FINAL REPORT OF THE
JOINT SUBCOMMITTEE STUDYING

The Laws Governing Savings Institutions, The Interstate Activities of Financial Institutions and and the Interest Rate Laws of the Commonwealth

TO THE GOVERNOR AND
THE GENERAL ASSEMBLY OF VIRGINIA

House Document No. 40

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Final Report of the Joint Subcommittee
Studying the Laws Governing Savings Institutions,
the Interstate Activities of Financial Institutions
and the Interest Rate Laws of the Commonwealth

TO: The Honorable Gerald L. Baliles
Governor of Virginia
and
The General Assembly of Virginia

INTRODUCTION

The joint subcommittee studying the laws governing savings institutions, the interstate activities of financial institutions and the interest rate laws of the Commonwealth was established pursuant to House Joint Resolution No. 30 of the 1984 Session of the General Assembly. During the 1984 interim the subcommittee studied all three issues and recommended legislation to revise the laws governing the savings institutions and the interstate activities of the savings institutions and to enact statutes regulating interstate banking. Both of those bills were passed by the 1985 Session of the General Assembly and enacted into law. House Document No. 20 printed, January, 1985, is the report of the subcommittee on its work during the 1984 interim. The subcommittee recommended in that report that a resolution be passed by the 1985 General Assembly to continue the study of the subcommittee in order that it may further deliberate and consider the revision of the interest rate laws of the Commonwealth and to monitor the interstate activities of the banks and savings institutions of Virginia and to monitor newly revised savings institution statutes. The 1985 General Assembly passed House Joint Resolution No. 217 to continue the study. During the 1985 interim the subcommittee studied the interest rate laws of the Commonwealth and recommended legislation to revise the interest rate statutes. House Document No. 28, printed January, 1986, is the report of the subcommittee's work during the 1985 interim. House Bill No. 400 was introduced in the 1986 General Assembly, but due to its complexity and the issue concerning the regulation of second mortgage lenders the bill was carried over to the 1987 legislative session. House Joint Resolution No. 41 was introduced during the 1986 session to continue the study of the interest rate laws and it was passed by the 1986 General Assembly. The resolution also directed the joint subcommittee to study the credit card situation in Virginia, to consider some sort of regulatory scheme for unsupervised lenders and to study add-on interest rates to determine if they should be abolished. That resolution reads as follows:

HOUSE JOINT RESOLUTION NO. 41

House Amendments in [ ] - February 10, 1986

Continuing the joint subcommittee established pursuant to House Joint Resolution No. 30 of 1984, and continued under House Joint Resolution No. 217 of 1985, to review the savings and loan laws and interest rate laws of the Commonwealth, and interstate banking.

WHEREAS, House Joint Resolution No. 30 of the 1984 General Assembly established a joint subcommittee to study the issue of interstate banking and to revise the savings and loan laws and interest rate laws of the Commonwealth; and

WHEREAS, although the joint subcommittee was able to complete for the most part its work on the interstate banking issue and on the revision of the savings and loan laws, it was unable to complete its work on the interest rate laws revision because of the complexity of the issues and thus was carried over for additional study by House Joint Resolution No. 217 of the 1985 General Assembly; and

WHEREAS, the interest rate subcommittee of the full joint subcommittee was for the most part able to complete its work on the interest rate revision yet feels it needs to continue its study to fine-tune and monitor the law changes; now, therefore, be it

RESOLVED by the House of Delegates, the Senate concurring, That the joint subcommittee established pursuant to House Joint Resolution No. 30 of the 1984 General Assembly and continued pursuant to House Joint Resolution No. 217 of the 1985 General Assembly, be requested to continue its study of the savings and loan laws and interest rate laws of the Commonwealth, and interstate banking.

During its study the joint subcommittee shall not only continue to work on the interest rate revision but shall also: (i) continue to monitor interstate banking and savings legislation and activities; (ii) study the credit card situation in Virginia; (iii) consider some sort of regulatory scheme for unsupervised lenders; and (iv) study add-on interest rates to determine whether they should be abolished.

The membership of the joint subcommittee shall remain the same and any vacancy that should occur in the membership shall be filled by the same person or committee as provided in House Joint Resolution No. 30 of 1984.

All agencies of the Commonwealth shall assist the joint subcommittee in its study.

The joint subcommittee shall complete its work [~~in time to submit recommendations to the 1987 Session of the General Assembly~~ prior to November 15, 1986].

The costs, including direct and indirect costs, of this study are estimated to be $18,600.

Delegate George H. Heilig, Jr., of Norfolk continued to serve as chairman of the subcommittee. The other members of the House of Delegates serving were: William T. Wilson of Covington, Alson H. Smith of Winchester, Franklin P. Hall of Richmond and Vincent F. Callahan, Jr. of McLean. Senator William F. Parkerson, Jr. of Henrico remained the Vice-Chairman of the subcommittee. The other Senate members serving or appointed to serve on the joint subcommittee were Peter K. Babalas of Norfolk and Richard J. Holland of Windsor; appointed to serve was Elmon T. Gray of Waverly who was appointed to serve due to the death of Senator Edward E. Wiley of Richmond. Two citizens members, John B. Bernhardt Vice-Chairman of the Board of Sovran Bank and Edwin B. Brooks, President of Security Federal Savings and Loan Association, continued to serve with the subcommittee.

C. William Cramme', III, Senior Attorney and Terry Mapp Barrett, Research Associate of the Division of Legislative Services served as Legal and Research staff for the subcommittee. Barbara Hanback and Ann Howard of the House Clerk's Office provided administrative and clerical staff for the subcommittee.

WORK OF THE SUBCOMMITTEE

The full joint subcommittee held it first meeting on July 15, 1986. Representatives of the various financial institutions and the State Corporation Commission were asked by the Chairman of the subcommittee to update the subcommittee on recent state and national interstate activities and law changes. The meeting was also held to hear from a representative from the Tayloe Murphy Institute at the University of Virginia regarding the 1985 credit card billing practices study. Thirdly, the meeting was held to discuss the method by which the full joint subcommittee would study the interest rate laws and House Bill 400 that was carried over by the 1986 General Assembly.

Representatives of the Virginia League of Savings Institutions testified that currently the states are controlling by their statutes, interstate activities. They stated that the Federal Home Loan Bank Board has the regulatory authority to permit interstate activities on a national basis when an institution is in trouble. They stated, however, that there is very little interstate activity in Virginia.

Representatives of the Virginia Bankers Association stated that there is great concern over a bill in Congress that will force states to permit interstate banking on a national basis after five years. However, that bill was still pending in Congress. They noted that another bill that would close the non-bank bank loophole was still pending in Congress. They advised the subcommittee that in the southeast region of the United State, twelve of the thirteen states *had adopted interstate banking legislation that, in most cases, closely parallels Virginia's interstate banking statute. They added that seventeen other states outside the region had adopted interstate banking legislation. They also briefly explained various interstate activities and acquisitions being made by Virginia banks outside of the State. They noted that there is a little activity from out-of-state banks attempting to move into Virginia through interstate acquisitions. Due to one of the out-of-state banks attempts to purchase a Virginia savings institution, the Bankers stated that there may be need to make technical changes to the Virginia interstate banking statutes and savings institution statutes in order to clear up the issue of a bank purchasing a savings and loan and thereby avoiding the interstate banking and savings institution statutes.*

Representatives of the State Corporation Commission's Bureau of Financial Institutions testified that in the particular acquisition commented on by the Bankers Association, North Carolina National Bank is attempting to acquire Ameribank Savings Bank, and that particular acquisition is causing problems due to the fact that there is a question whether a bank can acquire a healthy thrift institution. They stated that the law presently requires that prior to being acquired institutions must be in existence continuously for two years and that the bank holding company act has been interpreted as prohibiting the acquisition of a savings and loan by a bank holding company. They explained that NCNB proposes to acquire a small bank, and since the law permits the merger of savings and loans directly into banks, they are proposing to merge the savings and loan into that bank. They explained further that they could not convert that savings and loan into a bank and then acquire that bank because of the two year restriction.

