Truth In Lending: What Constitutes Adequate Disclosure in Consumer Credit?

In 1968 the Truth-in-Lending Act became law. The Act was intended to better enable consumers to comparison shop for credit by requiring the disclosure of certain aspects of the loan (e.g., APR, number and amount of payments, total finance charges). It is nevertheless possible for lenders to comply with the requirements under the Truth-in-Lending Act while circumventing its intent. This educational program was designed to assist consumers who are engaging in credit search behavior by exposing those techniques.

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Background

Perfect information is assumed in competitive markets (Barron & Lynch, 1993). Indeed, consumers' ability to make rational decisions depends upon their having access to accurate information. To improve the quality of information provided to American borrowers, Congress passed the Truth in Lending Act (TiL) in 1968.

Under TiL, lenders are required to disclose to the borrower certain information regarding the proposed or pending loan. It was felt that this knowledge would benefit consumers by 1) providing a simple method of comparing competing loan offers, 2) allowing consumers to identify particularly good or bad proposals and 3) permitting borrowers to compare the merits of using existing liquid assets versus additional borrowing (Egan, Freeman & Simon, 1971). Among other things, lenders must disclose the cost of the loan, expressed as an annual percentage rate, an itemized total of the amount financed, the cost of the loan expressed in dollar terms and the number, amount and due dates of the payments required under the terms of the contract (Morganstern, 1972).

In the lending process, the potential for manipulating the consumer is highest during the actual signing of the loan contract, a process known in the trade as "closing the loan." By subtly controlling the terms of the interaction, it is possible for lenders to conduct the closing in a manner than ensures compliance with Truth in Lending while subjugating TiL's intent.

Educational Program Contents

"Into the Shark Tank: Surviving the Loan Closing Process," is an instructional package developed and produced Purdue University's Cooperative Extension Service describing how lenders can obscure the intent of the Truth in Lending Act. The materials were designed for use with several diverse audiences in the context of a basic money management information course or series of seminars.

A short videotape presents several vignettes illustrating ways in which the loan closing may be directed by the loan officer to manipulate the consumer. The host of the video is a former loan officer who was trained in using these techniques and speaks from personal experience. Each is followed by a brief explanation in which the host exposes the manipulation, describes why each is so effective and offers suggestions for countering each.

The package also includes camera-ready copies of reading materials summarizing the information presented in the video (designed as handouts for program participants), and pre- and post-test participant evaluation tools. Program evaluations ($t=1.88$, $p=.05$) indicate that participants completing the program are better equipped to enter the consumer credit arena and negotiate a contract satisfactory to both borrower's and lender's interests.

References

Barron, J., & Lynch, G. (1993). Economics (3rd ed.). Boston: Irwin.

Egan, J.O., Freeman, J.T., & Simon, H.M. (1971). The impact of truth in lending on automobile financing: An empirical study. In C. Vanderwold (Ed.), Legal problems of consumer credit. Davis, CA: University of California-Davis Press.

Morganstern, S. (1972). Legal regulation of consumer credit. Dobbs Ferry, NY: Oceana Publications.

Endnotes

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