailing are passed on. But, in the long run, the costs of a new system should be more than compensated for by increased efficiency and competition, reduced costs for advertising and some processing, more stable prices, a halt to the precipitous decline of modest-sized farms and perhaps most important, reduced health care costs as nutrition improves at home and abroad. The new policy should have six elements.

I. Determination of Nutritional Needs

A food policy should be based on a detailed assessment of what the nutritional needs of the people are. To even begin to develop a food policy, we must first know what persons in various age, sex, racial and ethnic groups, lifestyles and geographic locations need nutritionally for optimal growth and performance and continued well being. Determining these needs will require a commitment to increased human nutrition research. A small program of nutrition research has been carried out in the United States since the 1870's. But we still do not have adequate answers to some of the most basic questions. For example, the recommended daily allowances of various nutrients are widely used, but are often of limited value in helping a person select a proper diet suited to particular stages of life and level of physical or mental activity. For some nutrients (such as some trace minerals) so little reliable data exists that no RDA at all has been established although the nutrients may be essential to good health.

We also need research on the relation of diet to disease. It now appears that six out of the ten leading causes of death in the United States may be degenerative diseases whose onset may to some degree be related to nutritional factors. Some recent studies have linked various nutritional factors to cancer. At the same time, we need to learn more about the nutritional consequences of our increasing reliance on convenience foods, processed foods, and eating away from home.

To forge an effective food policy, we will need not only to increase our knowledge of nutritional requirements--but also to determine what levels and types of production are necessary to meet these needs. This will require an ability to translate nutritional needs into production terms. We should know, for example, how much wheat and what kinds of wheat should be produced to insure people with adequate levels of B vitamins. It is also important that we know what naturally-occurring vitamins change when wheat is milled. We will need to know if the vitamins can be replaced by fortification. These and similar assessments will have to deal with the combinations required to provide the necessary nutrients in diets as consumed, not just as generated in the laboratory.

II. The U.S. Role in Feeding the World

The second element of a national food policy is the role the U.S. chooses to play in meeting international food and nutrition needs. The federal government must determine what portion of this will be done through trade, what portion through assistance, and how much additional production is necessary to meet those needs.

The 1977 Farm Act calls for a domestic grain reserve system. It also encourages the Secretary of Agriculture to "enter negotiations with other nations to develop an international system of food reserves" for humanitarian relief. Participation in an international emergency food reserve is crucial if the U.S. is to live up to its international obligations. It can also demonstrate that participation in such a system will not ruin domestic farm prices or destroy foreign food markets.

But the complexity of international food issues demands more than a reserve system. Through Public Law 480, amended slightly by the 1977 Act, the federal government has for 23 years used U.S. farm production as both a means of developing foreign markets for U.S. goods and as a means of providing food aid. A national food policy must determine how to balance the need of hungry people abroad with the needs of American producers eager to find new markets. We cannot allow over-emphasis on one to undercut the importance of the other. Nor can we permit political consideration to determine where we provide decent assistance.

Maintaining good, stable trade relationships is extremely important. It is clear that a vigorous trade program is essential to keeping stability in our balance of payments. In addition, stable trade relationships protect American farmers--and consumers--from the fluctuations of a speculative market in food exports. We must strive to avoid the circumstances that have led in the past to pressures for embargoes on food exports. The embargoes of soybeans in 1974 and wheat in 1975 benefited no one. Trading partners and farmers were hurt. No discernible benefits accrued to consumers. Embargoes are basically an admission of policy failure and in an economy like ours, in which food is the keystone, we cannot afford such failures.

Although America's capacity for food production is unparalled in the world, we cannot permit the need to sell American food abroad to destroy the incentive for other less developed nations to become more self-reliant in food production. The U.S. cannot base its entire food economy on exports.

III. Stimulation of Adequate Production

The third element of a basic food policy is to stimulate and sustain production adequate to meet domestic and international nutrition needs, and our country's trade needs. In one sense, this does not represent a major departure from the policies we have

followed for a number of years. Government policies have long encouraged certain kinds of production and marketing and discouraged others through support prices, research and regulation. Government production policies have never benefited all producers equally. Livestock growers, for example, are not covered by support programs. Fruit and vegetable producers are only sporadically covered by federal and state marketing orders. Federal government actions have always helped some areas of agriculture at the expense of others. Support programs leading to higher feed grain prices, for example, hurt livestock producers.

What a new food policy must do is to reassess <u>which</u> areas of agriculture are supported and promoted. In the future, the basis of such decisions must be to meet nutrition reorientation of production patterns. Naturally, a new food policy that reorients production patterns and support systems will initially be regarded as threatening by some persons. But the new policy does not have to be a threat. Changes can be carefully designed to avoid inequities, to make sure that one region of the country or some group of producers are not victimized by new policy goals, and to remedy inequities. Indeed, any new policy must be constructed so that over the long run, it will cause less dislocation and be less inequitable than the policies of the past. In previous years federal policies, and the results of federally funded research, have caused economic dislocation of farmers (especially small farmers), of farmworkers, and of some processors and retailers--and usually without any compensation.

There are a number of factors that would limit reorientation of production patterns. Among these are geographical factors and farmers' knowledge of new and different crops.