Representatives of the Bureau also testified that some questions had been raised regarding recent changes in Washington, D.C.'s laws regarding interstate banking. They advised the subcommittee that the laws and regulations require institutions acquiring D.C. banks to make certain capital investments in the Washington area and provide certain services in certain areas, such as providing for certain number of jobs, and loans to low and middle income people. They explained that the Virginia Act provides that the Commission shall impose upon the institution seeking to acquire a Virginia institution whatever restrictions and regulations that that jurisdiction from which the institution comes would impose on a Virginia bank seeking to acquire an institution in that jurisdiction. He noted that the acquisitions that had already been approved would not be affected.

The Bureau's representatives also testified that representatives of the Bureau had met with the regulatory authorities with other states and executed written agreements with those states that pass regional reciprocal legislation as of the first of the year.

A representative of the Tayloe Murphy Institute of the University of Virginia discussed their study of the credit card billing practices. She stated that the study was requested by Senate Joint Resolution No. 34 of 1985 and the results are found in Senate Document 4 of 1986. The study focused on three public policy issues: (1) Is the disclosure of the methods used by the issuer to assess finance charges adequate; (2) Is the card billing efficiently done; and (3) Is the credit card fairly priced. She explained that critical to the investigation was information received from Virginia bankers and retail stores. They noted that the Virginia Bankers Association and the Retail Merchants Association helped them in designing the survey to which they had a very good response. In reviewing the findings of the study, she explained that one of the study's main findings is that consumers find it difficult to understand how the timing of their payments affect their finance charges and how their finance charges are computed. The second finding of the study was that banks and retailers with large volumes of credit card transactions have made card processing more efficient by the application of electronic technology to these operations. They noted that payments are increasingly posted to the accounts soon after the day of transaction and payments are credited on the day of receipt. They noted that most card issuers mail their bills no later than 6 days after the close of the billing cycle. The third finding, she reported, related to the fairness of credit card financing and the need to find a way to reduce any subsidies that customers who carry balances over from one billing period to the next make to support the convenience need of those who do not carry balances over. Regarding the legislation passed in 1986 requiring the posting of payments within two banking days of their receipt, she stated that the affect of the law most likely would be greatest on card issuers who handle large volumes of payments and specify particular payment addresses. She noted that in her survey a small percentage of banks and retailers indicated that they take longer than two days in crediting non-conforming payments. Regarding a proposal for a ceiling on credit card interest rates, she stated, some states have them and that information regarding their finance charges and fees is included in Senate Document 4 of 1986. In considering whether to establish a ceiling, she said, it would be difficult to determine how Virginia card issuers would fair under such a restricted ceiling, since now with interstate banking, more banks will be coming into the Commonwealth. She questioned the benefits of a strict ceiling to credit card issuers. She also advised the committee that at that time there were eleven bills in Congress relating to credit card pricing, two of which mandated a cap. She testified that one of the eleven bills ties the cap to the treasury bill rate plus 5%. She explained further that three bills are related to thorough disclosure of credit card rates particularly in credit card solicitations and advertising. She testified that the direction of Congress seems to be in the improved disclosure requirement rather than a cap. In summing up, she stated, that better information in use of credit cards is needed to determine the best method for computing the finance charges and that information is also needed on what card features are considered to be most important, how important the finance rate is to customers and how often do cardholders switch cards.

The members of the subcommittee noted their concerns about the affects of placing a cap on finance charges on credit cards by stating that due to interstate banking, the imposed limit on credit card rates would not affect those banks coming into Virginia and that the banks in Virginia may be at a competitive disadvantage. Other members stated that if they limit the rate, those who need the credit card would be affected more dramatically than those who pay it off each month since banks would be more selective in choosing persons to whom they will issue cards. They pointed out that the General Assembly would have to weigh the cost in benefits of restricting rates before doing so. The Virginia Bankers Association's response to the Tayloe Murphy Report appears as Appendix 1 to this report.

Following the July 15th meeting, Delegate Heilig appointed members to serve on two subcommittees. He decided that a House Bill 400 subcommittee and a Credit Card Subcommittee should be established to study the respective issues in an effort to save time and to effectively and expeditiously study the matters. He decided to chair the subcommittee on House Bill 400 and appointed the following members to serve with him: Senator William F. Parkerson, Jr., Delegate Franklin P. Hall, Delegate Vincent F. Callahan, Jr., Senator Richard J. Holland and Edwin B. Brooks. He appointed Delegate Lewis W. Parker to chair the Credit Card Subcommittee and the following members to serve with him on that committee: Delegate Alson H. Smith, Senator Elmon T. Gray, Delegate William T. Wilson, Senator Peter K. Babalas and John B. Bernhardt. Both subcommittees held two meetings; each met on September 16 and December 16, 1986. The full joint subcommittee held its final meeting on January 20, 1987 at which time it made its final recommendations. The findings and recommendations of the two subcommittees of the full joint subcommittees will be related in the REASONS FOR RECOMMENDATIONS portion of this report.

All of the meetings of the full joint subcommittee and of the two subcommittees of the full joint subcommittee were public hearings and representatives of the following industries and associations offered testimony and assistance to the subcommittee: the Virginia Bankers Association, the Virginia League of Savings Institutions, the Virginia Independent Bankers Association, the Bureau of Financial Institutions of the State Corporation Commission, the Virginia Mortgage Association, the Virginia Mortgage Bankers Association, the Virginia Credit Union League, the Virginia Consumer Finance Association, the law firm of Mays, Valentine, Davenport and Moore, the law firm of McGuire, Woods and Battle, the Virginia Retail Merchants Association, Beneficial Management Association, Household International, Virginia Industrial Loan Association, the law firm of Thomas and Fiske, the Virginia AFL-CIO, the Virginia Manufacturers Association, and several businesses and companies representing themselves. Also, private citizens attended the meetings and offered testimony and advice to the subcommittee. After hearing testimony from all the interested parties, the subcommittee thoroughly discussed and carefully considered which recommendations to make to the 1987 General Assembly. At its January 20th meeting, the subcommittee announced those recommendations.

RECOMMENDATIONS

The subcommittee offers the following recommendations to the General Assembly.

I. THAT THE GENERAL ASSEMBLY SHOULD PASS AN AMENDMENT IN THE NATURE OF A SUBSTITUTE FOR HB 400 TO REVISE AND REORGANIZE THE MONEY AND INTEREST RATE LAWS OF THE COMMONWEALTH. THAT SUCH LEGISLATION SHOULD REORGANIZE AND REARRANGE THE MONEY AND INTEREST RATE STATUTES IN A MORE LOGICAL MANNER. THAT SUCH SUBSTITUTE SHOULD INCLUDE THE CHANGES MADE TO THOSE STATUTES BY THE 1986 GENERAL ASSEMBLY. THAT SUCH LEGISLATION SHOULD UPDATE THE LANGUAGE IN THE MONEY AND INTEREST RATE STATUTES TO PUT THEM IN MODERN-DAY AND READABLE TERMS, AND SHOULD MAKE SUCH CLARIFYING CHANGES AS NECESSARY AND AS FEW SUBSTANTIVE CHANGES AS POSSIBLE TO ACCOMPLISH THIS UPDATE.

II. THAT THE GENERAL ASSEMBLY SHOULD PASS A BILL TO REQUIRE ISSURERS OF CREDIT CARDS TO DISPLAY ON THE UPPER PORTION OF EACH MONTHLY STATEMENT, IN WORDS AT LEAST EQUAL IN SIZE TO THE WORDING OF THE MINIMUM PAYMENT TERMS, UNDERSTANDABLE LANGUAGE INFORMING THE CONSUMER HOW TO AVOID FINANCE CHARGES ON HIS ACCOUNT.

III. THAT THE GENERAL ASSEMBLY SHOULD PASS LEGISLATION TO MAKE THOSE NECESSARY TECHNICAL AMENDMENTS TO THE BANKS' AND SAVINGS' INSTITUTIONS INTERSTATE STATUTES WHICH WILL CLOSE ANY EXISTING LOOPHOLES WHICH MAY ALLOW NONREGIONAL FINANCIAL INSTITUTIONS TO ENTER VIRGINIA.

REASONS FOR RECOMMENDATIONS

I. THAT THE GENERAL ASSEMBLY SHOULD PASS AN AMENDMENT IN THE NATURE OF A SUBSTITUTE TO HB 400 TO REVISE AND REORGANIZE THE MONEY AND INTEREST RATE LAWS OF THE COMMONWEALTH. THAT SUCH LEGISLATION SHOULD REORGANIZE AND REARRANGE THE MONEY AND INTEREST RATE STATUTES IN A MORE LOGICAL MANNER. THAT SUCH SUBSTITUTE SHOULD INCLUDE THE CHANGES MADE TO THOSE STATUTES BY THE 1986 GENERAL ASSEMBLY. THAT SUCH LEGISLATION SHOULD UPDATE THE LANGUAGE IN THE MONEY AND INTEREST RATE STATUTES TO PUT THEM IN MODERN-DAY AND READABLE TERMS, AND SHOULD MAKE SUCH CLARIFYING CHANGES AS NECESSARY AND AS FEW SUBSTANTIVE AS POSSIBLE TO ACCOMPLISH THIS UPDATE.

In making this recommendation, the subcommittee noted that House Document No. 28 explains most of the reasons for the need of providing a new order in the organization of the interest rate statutes and the need to remove archaic language in order to update the statutes and add provisions new to the interest rate laws. Those reasons were found between pages 6 and 13 of that document. The subcommittee restated its position that House Bill No. 400 was introduced during the 1986 Session to rearrange and clarify existing law. Due to the considerable time spent by the House Committee on Corporations, *Insurance and Banking on a separate bill which dealt with a separate mortgage lender issue, House Bill 400 was carried over. The subcommittee agreed that with some exceptions, the substitute bill they are recommending to the 1987 General Assembly is meant to provide clarification to current money and interest rate statutes and to make as few substantive changes as possible to modernize and rearrange money and interest rate statutes.*

A. Non-Substantive Changes.

Some of the non-substantive, clarifying changes made to the money and interest rate statutes are as follows:

1. Those changes necessary to conform House Bill No. 400 to the changes made by the 1986 General Assembly;

2. Changes in the section establishing the legal rate of interest to include installment sales contracts and/or loan contracts;

3. The inclusion of new language in the section establishing the contract rate of interest (i) to allow a lender to collect interest and other charges in the amounts agreed upon by the parties in any case of a loan where the borrower is not permitted to plead usury, and (ii) to clarify that a lender may charge and collect other charges permitted by law in those instances where a loan or extension of credit is enforced as agreed upon or stated in the instrument of indebtedness and that those other charges are not to be included in the calculation of the applicable rate of interest;

4. Those changes in the section setting forth penalties for usurious transactions necessary to (i) remove a potential floating statute of limitations problem by requiring the suit or action to be brought within two years from the date of the last <u>*scheduled*</u> *payment, (ii) make this penalty provision section applicable regardless of whether the borrower made payments after he filed suit or not and (iii) include language which would state that any lender or creditor charging and collecting usurious interest as a result of a bona fide error in computation would not be liable for penalties described in the section but only required to return to the borrower the amount of interest collected in excess of that permitted. This last change would include within the statute what is presently common law in Virginia and provides uniformity since a similar provision exists for a subordinate mortgage statute.*

Another change to this section was suggested to the subcommittee for its review and recommendation. That change would have defined excess interest as that "in excess of that permitted by law", rather than "in excess of that permitted by the applicable statute." See page 3, line 6 of Appendix 2. However, the subcommittee found that the use of the word "law" would allow the imposition of the statutory penalties not only where a statute *made an interest charge illegal but also where a court decision made a charge illegal. For example, the common law prohibition on compounding of interest is only forfeiture for the amount of compound. By use of the word "law", the forfeiture would not only be the compound, but also the penalties provided in the section. The subcommittee decided to continue to use the term "applicable statute" rather than "law." They stated that they would not be in favor of changing the common law policy of forfeiture of the compound only, which has been a part of Virginia law since the first decided cases. See, Pindall's Ex'x vs. Bank of Marietta, 37 Va. (10 Leigh) 41 (1839). Secondly, as a practical matter, the new federal tax law they found was going to result in a number of new types of credit programs, many of which will involve variable rates and possible negative amortization. These programs will be desirable from the consumer's point of view because of the inability under the new tax law to deduct most types of consumer debt interest, unless the debt involves a real estate mortgage. However, they noted that they would not like to see a creditor who offers some innovative program to meet this need subjected to a double interest penalty and attorney's fees charged because compound interest resulted from a variable rate agreement. Thirdly, they disagreed philosophically with the concept of statutory penalties being applied to charges which are not made illegal by statute, but rather only by court decision. While noting that it is the province of the legislature, as the policy making branch of government, to determine by statute those acts which should be subject to a statutory penalty, they decided that the legislature cannot anticipate or control the decision by court declaring illegal some charge that is not expressly prohibited by statute. Therefore they decided that the continued use of the term "applicable statute" would be in conformance with the present part of the Virginia penalty statutes.*

5. The deletion of the word "service" and the insertion of the word "finance" before the word "charge" to conform the term with current terminology. The need for the change arose where a Norfolk Circuit Court judge held in the Spring of 1986 that the term "service charge" as it appears in old § 6.1-330.21 does not include "interest", and that while any amount of service charge the customer may have agreed to pay may be collected pursuant to § 6.1-330.21, any "interest" charged on a retail installment sale contract is limited to the 8% contract rate described by old § 6.1-330.11. Following the submission of briefs by several groups as amici curiae, and related oral argument, the judge reversed himself and ruled that "service charge" and that "interest" are synonymous for the purposes of § 6.1-330.21. The subcommittee decided that this problem suggested that perhaps clarification of § 6.1-330.21 as well as other sections of the money and interest rate statutes was desirable. They decided that clarification could be accomplished simply by substituting the term "finance charge" for "service charge" in the various statutes.

6. A rewriting of subsection D of the section allowing lenders to collect fees and charges in connection with loans secured by real estate to clarify the authority for the financing of such fees and charges;

7. Changes to the section requiring lenders to comply with the Truth-In-Lending statutes and regulations in offering or in extending consumer credit so that the state law does not require compliance with Truth-In-Lending with regard to a particular type of loan, even though the federal law itself does not require compliance; and

8. Those conforming and technical changes necessary to revise and rearrange in a more logical manner the money and interest rate statutes.

B. Substantive Changes

The following are the substantive changes to the money and interest rate statutes which the subcommittee recommends that the General Assembly adopt:

1. Definitions of the terms "bank", "credit union", "entity", "loans", "persons", and "savings institution" are included in Article 1 of the substitute legislation. The words "bank" and "savings institution" were not defined in prior statutes and are here defined as being both a Virginia bank and a bank outside of Virginia, and a Virginia savings institution and a savings institution from another state (both national and state banks and both federal and state savings institutions). Credit unions are treated similarly except for the exclusion of the federal credit union which is controlled by federal statute;

2. The legal rate of interest is increased from 6% to 10% with some thought of reducing that to 8% during the legislative process. The legal rate of interest is the implied rate of interest in a contract (other than a negotiable instrument) which says "interest" and does not specify a rate. The parties are presumed to have intended a 10% rate. Negotiable instruments are still controlled by the judgment rate pursuant to § 8.3-118;

3. The contract rate of interest is increased from 8% per year to 12% per year. This is the maximum rate which individuals may contract with each other unless they can find an applicable exception to this 12% maximum;

4. Regarding the penalties for usury, the defense to any unaccrued interest is maintained. The right to recover usurious interest paid has made the penalty more onerous. Previously it was twice the interest paid within the prior two years. This bill increases that to cover the double penalty plus the amount of excessive interest and attorney's fees, although national banks are subject to the federal statute of the double penalty;

5. The null and void penalty on usurious second mortgage loans made prior to July 1, 1986, is retained;

6. Credit unions are given the authority to make loans to its members and charge interest as agreed by the borrower and lender provided such interest is not charged in advance. Previous provisions relating to credit union authority to make loans to its members were limited to lending at a maximum rate of 18%;

7. The section which allows the private college or university in Virginia to make market rate interest loans to students, parents or guardians in order to defray college expenses which thereby denies the plea of usury on such loans made to such persons, is expanded by this substitute to include any loans made by such a school, the proceeds of which are used for educational expenses to anyone, notwithstanding the lack of formal appointment of guardian;