One example of the type of action of shaping production policy to meet nutrition and trade needs is the creation of a domestic wheat and feed grain reserve. The new reserve system established by the 1977 Food and Agriculture Act is aimed at protecting farmers against low prices in years of surplus, and at providing an emergency food supply to meet domestic nutrition needs. The creation of the grain reserve provides a floor for farm production and is a basic step toward stable prices for one of our most essential crops. It also will provide the opportunity for government to prove it can administer a production program equitably.

One fundamental issue of production policy that was not addressed by the 1977 Act is the problem of skyrocketing land costs. Record grain prices in 1972 kicked off a boom in land prices that has not relented, despite the dropping grain prices farmers now face. Nationally, agricultural land prices have doubled, on the average, since 1971. In the midwest, prices have tripled. In the mid-atlantic area urban development pressures have pushed up land prices. In the midwest, speculation based on high farm prices has pushed up costs. It is estimated that a new farmer needs $500,000 to buy a farm and enter production. Few individuals have access to the

credit necessary to borrow $0.5 million. This encourages purchase of land by banks, foreign investors and corporations, and it encourages renting rather than farmer ownership of land.

Moreover, if land costs continue to inflate as they have, the nation can expect ever-higher consumer food prices--which would in turn, if past trends remain true, further inflate land costs. In addition, continuously inflating land costs will effectively doom the family farm and seriously deplete competition among food producers. Such a result is clearly out of line with fostering stable prices.

The federal government should begin an intensive investigation of the reasons for rising land costs and begin to develop policy recommendations to slow the trend. At the same time the Department of Agriculture must continue to develop more satisfactory formulas for dealing with land costs in support programs.

Finally, a new production policy will have to assure the farmer of adequate supplies of the elements of production. The energy crisis of 1973, and its resulting fuel/fertilizer price spiral, proved how vulnerable our food system, and individual farmers, are to energy shortages. Consideration should be given to the possibility of mandatory allocation of petro-chemicals for farm use. A new production policy might also include energy and soil conservation incentives and incentives for new kinds of energy-saving pest control and fertilization techniques.

IV. Reasonable Food Costs

A fourth element of a new food policy must be to assure the availability of food at reasonable prices. In past years, full production has sometimes been touted as the answer to reasonable prices. But full production on the farm will not, by itself, guarantee moderate retail price levels. One of the most important elements in determining food prices is what happens to food after it leaves the farm. Marketing costs have risen so sharply during the past few years that they now comprise 60% of the total food bill. Indeed, the economic research service observes that the food price inflation of the 1970's has, to a large extent, been attributable to marketing cost increases. Between 1974 and 1976, marketing costs increased about 10% annually. According to the ERS, "increased marketing costs will again account for most of the rise in consumer food expenditures in 1977."

It is true that some of the marketing cost increase is attributable to higher energy costs and the general inflationary trend. But if we are to have both reasonable levels of farm income and reasonable prices for consumers, we simply must develop mechanisms to discourage unnecessary costs from being built into the food system between the time food leaves the farmer and the time it reaches the consumer. This means that the government must cease

any encouragement of industry practices, and halt the issuances of any government regulations, that add to costs unnecessarily. Government transportation regulations are an obvious area where review and revision could lead to reduced costs. The "back haul" regulations are a case in point.

Other areas that may also lead to unnecessary and inflated costs are inadequate competition, excessive advertising, and excessive packaging.

Inadequate competition is a particularly troublesome area. Recent studies have indicated that economic concentration in food manufacturing and retailing is increasing. According to Russell Parker, former Assistant Director of Economics at the Federal Trade Commission, twenty large grocery chains accounted for 37% of total grocery store sales in the United States in 1975. This represents an increase of more than one-third from the 27% controlled by the twenty largest chains in 1948. In a study for the congressional Joint Economic Committee (JEC) earlier this year, University of Wisconsin researchers found that the four largest grocery retailers in 194 metropolitan areas held an average of 54% of grocery sales. In one fourth of those areas, they held 60% or more of sales. Parker believes this leads to higher prices for many consumers. He asserts that FTC data show that "grocery chains use higher markups or gross margins in high market share areas and have lower markups where they have lower market shares."

The study prepared for the JEC reached similar conclusions. It found "strong evidence that monopoly overcharges, i.e., prices above those in competitive markets, are likely in markets that are dominated by one or two firms and/or where sales are highly concentrated among the largest four firms." The study estimated that total consumer overcharge due to economic concentration in 1974 was $662 million. The researchers concluded that overcharges vary from city to city, depending on the extent of concentration. They found that, in 1974, consumers in one city with four firm competition suffered a $1.6 million overcharge, while in another city with only two firms controlling most of the market consumers experienced an $83 million overcharge.

Concentration is also increasing among food processors. The number of food manufacturers has declined substantially over the past thirty years. In 1947, there were 44,000 food manufacturers. In 1972, there were only 22,171. This may seem like a large number when compared to domestic automobile or steel manufacturers, but several major food lines are highly concentrated. Four firms control 84% of the breakfast cereal market and 95% of canned baby foods. Two firms have 58% of the soft drink market. There are no meaningful national figures on concentration in the bread baking industry, but on a regional basis, the 4 top firms in 18 different cities accounted for about 60% of consumer bread purchases.