8. The statute that denies the plea of usury on business loans of $5,000 or more is amended to also prohibit a plea of usury for the compounding of interest in such cases. The subcommittee found that under the present money and interest rate statute relating to loans made by lenders that are secured by real estate negative amortization is allowed on first mortgage loans. They decided to make the change in the statute to allow negative amortization to be permitted with regard to corporations and businesses. This change will allow businesses to take second mortgages at negative amortization rather than refinancing the entire first mortgage. Although there is not a lot of demand for this they found that it makes a lot of sense to allow this type of lending activity particularly with todays commercial setting and the type of legal lending that is presently in the market. They also noted that it removes a loophole or trap in the law since someone making compounding loans to a business takes a risk presently under the law. The subcommittee felt that negative amortization, which sometimes occurs in adjustable rate loans, should be permitted with regard to business loans;

9. With regard to the change discussed in paragraph 8 above changes were made to deny a plea of usury to a corporation, partnership, professional association, joint venture, investment trust ect. in order to avoid the payment of compound interest. This permits negative amortization for corporate loans and other enumerated types of business loans;

10. Present § 6.1-330.40 is repealed due to the increasing from 8-12% the contract rate of interest. That section authorizes banks or brokers to make loans for agricultural purposes at 12% a year. This provision is made obsolete by increasing the contract rate of interest to 12%. Also, the subcommittee found that prior to 1984 there were three agricultural credit corporations in the Commonwealth of Virginia. By this statute they were authorized to charge one and one-half percent a year in excess of the rate offered them by the federal intermediate credit banks. Since that time, each of these corporations has severed their borrowing relationships with federal intermediate credit banks and are not considered bank subsidiaries. As bank subsidiaries they can charge any legal rate that a bank can charge. Also, the repeal of that section does not affect the status of any bank now existing in Virginia; and

11. Those changes necessary to conform the money and interest rate statutes with regard to the establishment by House Bill 1571 of the 1987 General Assembly creating a new class of regulated mortgage lenders, who previously were unsupervised and unregulated.

For the reasons cited above, the subcommittee recommends that the Amendment in the Nature of a Substitute for House Bill 400, attached as Appendix 2 to this report, be passed by the 1987 General Assembly, in order to revise and rearrange the money and interest rate statutes of the Commonwealth. The subcommittee agreed in making this recommendation that the changes to the money and interest rate statutes are meant to be stylistic and clarifying in nature and not intended to change statutory or common law, except in those instances referred to in this report.

II. THAT THE GENERAL ASSEMBLY SHOULD PASS A BILL TO REQUIRE ISSURERS OF CREDIT CARDS TO DISPLAY ON THE UPPER PORTION OF EACH MONTHLY STATEMENT, IN WORDS AT LEAST EQUAL IN SIZE TO THE WORDING OF THE MINIMUM PAYMENT TERMS, UNDERSTANDABLE LANGUAGE INFORMING THE CONSUMER HOW TO AVOID FINANCE CHARGES ON HIS ACCOUNT.

The Credit Card Subcommittee during its two meetings received both oral and written testimony from the Virginia Retail Merchants Association, the Virginia Bankers Association and persons representing consumers such as the Bank Cardholders of America and the Virginia AFL-CIO.

Representatives from the Virginia Retail Merchants Association testified that low interest rates on credit cards do not benefit all consumers and that it is important that the needs of various consumers are balanced. They stated that those who can get credit easy can benefit from a cap on rates and those that cannot will have to pay higher prices. Also, they noted, that for those that pay off their bills each month, interest rates are not crucial. They pointed out that some of the major problems resulting from placing a cap on interest rates include: (1) the rationing effect, i.e. less credit will be available and those who need it most (those who do not pay off their bills once they receive them) will not be able to obtain it; and (2) higher cash prices are created, i.e. when merchants are forced to offer services for less than their costs, they will have to make up the difference in prices. They pointed out that the support for caps on credit card interest has been based on misinformation. They explained that often people focus only on interest rates but pointed out that interest rates do not constitute the total cost of credit. See Appendix 3 of this report which is part of a study that speaks to the cost of credit, prepared by Touche Ross & Co. in July, 1986 and entitled <u>Economic Characteristics of Retail Store Credit</u>. They testified that people also overstate the cost impact of credit card rates by thinking that if a retailer charges an annual rate of 21% they will pay $21.00 for every $100 extended. They stated that credit cards are unique and not comparable to installment loans since it is actually cheaper to finance $1,000 on a credit card for one year than it is to finance $1,000 as a loan with an interest rate of 18%. They explained that the reason for this is that retailers do not charge finance charges for the first month or when the balance is paid off.

Further, the retail merchants stated that there have been a lot of questions as to why retail credit rates have not dropped when all other rates are down. They explained that retailers lagged behind others when rates went up so much several years ago and that the only thing that has gone down in recent years is the cost of borrowing money. They noted that since 1960, the minimum wage has risen from $1.40 per hour to $3.35 per hour and postage has risen from $.05 to $.22. Appendices 3 and 4 to this report discuss generally the cost retail stores incur to provide customers with credit services.

The retail merchants testified that some people have suggested that the solution to the problem is variable rates yet, they stated, all this would do would be to change the argument from that of the interest rate cap, to that of the base rate and how many points above the base rate should be charged. They stated that all variable rates are based on the cost of money relating to some index plus some percentage factor. They stated that variable rates create compliance problems for card issurers when rates change because when rates change they must freeze the rates on all balances and that this is very confusing to consumers since they do not know from one month to the next what the rates are. They explained that the variable rates will introduce a cyclical risk into the decision making process since no one will know what the rate will be next year.

Retail merchants argue that in Virginia where there is no rate ceiling and where there are 36 retailers providing store credit, one-half of such retailers are charging 18%, yet the highest is charging only 21.6%. They pointed out if they take into consideration how costs have changed over the years, 21.6% today is not out of line with 18% in the 1960's.

In regards to concerns recently raised over billing methods, the retail merchants stated that the choice of a billing method can have a great effect on rates and can, if a particular method is mandated, result in rationing. One method will benefit one type of consumer and another method benefits another type. They stated that the choice of billing method makes no difference when the cheapest method is compared to the most expensive, there is only a difference to customers, yet the cost to retailers is extensive. They suggested that disclosure of everything including (i) the monthly rate of charge, (ii) the balance upon which it is computed, and (iii) whether the balance upon which it is computed includes new purchases, and annual fees, is the right way to approach consumers concerns with credit card practices. In summarizing, they pointed out that if someone wanted to make a major purchase of $1,000, he could borrow from a bank or put it on his retail card and that putting the purchase on his retail card would not cost any more than getting a loan. They explained that over the period in which the loan or card would be paid off, borrowing at a lower rate would not necessarily be cheaper. They noted that with the retail plan the customer would probably pay off the balance in 8 or 9 months, but that with the bank it would take 12 months, and that the cost of such borrowing *would be less by borrowing on a credit card because of the free time built in by the retailer. They emphasized that one cannot look at the interest rate alone. See Appendix 4 of this report for testimony representative of that heard by the subcommittee from the Retail Merchants.*

The Virginia Bankers Association reviewed for the Credit Card Subcommittee three areas: (1) the question of interest rates; (2) the free period; and (3) disclosure. First, with respect to the interest rate question, the Bankers Association stated that there is some suggestion that Virginia already has a rate cap. However, they stated that they feel that the market place is working and that a number of Virginia banks have announced more variable rate options and have dropped their traditional 18% rate. They pointed out that in placing caps on in-state banks the legislature is not touching the out-of-state issuers who bring cards into Virginia. They testified that they feel such regulation would put Virginia's domestic corporations that are providing jobs and contributing to the economy at a very competitive disadvantage as opposed to those out-of-state card issuers. They noted that this out-of-state situation is not insignificant. Bankers estimated that 40% of the cardholders in Virginia carry an out-of-state card. Appendices 5 and 6 to this report are statements offered by Virginia Bankers Association and a small independent bank in Southside Virginia relating to credit card rates.

The Virginia Bankers stated that the 25-day free period mandated by state law allows the consumer to enjoy a free period from 30 to 60 days depending on when the purchase was made. They noted that it has been suggested that the free period be further extended to purchases made in a billing cycle when during that cycle an unpaid balance is carried over. They testified that it is their understanding that current law assumes that if you choose to convert the credit card to a credit instrument rather than a payment mechanism by choosing to carry a balance over to the next billing period you no longer get a free period for current purchases. They stated that they feel that the free period exists because of a legislative mandate but certainly do not feel that it should be extended further by a mandated legislative enactment. They advised the subcommittee that a more serious problem exists as far as the rate is concerned regarding out-of-state banks since out-of-state banks could continue to issue their cards in Virginia without meeting this requirement.

Concerning the last point relating to disclosure, the Bankers Association stated that some people feel that banks don't want to disclose, don't disclose, and the consumer does not know what rate he is paying or how to pay his bill to avoid finance charge. Representatives of the Bankers Association stated that monthly bills presently show the annual percentage rate and the amount you have to pay in order to avoid finance charges. They advised the subcommittee *that under Regulation Z of the Truth in Lending Act, banks are required to disclose certain information to cardholders on a monthly and annual basis and are required by state law each month to inform the cardholder what the requirements are.*

In response to the comments made by the Virginia Retail Merchants Association and the Virginia Bankers Association, a representative of the Virginia AFL-CIO stated that current interest rates provided by Virginia card issuers are not realistic in todays market. They stated that the AFL-CIO has negotiated on a national level with banks seeking to reduce credit card interest rates for their members. They stated that the national AFL-CIO and its participating unions formed a corporation in order to negotiate with banks. They noted that the difficulty with such negotiations was getting a bank large enough to handle an anticipated 30,000 cardholders. They advised the subcommittee that the application process in this credit card program is the same as with any other card and that various options are being provided to the membership. A representative of the Bank Card Holders of America submitted written testimony by mail to the subcommittee and it appears as Appendix 7 to this report.

In reviewing the available testimony and options that the subcommittee could take, the subcommittee reviewed current § 6.1-330.19:1 of the Code of Virginia which requires bank credit card issuers, after April 30, 1987, to provide to all new card holders and annually thereafter to all active accounts a certain notice concerning the imposition of finance charges on new purchases made during the current month in the event the balance was not paid in full. The subcommittee expressed its concern that cardholders were not receiving adequate warning about the imposition of finance charges on current purchases in the event that they do not pay their balance in full. The subcommittee decided that the present notice provided by that section was inadequate and recommended that a new notice provision be drawn to the existing statute to require that a notice be placed on the periodic statement to better advise consumers with respect to this issue. They decided that the notice would be in addition to the disclosure of the free period presently being given in the periodic statement as required by Regulation Z. However, the subcommittee had concerns that the amended form of the notice and the way in which they desired to propose it to be displayed on the periodic statement may be inconsistent with the applicable provisions of the Truth-In-Lending Act and Regulation Z. The subcommittee asked the Virginia Bankers Association to express its concerns to the Division of Consumer and Community Affairs of the Board of Governors of the Federal Reserve System and ask if the proposed new notice would be consistent with the Truth-In-Lending Act and Regulation Z. In response to their inquiry, that Division notified the bankers advising them that such a proposal would not be inconsistent with the Act or the Regulation.

For the reasons cited above, the subcommittee recommends that a new notice provision be drafted to replace the current notice provision in the bank credit card section and that a notice provision section be added to the retail merchants card section to require adequate information on the upper portion of the monthly statement to explain how a consumer can avoid finance charges on their account. Appendix 8 to this report represents the proposal of the subcommittee.

III. THAT THE GENERAL ASSEMBLY SHOULD PASS LEGISLATION TO MAKE THOSE TECHNICAL AMENDMENTS TO THE BANK AND SAVINGS INSTITUTION INTERSTATE STATUTES WHICH WILL CLOSE ANY EXISTING LOOPHOLES WHICH WOULD ALLOW NONREGIONAL INSTITUTIONS TO ENTER VIRGINIA.

Because of information received by the subcommittee reviewing House Bill No. 400, regarding attempts by holding companies outside of the Southeast Region, as defined in the Virginia Savings Institution Act and the Virginia Interstate Banking Act, to acquire institutions within Virginia, the subcommittee decided to make technical amendments to the interstate provisions of both the Savings Institution Act and the Banking Act. Under present law, a loophole may exist which permits a bank holding company outside of the southeast region, as defined in those acts, to acquire a Virginia savings institution or a savings institution holding company from outside the region to acquire a Virginia bank. The subcommittee decided that both statutes should be amended to make it clear that the acquiring bank holding company or savings institution holding company must be located within the southeast region as defined by Virginia statutes. Appendix 9 to this report represents that legislation which the subcommittee proposed in order to close the existing loophole.

For the reasons cited above, the subcommittee recommends that legislation closing the loophole in the interstate statutes which presently may allow a nonregional institution to enter Virginia to be pass by the 1987 General Assembly.

C. Recommendations agreed upon.

At its January 20th meeting, the subcommittee reviewed the drafts appearing in Appendix 2, 8, and 9 and unanimously agreed that these bills be introduced in the 1987 General Assembly to accomplish those three recommendations cited in this report above. They decided that it was their intent that these bills be introduced and forwarded on to the respected committees of the House and Senate, and if any further language changes need to be made that they be made in those committees. With regard to the Substitute for House Bill 400 being recommended by this subcommittee, the subcommittee reitterated at this meeting that this report should explain that the language changes being made to the Code by House Bill 400 were intended to be clarifying and stylistic in nature and not intended to substantively change the law except in those areas as noted by this report.

CONCLUSION

The subcommittee expresses its appreciation to all parties who participated in its study. The subcommittee expresses its desire that all parties who participated will continue to participate in the review of the bills recommended by this subcommittee as introduced in the 1987 General Assembly. The subcommittee's recommendations have been offered only after carefully and thoroughly studying the data and testimony that was received. The subcommittee believes that its recommendations are in the best interest of the Commonwealth and encourages the General Assembly to adopt those recommendations.

Respectfully submitted,

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William F. Parkerson, Jr., Vice-Chairman
Lewis W. Parker
William T. Wilson
Alson H. Smith
Franklin P. Hall
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Elmon T. Gray
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APPENDICES

1. *Virginia Bankers Association's response to credit card study.*
2. *Comparative Tables for H.B. 400. Substitute for H.B. 400.*
3. *Cost of credit study by Touche Ross & Co.*
4. *Thalhimer's testimony to credit card subcommittee.*
5. *Virginia Bankers Association's testimony on credit card rates.*
6. *Bank of Southside Virginia's testimony on credit card rates.*
7. *Bankcard Holders of America's testimony on credit card issue.*
8. *H.B. 1486.*
9. *H.B. 1079.*
   H.B. 1272.

VIRGINIA BANKERS ASSOCIATION
Response to
THE TAYLOE MURPHY INSTITUTE REPORT ON
CREDIT CARD BILLING PRACTICES IN VIRGINIA

Introduction

The credit card enjoys broad acceptance and extensive use. Virginia banks have over 2,559,000 cardholders. Although the exact figure is not known, the number would be ballooned substantially with the addition of Virginia cardholders holding cards issued by out-of-state banks and by various retailers.

The study finds that "although the Attorney General's Division of Consumer Council Office receives almost 2,000 complaints each year, fewer than 5% of them relate to credit." In other words, the Consumer Affairs Office only receives 100 complaints a year relating to credit. Even if half of these complaints relate to credit cards, the number of complaints compared to the number of cards in use is minuscule. The report further concludes that "few complaints about billing practices have come into local offices." There is simply no evidence that "many people" are concerned about their credit cards or credit card procedures. In fact, to the contrary, it would appear that the industry has an enviable record of consumer acceptance. We, therefore, find the conclusions of the study to be somewhat mystifying and in some cases based on faulty assumptions.

Response to Public Policy Issues

Page 2 of the report contains four "important public policy issues". Those issues are listed below with our response to each.

1. Is the information that credit card issuers provide concerning balance computation methods and a free period for which no interest is charged adequate to allow consumers to compare accurately and completely their credit options?

The information currently provided is mandated by Regulation Z. Among the numerous items that must be disclosed are the APR, the method of balance computation, a description of any other charges applied, and a description of the free period provided. The furnishing of additional information runs the risk of violating Regulation Z. Regulation Z permits additional disclosure only if it is not confusing or distracting of attention from the information already given. Such a determination that additional information was not confusing or distracting could be fraught with legal complications.