Inadequate competition may explain why soft drink prices, pre-sweetened cereal prices and bread prices rose as sugar and wheat prices went up a few years ago, but have not followed the downward spirals of those raw materials.

Many individual areas of food processing do remain competitive and fairly reflective of changes in the prices of basic comodities, but this is an area where public policy has skirted serious problems. The latest data available on food marketing in many cases is from the 1966 studies of the National Commission on Food Marketing. Ten year old studies are of a limited value in making food policy, and a first step in this area should be creation of another commission or a specific mandate from congress to update the Food Marketing studies. Once the data is available, government should act to assure adequate competition in the food industry.

When competition on the basis of price declines, competition based on "product differentiation" and making heavy use of advertising, often increases. Competition among airlines is a classic case in point. Airlines now spend enormous sums to tell us that their planes fly in "friendly skies" or feature attractive hostesses who will "fly us" to our destination. This same pattern is frequently seen in parts of the food industry. The decline of price competition is replaced by an upsurge in "product differentiation" competition. In the food area, advertising and packaging are key elements of this growing type of competition. While both advertising and packaging have valid market place roles, expenditures for both have grown beyond reason in some product lines. Both together have become a significant portion of the increasing food marketing bill and need reexamination by manufacturers and policymakers. Advertising now accounts for about three percent of the food marketing bill. Some of it is price specific but most of it is directed at product differentiation.

Of major concern is the increasingly heavy role of advertising in promoting non-nutritive food items. Government is becoming more concerned with the health implications of food advertising. The FTC has moved to regulate nutritional claims and may act to strictly limit food advertising aimed at children. The FDA commissioner has made clear his view that advertising is an extension of labeling and should be regulated accordingly.

There may be other ways government should encourage food value as measured by price and nutrition. Companies that advertise food on television might be required to give equal time to nutrition messages. Government could make comparative nutritional price information available to consumers in places where people buy food and/or in the electronic or print media. Government encouragement of advertising through tax deductibility has been attacked by some consumer organizations, and this area is one for examination in public policy formation. Any limits on tax deductibility

would, however, have to deal with the problem of special provision for advertising by new competitors entering concentrated markets, and for competitors with a small share of concentrated market.

Packaging is another important area. Packaging costs now account for 13% of the food marketing bill. Between 1958 and 1974, the consumer product cost represented by packaging doubled for items like dairy products, produce, beverages and candy. The economic research service says that packaging costs are likely to increase 7% a year through 1980. The increase will come both from growing costs of materials and from increased use. We don't know how much of these costs are accounted for by unnecessary packaging, nor do we know how much packaging is used solely for product identification purposes or how much packaging is needed for protection in shipping and sales. It is unlikely that government can make reasonable decisions about packaging without that knowledge.

It should also be noted that packaging now accounts for 30-40% of total municipal solid waste--and expenditures for solid waste disposal amount to about $4 billion a year. Reasonable public policy should assess whether that is an acceptable cost.

A few final points on food prices and what to do about them should be noted. There are two courses of action that we must resist as possible cost-cutting measures. One is to cut food costs by cutting farmer income ever further. The other is to permit the use of questionable substances in foods or to relax health and safety regulations. There are few if any acceptable tradeoffs of safety for savings. A cheap food supply purchased at the expense of health protection is no bargain.

V. Safe and High Quality Food

It should come as no surprise that the assurance of a safe and high quality food supply is the fifth element of the food policy changes. Although food safety is virtually unchallenged as an appropriate goal, the means to achieving food safety have been in dispute for over eighty years. The federal effort to assure food safety dates back to 1906, when the original Pure Food and Drug act was passed--in large part because of a grave public concern over the use of chemicals in prepared food. the acceptability of chemicals in food continues to be a hotly debated issue today. There are a number of laws on the books--such as the Food and Drug Act, the Meat Inspection Act, and the Poultry Products Inspection Act--that are firm in their rejection of safe chemicals. A food policy that has as its first concern the nutritional well-being of the public can ill afford to be less strict than present law. Such a food policy must also include vigilant enforcement of these laws.

This may not be enough, however. Government action to promote food safety may need to enter new areas. Present laws deal with food additives and manufacturing processes. Yet evidence now

suggests links between high consumption levels of substances such as salt and fat, and such diseases as high blood pressure and a variety of cancers. A food policy concerned with food safety should be able to deal with these problems as well. Perhaps we should become as concerned about the fat in a hot dog as we are about the nitrite. In any event, whenever government takes action on a food safety issue to protect the health of its citizens whether the action involved as unsafe chemical or a substance such as fat, there is a potential for adverse economic impact on some companies and individuals. For example, pending government decisions that could lead to bans on the use of tetracycline in animal feed or the use of sodium nitrite in meat processing may have significant impacts on meat producers and processors.

When government acts to exclude previously approved products, public policy on food safety should include ways to ease the transition. This would require, at a minimum, collection of adequate data on what the real costs to the industry will be. Present data are almost always the industry's "worst case" assessment of the impact. Policy may also have to include mechanisms for easing the financial burden of smaller firms.

Some will argue that consumer sovereignty in the market place should permit consumers to purchase anything, no matter what its health effects. But in other areas, the federal government does not fall back on that argument as a way out of its responsibilities. The federal government regulates dangerous or toxic chemicals. We attempt to control water and air pollution. Government funds the construction of municipal santitation system. Federal programs help protect people from disease via vaccination and innoculation campaigns. Government should play no less responsible role in the food system.