Regulation Z, although it gives very complete information to the consumer, gives the average consumer much more than he can absorb. Overdisclosure of too many items may result in no disclosure at all.

2. Does competition for credit card business sufficiently protect consumers from inefficiencies of credit grantors in the processing and handling of credit card transactions?

Virginia is really a part of a national market with respect to credit cards. Today there are approximately 130 million bank cards in the possesion of consumers. In addition, there are over 350 million retail credit cards, 113 million oil company credit cards, and several million other types of credit cards. Over 13,000 banks issue VISA, MASTERCARD, or other bank cards. In addition to the existing competition, there are entrants appearing almost every day. Sears has begun testing its multipurpose Discover Card; Shell has announced a new multipurpose card; Household International has also indicated intentions to market a similar product.

It seems quite apparent that the credit card industry is a marketplace that has been competitive and is rapidly becoming even more competitive.

Consumers recognize the value of the credit card and the services that it provides. It is a safe, convenient, secure method of payment for a vast array of retail purchases. It provides a monthly accounting of those purchases and allows the option of either full payment or partial payment and the use of the credit feature of the plan.

Consumers are very astute. If they feel they are not getting their money's worth from their card and its services, they will pick up their assets and walk across the street to the service provider they feel has the best combination of price and services. In short, we would suggest that competition for credit card business does sufficiently protect the consumer. The principles of the free enterprise system are certainly very much at work in the credit card business.

3. Does a loss of earnings from a statutory free period result in higher finance charges, reduced availability of credit card plans, and restriction of consumers' credit card choices to fewer outlets? Should a free period be required by law?

The 25-day free period does not cause reduced availability of credit card plans, nor is there any evidence that it restricts the consumers' credit card choices to fewer outlets. Further, the free period does not cause a consumer to pay higher finance charges. In fact, the contrary is probably true. The credit card is a volume operation and with sufficient volume, cost can be spread over a larger customer base for the ultimate benefit of all. If the free period were to be eliminated, an institution would potentionally lose 45% to 50% of its volume. Some of this volume would be eliminated entirely, some would go to other competitors, like American Express, and some would move to cash, debit cards, and checks. As a result, operating expenses per account for the revolver would increase since the volume that allows economy of scale would be reduced drastically.

The free period is an important competitive element of the product and a service the consumer values in making a product selection. As noted in the study, a free period would likely be provided even if not mandated by law.

4. Do cardholders who use the roll-over payment feature of revolving credit subsidize credit cardholders who pay their balances in full within the 30-day billing cycle?

To the extent that the added volume of non-revolvers spread fixed cost over a larger base, it could be argued that non-revolvers subsidize revolvers. For all the reasons stated in #3 above, however, subsidization is not a component of pricing strategy. In a fee market, a differential in price between two different products is expected. The fact that a large side-by-side refrigerator/freezer costs more than an apartment-size refrigerator does not mean that the price of one is subsidizing the price of the other; likewise with credit cards. To the non-revolvers, the card is a payment mechanism. To the revolver, it is a combination payment mechanism and a source of credit. There are additional costs associated in providing the credit feature which is covered in the interest charge. These costs include the cost of funds for carrying credit (around 90% of a card company's outstanding balance is generated by revolvers), additional accounting requirements to track credit extended, and the high frequency of payment default on the unsecured source of credit.

Response to Documentation

A number of additional comments need to be made with respect to major assertions in the report that are used to document the report's findings.

*On Page ii, is the statement ". . .a practice that is becoming more common is to charge interest in the second billing cycle retroactive to the date of the posting of each purchase to the account during the first billing cycle." An example of this is shown in Exhibits C.2 on Pages C-14 and C-15. We only know of one Virginia bank using this method of billing. This is hardly evidence of a "practice that is becoming more common." Moreover, this bank's methods of balance computation is not necessarily less fair to the consumer in that it provides a free period for current purchases when an account is in rollover status. A free period is not provided by other banks when an account is in rollover status. The point is simply this--various approaches used to compute balances can be shown to be more or less favorable to the consumer depending on the purchase pattern and billing period illustrated. Over time, they all average out about the same. The study proves the point it chooses to prove by use of selective snap shots in time which distort results.

*On Page iii is the statement ". . .people who have unpaid balances on their credit card can pay more than double the stated APR and not get a 25-day free period", and on Page C-17, the statement ". . .although the stated APR may be 18%, cardholders who rollover, say $100 each month, may pay more than double that rate." The supporting example in Table C.4, Page C-17, contains the statement that ". . .in essence the consumer revolves $100 for 12 months." This is not an accurate calculation. The consumer actually has $100 credit for days 1-9 of each of the 12 months, $300 for days 10-31 in January, and $400 for days 10-31 from February through December. It is obvious, even to the casual reader, that the consumer in this example revolved more than $100 for 12 months. The average daily credit actually revolved is $302.82, yeilding an APR of 18%, not 54% as alleged in the study report. In short the example on Page C-17 is critically flawed, and the conclusion that people are paying more than double the stated APR is without merit.

*On Page 6, the study gives an analysis of four methods of computing finance charges. In this analysis, the average daily balance is the second most expensive, with previous balance being the most expensive. We would suggest that the example chosen is inappropriate. A more typical example would be one using a balance of $1000 with $140 payment and purchases of $80 both on the 15th day. This example shows that average daily balance is the third most expensive with both previous balance and ending balance being the most expensive. The point is simply that average daily balance is the most equitable approach to computing a balance for the purpose of determining interest. It takes into account the actual days a given amount of credit was actually extended. Conversely, previous balance and/or ending balance may be more expensive or less expensive depending on the quirk of timing and the balance that any one individual might have at the time the previous or ending balance was computed.

*On Page 14, the report contains the statement, "Over 47 percent of all bank and retail cardholders pay no finance charge." We would agree that the non-revolvers contribute from 45% to 50% of retail sales volume. However, the percentage of customers billed each month who do not pay finance charges actually range from 20% to 30%, and non-revolves constitute only 10-12% of total outstanding balances for most credit card operations. Stated another way, even though 45-50% of sales voluem is generated by non-revolvers, the non-revolvers accounts for only 10-12% of outstanding balances because the non-revolver does pay in full at the end of the billing cycle.

Response to Suggested Legislative Options

The report lists seven legislative options. Our response to those options are as follows:

1. Prohibit calculation of finance charges using purchases from a previous billing cycle.

To our knowledge, there is only one Virginia bank that charges interest in the second billing cycle retroactive to the date of the posting of each purchase to the account during the first billing cycle. The bank offers a free period on all current purchases, even though the account may be in rollover status. It uses retroactive posting as a technique to capture interest on unpaid balances that occur when a customer fails to pay for purchases made in a previous billing cycle for which a free period had been extended. All other Virginia banks, because they do not extend a free period for current purchases when an account is in rollover, simply start a new billing cycle by carrying forward whatever unpaid balance existed at the close of the previous cycle. The suggested prohibition would uneccessarily remove a consumer option now available.

The main point to be made is that the consumer is in control. He can choose the card of the company that he feels offers the best deal for his objectives. He can choose to pay in full, as do about 1/3 of cardholders, and essentially just use the payment aspect of the card, or he can choose to pay only part of the balance, thus activating the credit feature.

2. Allow a user fee for a credit account by eliminating the statutory free period requirement.

An annual fee could also be called a user fee, but charged on an annual basis. The credit card has a worth to consumers in addition to that of a credit instrument. For example, it can be used as identification, as a means of guaranteeing hotel reservations, guaranteeing airline reservations, guaranteeing car rental, and so forth. In addition, it can be used to access a growing network of ATMs. An annual fee for this service is appropriate, as opposed to a transaction fee that would make the card "free" to the above listed users and load more cost on purchase users of the card.

3. Bar mininum finance charges and late fees.

Banks in Virginia do not charge minimum finance charges. On the contrary, if finance charges are less than a dollar during a billing period some banks in Virginia will suppress the bill and the consumer never sees it.

Late charges, on the other hand, are an inducement to maintain accounts on a current basis and they help offset expenses of collecting delinquent accounts. This is a very fair charge in that it is directed at the people who have late payments. It also allows banks to recover some of the administrative and overhead costs incurred as a result of having to institute collection proceedings.