Government policy must also deal with the emerging issue of food quality. Public policy should address more adequately such questions as the construction and composition of processed foods. Industry is engaged in a constant effort to bring new technology to food processing. The results are sometimes ice cream that is not like what mother used to make, or tissue from ground bone in hot dogs. It is unlikely that public policy should exclude the results of new technology from the marketplace, but it must find better ways to assure consumers that the quality of new foods--their nutritional value, taste and appearance--are as good or better than the previous product. We must also find better ways to differentiate between products associated with certain basic materials or processing methods and those made in laboratories or with new ingredients or methods so that customers will understand what they are purchasing.

VI. Domestic Food Assistance

Finally, Food policy must also deal with those people who do not have the ability to afford an adequate diet. Present government policy supports food for such individuals through a variety of programs that approach the problem in various ways. The Food Stamp Program increases food consumption by increasing income and limiting the increase to food purchases. The school breakfast, school lunch and other child nutrition programs provide meals in an institutional setting. The Women, Infants, Children Food Program (WIC) provides prescription food packages to vulnerable persons at nutritional risk during the most critical phase of human growth and development.

The President has proposed to eliminate the Food Stamp Program in favor of a general cash assistance program. His proposal assumes there will be no appreciable loss of nutrition as a result. Available studies seem to support that assumption. They show that low-income families tend to allocate their money wisely and to get more nutrients per food dollar than the middle income.

In the institutional feed programs--such as school lunch--the issue of food quality is becoming a growing concern. In the past few years, some items of questionable nutritional value--such as fortified grain-fruit products and formulated milk products, were allowed into some of these programs. We have moved to prevent their further use. Plate waste and meals that fail to meet portion and nutrition requirements are additional problems of the institutional feeding programs. These programs must be upgraded by placing greater emphasis on serving healthy, appetizing diets in attractive settings. These programs should be learning laboratories for good nutrition--teaching by example that food can be both nutritious and appetizing.

The Women, Infant, Children Feeding Program has perhaps the greatest capacity to use good nutrition to improve health and assist in breaking the cycle of poor childhood development that is often associated with poor nutrition. It provides high quality protein, iron, calcium and vitamins A and C to pregnant women, nursing mothers and young children. Because WIC operates through health care programs, it integrates health care, nutrition education and food assistance. It has been shown to result in substantially increased visits to prenatal and neonatal health clinics, as well as in the increased consumption of nutritious foods during a critical growth stage.

Conclusion

The food policy described above, and the questions it raises, may make some people uncomfortable. Consumers worry that changes in the food economy will hurt them by creating higher prices. Farmers are already angry because more of the returns from retail food sales does not flow to them. They fear that government intervention

in production in the name of health or nutrition will put them in an even more precarious economic situation. Processors and retailers already complain that their profit margins are too low and that more government regulation will cause their financial ruin.

The concern about prices and profits is reasonable. But we cannot ignore our basic responsibilities to safeguard the nutrition and health of our citizens. The challenge before us, therefore, is to shape a new food policy that provides healthful food, and does this at reasonable prices with a reasonable return to those who get the food to our tables. This is a big job, but it is one of the most important tasks of public and private policy in our time.

CONSUMERS' EDUCATION

LOOKING AHEAD WITH THREE YEARS EXPERIENCE

Dustin W. Wilson*

The grant proposals to the Office of Consumers' Education have revealed national needs and challenges for consumer education in the future. A new challenge for consumer education is to develop appropriate methods and materials which will best assist consumers to influence public policy. An extensive re-evaluation of our consumer education curricula will assist in accomplishing this goal.

The information and insight gained from the 2,250 applications and requests for $160,000,000 in the three years of the Consumers' Education Program are most informative in what they indicate are national needs, more revealing in what they do not note but infer, and challenging in the implications for professional consumer educators.

Explicitly, the unmet consumer needs of special populations i.e. senior citizens, the poor, both urban and rural, those with limited English speaking ability, American Indians are extraordinary and were identified by a whole host of applicants. Furthermore, in addition to the personal and family management problems always with us, the new and varied issues consumers confront today i.e. energy, utility rate setting, health and legal service systems, regulatory agencies, international affairs and food prices and jobs, industrial oligopolies are complex and require a high level of consumer skills. Inferentially, and also from other data, the institutions ordinarily expected to prepare and educate consumers i.e. the family, schools, colleges and universities are woefully unprepared. In recognition of, and responding to, this last condition, over half of the applicants are from other private and public non-profit agencies.

While these data are not surprising, the implications for consumer educators are immense. First, training in coping skills for individuals and families simply are not an adequate justification for consumer education. Second, while a greater understanding of the economic system and how the marketplace works is helpful, it does not resolve either the short or long term problems consumers face.

The challenge to the profession of consumer education is to develop appropriate and effective means and materials which will enable consumers to influence the market forces, both public and private, not merely react to whatever products and services are

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delivered or are available. This requires an intensive reexamination of the desired operational outcomes of consumer education, the development of new curricula and techniques which will produce knowledgeable consumers, but far more important, an activated and effective consumer/citizen.

A DECADE OF TRUTH IN LENDING

Dr. Richard Morse*

The original Truth-in-Lending legislation was passed ten years ago. The legislation has allowed consumers to compare rates more efficiently and accurately. However, there continues to be major problems to be corrected before the Act accomplishes its original purpose. The author enumerates several deficiencies with Truth-in-Lending and offers several recommendations that will eliminate these concerns.

Introduction

Eighteen years ago Senator Paul H. Douglas opened hearings on the Consumer Credit Labeling Bill, and eight years later it was enacted as the Truth in Lending Act. "The purpose of the bill," Senator Douglas said in his opening remarks at the committee hearings, "is to require that the American consumer be given the truth, the whole truth, and nothing but the truth, about the interest rates and finance charges he is asked to pay when he borrows money or buys an article on the installment plan."

Senator Douglas cited four disguises of the finance charges which were then prevalent:

1. Prices are quoted as so much down, so much a month, without giving the number of months to pay or the true annual rate.

2. The price of credit is quoted as a monthly rate without giving the true annual rate which is twelve times the quoted monthly rate.

3. The price of credit is quoted as a percentage of the original amount, rather than the unpaid balance, and

4. The price is stated as an "add-on" or "discount." The simple rate or true rate is approximately double these quoted rates. (S. 2755, pg. 12).

These and other disguises were made illegal with passage of Truth in Lending in 1968.

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Senator Douglas's original bill required two disclosures: (a) the dollar amount, and (b) the true annual rate on the unpaid balances, expressed as a simple annual rate. It did not set rates or regulate credit practices. It was a consumer credit labeling bill requiring disclosure of both the rate (price) and the cost of credit used. The "unit price" of credit expressed as dollars per $100 per period is now called the Periodic Percentage Rate, and when annualized, the Annual Percentage Rate. The cost of credit is now called the Finance Charge and is the product of the unit price rate applied to the amount of credit used, which is the unpaid balance each period. Douglas argued that "the excessive use of credit results frequently from a lack of awareness of the cost thereof to the user to the detriment of both the user and the economy." (S. 2755, p.3).

Some Notable Achievements

If nothing else, Truth in Lending has proven that a simple interest rate can be quoted. The annual percentage rate, based on the unpaid and not the original balance must now be disclosed. This was the major innovation of Truth in Lending. What Senator Douglas termed "true" and "simple" rate is now available in standard, comparable terms so consumers can compare the price of credit. A recent survey made for the Federal Reserve Board confirms the general acceptance and recognition of the annual percentage rate. "As of the summer of 1977, the proportions of consumer credit users who were aware of the annual percentage rates charged had reached 54.5% for closed-end credit, 64.7% for retail revolving credit, and 71.0% for bank credit cards."[1]

The results of a study made in Kansas presents an even more striking picture of success. The study used a unique historical series of data collected over the period of 1959 through 1977. Pre-Truth in Lending quotation accuracy, with a + or - three percentage point tolerance, was 69% for credit unions, 57% for banks, 41% for finance companies, and 13% for car dealers. Post-Truth in Lending quotation accuracy, with 1/8th percentage point tolerance, was 96% for banks, 95% for finance companies, 90% for credit unions, and 87% for car dealers. (Thurlow, 1977, p.42) The Thurlow study, unlike the FRB study, tested not only awareness but accuracy of quotations.

Truth in Lending clarified that 1% per month is indeed 12% a year; or, phrased in more general language, that the periodic percentage rate multiplied by the number of periods in a year is exactly the annual percentage rate. (Ambiguity regarding the length of a year continues to present a problem).

A Successful, yet Disappointing Record

After ten years of Truth in Lending we have not fulfilled the standards of disclosure embodied in Senator Douglas's concepts of full and meaningful disclosure.

It is ironic that after these ten years a backlash has set in against Truth in Lending. The charge of over-regulation is often brought in some manner, as before persons ridiculed Senator Douglas's pleas for simplicity. For example, a recent article entitled "The Protection Consumers Don't Want" concludes with encouragement to Senator Proxmire who allegedly "has announced intention to strip down the law so that all a creditor is required to send out is a statement with the true credit charge on it--and nothing more."

Regulations written and administered by persons unable or unwilling to capture the true philosophy of Senator Douglas have further encumbered the act. Current textbooks written by scholars in the field reflect a reluctance to accept the actuarial rate as the true rate; old credit concepts, which should have been recognized as obsolete, continue to be taught. Even such sophisticated publications as Money magazine persist in misconstruing the annual percentage rate. But probably most pervasive is the recalcitrant posture of the credit industry in not accepting Truth in Lending, as manifested in their reluctance to discard the use of "add-on" and "discount" rates, and their insistence on legitimizing such consumer rip-offs as Rule of 78's and credit insurance. These forces have resulted in some major disappointments in accomplishing full and meaningful disclosure such as:

1. Unawareness: Over one-fourth of credit users are not even aware of the annual percentage rate.[2]

2. Invalid oral disclosures. At least half of the oral disclosures of the annual percentage rate from banks were in violation of Truth in Lending even as late as 1974.[3]

3. Lack of enforcement. Not until the 1978 annual report is there mention of concerted effort of the Federal enforcement agencies for compliance. FDIC noted an increase from 26% in 1976 to 36% in 1977 in errors discovered. The Comptroller estimated 88% of national banks examined were not in full compliance and the Federal Reserve Board's estimate was 72 % of the state banks.[4]

4. Lack of training. Not until 1977, and then only in response to the recommendation of the General Accounting Office, did the bank regulatory agencies initiate a joint training program of bank personnel. This involved their developing and perfecting examination techniques for testing for compliance.