4. Repeal the statute that mandates a free period be given on purchases of merchandise and services.

If "card-issuing Virginia banks are likely 'to follow the retailers' free period allowances so that their cards remain competetive with retail cards in the purchase of goods and services on credit", there is little purpose in repealing the statutory provision. Moreover, as previously pointed out, the card volume generated by the free period helps spread fixed cost over a larger base to the advantage of the revolver.

5. Simplify the state's consumer credit laws by deleting provisions relating to the mailing of card statements; monitor new and developing credit transaction methods.

As the survey of ten Virginia banks showed, our Virginia banks do mail statements in a timely manner. Most banks see statement timeliness and prompt posting of payments as important customer service issues. And, the bank has a compelling incentive to collect its payment at the earliest possible date. Uncollected funds are a profit drain to be avoided. Therefore, Virginia banks already comply with the 8-day Virginia mailing requirement rather than the more liberal 14-day Federal requirement that would exist if the proposed deletion were enacted. We see no problem to really be addressed in this area.

6. Require a standard method of assessing finance charges.

The preceived need for a standard method seems to be based on the already described erroneous assumption that consumers are paying double the stated APR. Moreover, if an institution wants to offer a different alternative to increase marketshare, via a more favorable method of computing finance charges, why shouldn't it be able to do so as long as it is disclosed? As quoted on Page 21 of this study ". . .methods of finance charge assessment should be a matter of choice by the creditor based on his competitive situation, financial condition, technical capabilities, and the needs and desires of his customers." Eliminating competition by mandating procedures cannot be in the best interest of the customer.

7. Provide Virginians information about consumer credit laws that clearly states how the APR, balance computation method, and free period affect the total cost of credit.

In part, the idea of providing more information that clearly states how the APR balance computation and free period affect the total cost of credit is based on faulty assumptions which we have already addressed. Beyond that, as we also noted earlier, we are not sure a Virginia disclosure would work any better than Regulation Z. Moreover, additional disclosure could cause legal problems with Regulation Z. While we do not oppose in any way the providing of needed information, we simply do not believe that the findings of this study present a compelling case of potentially violating the requirements already spelled out by Regulation Z.

Conclusion

In conclusion, we would point out that on Page 3 of the study is the statement that "Virginia has at least 55 card issuing commercial banks". Information for this report was collected by a survey from only 10 of those banks that are domiciled in Virginia. Under federal law and court decisions an out-of-state bank operates under the laws of the state in which it is domiciled and simply imports its card into Virginia. This being the case, it is critically important that Virginia law not disadvantage its own banks with over-restrictive regulations that limit their ability to compete with out-of-state institutions operating under more favorable statutes. In fact, it has been the recent policy of the Commonwealth to maintain a deregulated credit card market in order to retain Virginia's existing card operations and the jobs they provide, and to attract out-of-state card operations to Virginia. This policy has served Virginia well. Credit card operations have flourished in Virginia and the resulting intense competition has been good for the consumer. The Tayloe Murphy report fails to document a need or justification to change existing policy.

H.B. 400

NEW	OLD
6.1-330.49	New
6.1-330.50	6.1-330.6
6.1-330.51	6.1-330.7
6.1-330.52	6.1-330.8
6.1-330.53	6.1-330.9
6.1-330.54	6.1-330.10
6.1-330.55	6.1-330.11
6.1-330.56	6.1-330.45
6.1-330.57	6.1-330.46
6.1-330.58	New
6.1-330.59	6.1-330.47:1
6.1-330.60	6.1-330.13:1
	6.1-330.14:1
6.1-330.61	6.1-330.44
6.1-330.62	6.1-330.41
6.1-330.63	6.1-330.19:1
6.1-330.64	6.1-330.18
6.1-330.65	6.1-330.42
6.1-330.66	6.1-330.42:1
6.1-330.67	6.1-330.44:1
6.1-330.68	6.1-330.15
6.1-330.69	6.1-330.37
6.1-330.70	6.1-330.23
6.1-330.71	6.1-330.16
6.1-330.72	6.1-330.24
6.1-330.73	6.1-330.25
6.1-330.74	6.1-330.38
6.1-330.75	6.1-330.44
6.1-330.76	6.1-330.43
6.1-330.77	6.1-330.21
6.1-330.78	6.1-330.20
6.1-330.79	6.1-330.17
6.1-330.80	6.1-330.26
6.1-330.81	6.1-330.27:1
6.1-330.82	6.1-330.27:2
6.1-330.83	6.1-330.29
6.1-330.84	6.1-330.30
6.1-330.85	6.1-330.31
6.1-330.86	6.1-330.32
6.1-330.87	6.1-330.33
6.1-330.88	6.1-330.34
6.1-330.89	6.1-330.35
6.1-330.90	6.1-330.36

H.B. 400

OLD	NEW
6.1-330.6	6.1-330.50
6.1-330.7	6.1-330.51
6.1-330.8	6.1-330.52
6.1-330.9	6.1-330.53
6.1-330.10	6.1-330.54
6.1-330.11	6.1-330.55
6.1-330.12	Repealed
6.1-330.13:1	6.1-330.60
6.1-330.14:1	6.1-330.60
6.1-330.15	6.1-330.68
6.1-330.16	6.1-330.71
6.1-330.17	6.1-330.79
6.1-330.18	6.1-330.64
6.1-330.19:1	6.1-330.63
6.1-330.20	6.1-330.78
6.1-330.21	6.1-330.77
6.1-330.23	6.1-330.70
6.1-330.24	6.1-330.72
6.1-330.25	6.1-330.73
6.1-330.26	6.1-330.80
6.1-330.27:1	6.1-330.81
6.1-330.27:2	6.1-330.82
6.1-330.28	Repealed
6.1-330.29	6.1-330.83
6.1-330.30	6.1-330.84
6.1-330.31	6.1-330.85
6.1-330.32	6.1-330.86
6.1-330.33	6.1-330.87
6.1-330.34	6.1-330.88
6.1-330.35	6.1-330.89
6.1-330.36	6.1-330.90
6.1-330.37	6.1-330.69
6.1-330.38	6.1-330.74
6.1-330.39	Repealed
6.1-330.40	Repealed
6.1-330.41	6.1-330.62
6.1-330.42	6.1-330.65
6.1-330.42:1	6.1-330.66
6.1-330.43	6.1-330.76
6.1-330.44	6.1-330.61
	6.1-330.75
6.1-330.44:1	6.1-330.67
6.1-330.45	6.1-330.56
6.1-330.46	6.1-330.57
6.1-330.47:1	6.1-330.59

HOUSE BILL NO. 400

AMENDMENT IN THE NATURE OF A SUBSTITUTE

(Proposed by the House Committee on Corporations, Insurance and Banking on January 22, 1987)

(Patron Prior to Substitute–Delegate Heilig)

A BILL to amend the Code of Virginia by adding in Title 6.1 a chapter numbered 7.3, containing articles numbered 1 through 12 consisting of sections numbered 6.1-330.49 through 6.1-330.90, and to repeal §§ 6.1-330.6 through 6.1-330.46 of the Code of Virginia, so as to revise, rearrange and amend the laws of Virginia relating to money and interest generally; penalties.

Be it enacted by the General Assembly of Virginia:

1. That the Code of Virginia is amended by adding in Title 6.1 a chapter numbered 7.3, containing articles numbered 1 through 12 consisting of sections numbered 6.1-330.49 through 6.1-330.90, as follows:

CHAPTER 7.3.

MONEY AND INTEREST.

Article 1.

Definitions.

§ 6.1-330.49. Definitions.– As used in this chapter, unless the context indicates some other meaning:

"Bank" shall mean any national bank, any bank organized under Chapter 2 (6.1-3 et seq.) of this title or any bank incorporated and organized under the laws of another state or territory of the United States, or the District of Columbia.

"Credit union" shall mean any credit union organized under Chapter 4 (§ 6.1-196 et seq.) of this title or any credit union incorporated and organized under the laws of another state. "Credit union" shall not include within its meaning federal credit unions.

"Entity" shall mean any association, corporation, partnership, firm, company, trust, estate or joint venture.

"Loan" means a loan or forebearance of money.

"Person" shall include an individual or an entity.