5. Complex open-end contracts. Open-end credit contracts are often unnecessarily complex and beyond the comprehension of both the creditor and the consumer. This is not a new discovery. Max (1970) compared disclosures before and after Truth in Lending. After Truth in Lending, open-end credit contracts were still not understood by creditors, but the

disclosures were sufficiently clear that a conscientious consumer could understand most of them. Last year, Nelson (1977) scrutinized open-end credit accounts on which consumers had paid finance charges. She identified, from the disclosures on the credit statement, the method used to compute the balance subject to finance charges and verified whether the charges made were in conformity with the method as interpreted. The results reflect a shameful inadequacy in fulfilling the intent of Truth in Lending. Not one of the eleven BankAmericard accounts could be verified, and only one-fourth of the Master-Charge accounts checked out. Furthermore, only 36% of the J.C. Penney and Sears accounts could be verified.

In 1970, the FTC compliance officer informed the Federal Reserve Board that large creditors with legal staff services were usually in full and substantial compliance, while small creditors were not. Nelson reports that 93% of the small local retailers' billing statements met her test of "read-ability and repeatability" for they could be understood and verified. The largest retailers with their skilled legal talents could not meet this simple consumer test; presumably, they met the test of compliance with Truth in Lending enforcement agencies. The enforcement agencies have not been using consumer interest criteria in their enforcement procedures.

6. Dual rates in advertisements. Advertising of two different rates for financing one purchase is certainly not within the spirit of the Douglas TinL Act. Testimony of Thomas W. Taylor, Associate Deputy Comptroller of the Currency for Consumer Affairs, in hearings before the subcommittee on consumer affairs exhibits advertisements which quote "simple 8.00% interest rate" and in another portion of the same advertisement, "interest expressed as annual percentage rate is 8.25%." This duality is in several of the advertisements which are part of Mr. Taylor's testimony.[5] Use of dual rates is in compliance with Regulation Z 226.10 (d) (1) (i). The regulations do not define simple annual rate, but merely stipulate that the simple rate shall not be stated more conspiciously than the annual percentage rate. Is there any wonder that consumers might be confused?

7. Obsolete concepts persist. Persistent use of such terms as "unearned interest," "rule of 78ths," "constant ratio formula," "precomputed interest," which are creditor-used terms are confusing to the consumer since they are irrelevant to the actuarial (U.S. Rule) concept of Truth in Lending.

8. Student loan exemption. A different standard for disclosure is allowed for student loans than for other loans (Regulation Z Sec. 226.809). So students with two or more credit contracts may have contracts using different credit language.

9. Inconsistent APR's. The same regulation permits two different APR values; one figured by a quotient method and the other by a multiplier method. As a result, a billing statement may have two rates disclosed for the set of facts.

Statutory and Regulatory Handicaps

Some of the most serious deficiencies of Truth in Lending can be attributed to flaws in the Act as passed by the Congress. There had been precedent for a better form of disclosure in the Department of Defense Directive of 1966, but these were too advanced to be acceptable at that time. Truth in Lending was further handicapped by regulations and interpretations of the Federal Reserve Board. Also lacking was rigorous enforcement.

The following are deficiencies in the act that inhibit full disclosure:

1. Sales and loan credit distinction. The preservation of a distinction between sale and loan credit for closed-end credit (Sections 128 and 129) makes no consumer sense. By what logic should the disclosure of the APR and finance charge be different for two car buyers in need of $2000 for the purchase, one wanting to borrow cash and the other wanting credit from the dealer? Furthermore, why is a distinction made between sales and loan credit for closed-end, but not for open-end credit?

2. Credit Life Insurance. (Section 106(b)) Truth in Lending exempts premiums from being included in the finance charge for credit life, accident, or health insurance, if not required by the creditor.

   Both the creditor and the consumer have an interest in whether the credit contract is insured; insurance protection for the consumer is also protection for the creditor who is saved from "chasing the hearse or the ambulance" to collect debts from the injured or deceased.

   The simplifiers argue that the insurance cost of an insured credit contract be either absorbed by the creditor, as is the current practice of credit unions, or included as a cost of credit in the finance charge and the quoted APR. This would not prohibit a creditor from including credit life insurance; the creditor could market insured and non-insured credit at different prices, giving the consumer a choice at these two prices.

3. Determination of the annual percentage rate (Section 107). This section title reveals a completely backward relationship between the finance charge and the annual percentage rate. If the APR were given, then the problem becomes one of how to find the finance charge, and not the reverse. Senator Proxmire, in describing this section of S5, said in his

introductory remarks to the Truth in Lending Hearings: "Annual percentage is arrived at by multiplying the percentage rate per period times the number of periods in a year. The percentage rate per period, thus, becomes the basic building block from which the annual rate is determined."

"The use of a percentage per period to arrive at the annual percentage rate eliminates the need to describe the percentage rate of finance charges as a 'simple,' 'effective,' 'true,' 'compound,' or nominal rate. It also eliminates the need to refer to actual 'add-on,' 'discount,' and other rate expressions." (S5,p.6)

Proxmire underscored the difference in approaching credit by starting with the cost and then determining its price and by starting with the price per unit and then computing the cost. He said: "....instead of asking 'how do you figure the rate, given the finance charge and a set of payments,' both the lender and the borrower will ask, and easily determine' what are the amounts of finance charges and payments, given the rate.'" (S5,p.6)

Truth in Lending, as enacted, failed to carry out this distinction. There is unwarranted consideration of how to determine the APR and estimates of its correctness. The opponents had been so determined to prove the difficulty of computing the APR that they distorted evidence of how simply it could be stated.

The great concern over whether the APR could be computed accurately is reflected in the various sections of the Act. Although such concern was somewhat warranted in 1968, it certainly is not today with the advent of inexpensive pocket calculators with which persons with little mathematical skill can figure all of the factors to an accuracy level beyond that needed by the consumer.

4. Add-ons, Discounts, Pre-computed and Unearned Finance Charges, Rule of 78's. Despite Senator Proxmire's prediction that Truth in Lending would eliminate such rate expressions as add-ons and discounts, their use continues and is even acknowledged in the Interpretation of Reg. Z (226.818-9) which is concerned with "refund of unearned finance charges" and "prepaid finance charges with add-ons and discounts." These concepts and methods have been popular with creditors and crept into Truth in Lending by authorizing the Board "to prescribe methods which materially simplify the computation of the APR" (Section 107 (n)(1) (B) and 107 (3). As a result, the Board has yielded to creditor-oriented pressures and condoned the very disguises which Senator Douglas had cited.

5. Step, Multiple and Graduated Rate (or Rates) permitted. (Sections 127 and 143, and 226.506). Disclosures of multiple rates

confound even the experts. And the consumer wanting to comparison shop is in a hopeless situation. For example, the consumer is often confronted with open-end disclosures such as 18% on balances up to one amount and 12% on larger amounts. How can the consumer blend these two "step" or graduated rates into a homogenous APR? Also, many state laws on closed-end credit recognize graduated rates such as 36% on the first $300, 21% on the next $700 and 14.4% on that portion over $1,000.

The simplest rate disclosure, and the only one which should be permitted, is the single APR applicable to the amount or range of amounts financed. Thus creditors wishing to charge higher rates for small loans can bracket those amounts financed for which this rate is applicable; and similarly, lower rates for higher amounts financed. The creditor is in a much better position to merge the multiple rates into a single and meaningful APR than is the consumer.

6. Average daily balance and daily periodic rate (Section 226.506 and 226.703). There seems to be some confusion in terminology and conceptualization in accommodating daily rates which were almost non-existent in 1968. The regulations cause one to question how the finance charge can be computed on the average daily balance by applying a monthly periodic rate. It would be sensible to apply a monthly periodic rate to a monthly balance (average or otherwise). Or, it makes sense to apply a daily rate to a daily balance. But a monthly rate applied to a daily balance presents problems.

7. Exemption of the finance charge disclosed for dwelling units (Section 128 (a) (6) and Section 129 (a) (4)) and other exemptions. The real estate home finance industry, disturbed with the specter of disclosed finance charges for fear that they would discourage consumers from making valid judgments, prevailed upon Congress to make this exemption. The Federal Reserve Board and others now recognize their fear to be without foundation, and have recommended against special treatment for this type of credit. The finance charge should be disclosed for all credit.

   Furthermore, exclusion from the finance charge of certain other costs which are clearly incident to the extension of credit, such as the cost of credit reports, should be deleted as an exemption.

8. Time price differential disclosure Deferred Payment Price. (Section 128 (a) (6)). Creditors have escaped prosecution charging usurious rates by taking refuge under the time price doctrine under which the cost of a credit sale is construed not to be interest, but merely a differential between the two prices--the time sale and cash prices. This differentiation, which serves no useful purpose for consumers, has served the sales finance industry well, and it is understandable why they wish it preserved.

Actually, the time sale price and cash price are not the viable options for most consumers since credit sales usually involve a down payment or trade in. The viable options for the consumer, then, revolve around the amount to be financed and alternative sources of this amount of credit. The Deferred Payment Price is useful only to compare with the cash price to learn the cost of deferrment, an exercise no longer needed since Truth in Lending requires disclosure of the Finance Charge.

9. The illogical ordering of disclosures under Section 128 (a).

Although the Board has explicitly recognized that the order of disclosures, as printed in the statute and regulations, is not required of creditors, nevertheless the order in the statute and regulation does not reflect a proper line of thinking. The Department of Defense directive had a more logical ordering. It merged sales and loan credit into one document beginning with "the price of goods being procurred and/or the amount of cash borrowed." To this were added what were termed "ancillary charges," that is charges which might have been included in the cash price or loan but "were not incident to the obtaining of credit or benefitical to the seller or lender." These were summed to give "the total cash delivered price, or the total amount of credit extended," that is, the amount of the cash required to satisfy the sale or loan. On the next line there were the subtractable items of cash "down payment or trade-in allowance" to obtain the amount financed, the "unpaid cash balance to be financed." The next logical disclosure would be the unit price for credit, that is, the periodic percentage rate and its annualized equivalent APR.

Simplify and Reform the Truth in Lending Act

In summary, the following are reforms that should be considered: (1) Consolidate credit and loan closed-end disclosures. (2) Include credit life and A & H premiums in the finance charge, allowing creditors to extend credit without insurance. (3) Proscribe the use of such terms and concepts as add-ons, discounts, unearned finance charge, prepaid finance charge, Rule of 78's, and other terms and concepts made obsolete by Truth in Lending's use of the actuarial rate and the U.S. Rule. (4) Proscribe the quotation of more than one APR for an amount financed. (5) Delete all references to the determination, estimation, or approximation of the APR. Instead, focus these on the finance charge (which, in the unique case of open-end credit is unknown). (6) Close the exemptions for home dwellings and student loans, and review the charges excluded from the finance charge. (7) Eliminate the deferred payment price or the total sale price as a

required disclosure. (8) Require that receipts of payment show the current unpaid balance. (9) Reorder the required disclosures to reflect the logic of deriving the finance charge from the application of the periodic percentage rate to the periodic unpaid balances.

There are three bills before the Senate (S.1312, S.1501, S.1653) to simplify and facilitate compliance of Truth in Lending on which hearings were held last July. In general, these efforts and particularly the recommendations of the Federal Reserve Board to simplify the format of the disclosure statement are productive measures. However, the recommendations are lacking in imagination and practicality. We are ready to step back and take a hard look at whether the true purposes of Truth in Lending cannot be accomplished more simply with a more straightforward consumer orientation. Therefore, the following are recommendations that should be considered:

1. Readability and Repeatability should be incorporated as a standard by which regulations are reviewed and contracts evaluated for compliance with Truth in Lending. Unless the consumer can understand the language disclosed, it is useless.

2. Timing of Disclosures. Truth in Lending should incorporate in its purposes the language found in proposed legislation for Truth in Savings. "It is the purpose of this Act to require meaningful disclosure...so that the individual will be able to compare..., to validate performance under the contract and to have ready access to prevailing contract conditions" (Sec. 2, H.R. 14, 94th Congress). It recognizes that consumers need information (1) before entering into the contract, (2) in their contract, and (3) when account activity is reported so the consumer can verify the records.

3. Uniform and Pervasive. The principles of Truth in Lending should be made pervasive throughout the government as well as private consumer credit contracts.

4. Consumer Education. There should be built into the Truth in Lending Act a consumer education component to be financed out of proceeds of finance charges collected.

5. Consumer Involvement in Enforcement. In order to encourage consumers' involvement in the enforcement procedures, it is proposed that consumers be given a bounty for discovery and reporting of creditors who are out of compliance.

6. Authorize Compound Finance Charges. Congress should come to grips with the question of whether interest on credit can be compounded. U.S. Rule is vague on this point.

7. Meaning of the Word "Annual". It is time that Congress define for purposes of disclosure whether the word annual pertains to a year of 360, 365, 366 or other numbers of days.

8. Creditor Performance Records. It is recommended that creditors be required to maintain for public review, and oversight by its regulatory agency, a statistical compilation of the rates charged and amounts financed. Such a record would provide the consumer with a factual basis for evaluating creditors similar to the "stats" provided baseball fans for evaluating players and their teams. The responsibility for this compilation should be directed toward the creditor with the regulatory agency evaluating the correctness of such disclosures.

9. Enact Truth in Savings. Passbook savings accounts are directly comparable with open-end consumer credit accounts. Both involve the application of a periodic percentage rate to the balance at the end of the period to compute an amount which is called the Finance Charge for credit, and Earnings for Savings.

CONCERNS OF CONSUMER MEDIA

Ms. Mary-Beth Kuester*

In 1977, a questionnaire was designed and mailed to journalists designated as consumer writers by their newspapers. The mailing was national in scope, reaching both large and small dailies. The survey was organized by Consumer Concepts, consultants in consumer affairs, working with a group of graduate students in marketing at the Business School of the University of Wisconsin-Madison. This report includes principal conclusions, supporting data and observations relevant to the thrust of consumerism in the United States.

Introduction

The importance of the consumer movement in the United States is undeniable. It has grown from maverick to institution in just a few years. Concern for the consumer now has one of the highest priorities for executives in business and industry, for officials of both state and federal governments.

As professional journalists--and thoughtful students of their assigned subjects--consumer reporters may readily be perceived as leaders in communicating the thrust of the consumer movement. By contrast to a good number of advocates, consumer writers tend to be generalists rather than specialists. Intellectually and emotionally, they are in tune with their communities...responsive to consumer issues that are meaningful and current to their fellow citizens, the people who read their newspapers.

These writers are in direct touch with the pulse of local consumer interests and issues. Their testimony would seem to be vital to anyone measuring the directions of consumerism in America. As a result, we decided to solicit their responses in a national survey.

What did we expect to gain from our study of newspaper consumer writers?

1. An indication of current consumer concerns and the degree of their relative importance.

2. An understanding of the status of consumerism in the U.S. newspaper establishment.

3. A measure of the confidence of consumer reporters in the effectiveness of federal and state programs.

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