"Savings institution" shall mean any savings institution, as defined in § 6.1-194.2, incorporated and organized under the laws of the United States, the Commonwealth, another state or territory of the United States, or the District of Columbia.

Article 2.

Money of Account.

§ 6.1-330.50. Money of account.–The money of account of this Commonwealth shall be the dollar, cent and mill. All accounts by public officers shall be so kept. No writing shall be invalid, nor the force of any account or entry be impaired, because a sum of money is expressed otherwise.

§ 6.1-330.51. Ascertaining value in money of account for money expressed in foreign currency.– In any suit for a sum of money expressed in any foreign currency or otherwise than in the money of account of this Commonwealth, the jury or the court shall ascertain the value in the money of account of the sum so expressed, making allowance for the difference of exchange as shall be just. The judgment or order may be for either the amount so ascertained, or for the amount of money so expressed which shall be discharged by an amount so ascertained. As to any such suit involving an instrument to which § 8.3-107 is applicable, the provisions of that section shall apply.

§ 6.1-330.52. Issuance of currency; contracts and securities obtained by illegal currency; capital stock of certain companies, etc., vested in State; proceedings to recover such stock; liability.– A. 1. No individual or entity unless authorized by law shall:

a. Issue, with intent that the same be circulated as currency, any note, bill, scrip, or other paper or thing, or

b. Otherwise deal, trade or carry on business as a bank of circulation.

2. All contracts made for forming any such entity as described in paragraph 1 of this *subsection shall be void.*

B. All contracts and securities that may originate from, or be made or obtained in whole or in part by means of any illegal currency dealing, trade or business, shall be void. If any person shall pay any money or other valuable thing on account of any such contract or security, such person or his or its representative, or assignee, may, by suit brought within one year after such payment, recover back the amount or value of such payment from the person or such representative to whom, or to whose use, it may have been made.

C. The capital stock of every such entity, whether paid up or merely subscribed, shall belong to the Commonwealth. The Attorney General, whenever informed of the existence of any such entity, shall institute a suit in the Circuit Court of the City of Richmond, for the purpose of recovering such capital stock. In such suit, all or any of the members of such entity, and any of its officers, agents, or managers, may be made defendants, and compelled to exhibit all their books and papers, and an account of everything necessary to enable the court to enter a proper order. But no disclosure made by a defendant in such suit, and no book or paper exhibited by him in answer to the bill, or under the order of the court, shall be used as evidence against him in any case at law.

D. Every member of any such entity, made defendant in any such suit, shall be held liable to the Commonwealth for his proportion of the capital stock in such entity held by him, or for his use or benefit, at the institution of such suit, or at the time of the order. Such order against any defendant shall be a bar to a proceeding against him for any act done in violation of subsection A of this section.

Article 3.

Legal and Judgment Rates of Interest.

§ 6.1-330.53. Legal rate of interest; when legal rate implied.—The legal rate of interest shall be an annual rate of ten percent. Except as provided in subdivision (d) of § 8.3-118 and § 6.1-330.54, the legal rate of interest shall be implied where there is an obligation to pay interest and no express contract to pay interest at a specified rate.

§ 6.1-330.54. Judgment rate of interest.—The judgment rate of interest shall be an annual rate of twelve percent, except that a money judgment entered in an action arising from a contract shall carry interest at the rate lawfully charged on such contract, or at twelve percent annually, whichever is higher.

Article 4.

Contract Rate of Interest.

§ 6.1-330.55. Contracts for more than legal rate of interest.—Except as otherwise permitted by law, no contract shall be made for the payment of interest on a loan greater than twelve percent per year.

For statutes which permit payment of interest greater than twelve percent per year, reference is hereby made to Article 6 (§ 6.1-330.60 et seq.), Article 7 (6.1-330.64), Article 8 (§ 6.1-330.65 et seq.), Article 9 (§ 6.1-330.69 et seq.), Article 10 (§ 6.1-330.75 et seq.) and Article 11 (§ 6.1-330.77 et seq.) of this chapter. Further reference is hereby made to Chapter 6, §§ 6.1-244 to 6.1-310, relating to powers of consumer finance companies; to § 38.2-1806, relating to interest chargeable by insurance agents; and to §§ 38.2-4700 through 38.2-4712, relating to interest chargeable by premium finance companies.

In the case of any loan upon which a person is not permitted to plead usury, interest and other charges may be imposed and collected as agreed by the parties.

Those provisions of this chapter providing that a loan or extension of credit may be enforced as agreed in the contract of indebtedness, shall not be construed to preclude the charging or collecting of other loan fees and charges permitted by law, in addition to the stated interest rate, and such other loan fees and charges need not be included in the rate of interest stated in the contract of indebtedness.

Article 5.

Usury; Penalty.

§ 6.1-330.56. Plea of usury; evidence; judgment.— Any borrower may plead in general

terms that the contract or assurance on which the action is brought was for the payment of interest greater than is allowed by statute. Once the court has determined that the contract is usurious, judgment shall be rendered only for the principal sum.

§ 6.1-330.57. Recovery of twice total usurious interest paid; limitation of action; injunction to prevent sale of property pending action.—A. If interest in excess of that permitted by the applicable statute is paid upon any loan, the person paying may, in a suit or action brought within two years from (i) the date of the last scheduled payment, or (ii) the date of payment in full, whichever is earlier, recover from the person taking or receiving such payments:

1. The total amount of the interest paid to such person in excess of that permitted by applicable statute;

2. Twice the total amount of interest paid to such person during the two years immediately preceding the date of the filing of the suit or action; and

3. Court costs and reasonable attorneys' fees.

B. If property has been conveyed to secure the payment of the debt and a sale thereof is about to be made, or is apprehended, an injunction may be awarded to prevent such sale pending the suit or action.

C. Any creditor who proves that interest or other charges in excess of those permitted by law was imposed or collected as a result of a bona fide error in computation or similar mistake shall not be liable for the penalties prescribed in this section, but shall only be liable to return to the borrower the amount of interest or other charges collected in excess of that permitted.

§ 6.1-330.58. Contracts, etc., in violation of public policy.—Any agreement or contract in which the borrower waives the benefits of this chapter or releases any rights he may have acquired by virtue of this chapter shall be deemed to be against public policy and void. The provisions of this section shall not apply to a waiver of benefits or release of rights made subsequent to a loan as part of a settlement of potential or pending claims by a borrower involving such loan.

§ 6.1-330.59. Applicability of §§ 6.1-330.56, 6.1-330.57 and 6.1-330.58 to certain loans made on or after July 1, 1986; effect of assignment; effect of errors in computation.—A. The provisions of §§ 6.1-330.56, 6.1-330.57 and 6.1-330.58 shall apply to all loans made under § 6.1-330.71 or former § 6.1-330.16 as amended in 1986, which are closed on or after July 1, 1986. Section 6.1-330.47 shall not apply to any loan closed on or after July 1, 1986.

B. As to any loan to which the provisions of §§ 6.1-330.71 and 6.1-330.72 are applicable, the borrower may assert any defense or claim he may have under §§ 6.1-330.56 and 6.1-330.57 against any assignee or transferee of the contract of indebtedness.

C. The provisions of § 6.1-330.47 shall continue to apply to loans made under former § 6.1-330.16 and closed prior to July 1, 1986. There shall be a presumption that a loan was closed on the date of initial recordation of the deed of trust or mortgage securing such loan.

D. The provisions of this section shall not apply to loans made by lenders enumerated in § 6.1-330.73, nor to loans closed prior to July 1, 1986.

Article 6.

Exceptions to Contract Rate of Interest;

Charges by Depository and Regulated Lenders.

§ 6.1-330.60. Charges by banks and savings institutions; installment loans.—Notwithstanding any statute or law relating to interest or usury, any loan made by a bank or savings institution payable in weekly, monthly or other periodic installments may be lawfully enforced as agreed in the contract of indebtedness. In addition to the foregoing, a loan fee not exceeding two percent of the principal amount of the loan may also be charged or collected in advance from the borrower. An interest rate charged in advance upon the entire principal amount of the loan or pursuant to a written modification agreement shall be lawful.

§ 6.1-330.61. Defense of usury not applicable to certain loans.– No person shall, by way of defense or otherwise, avail himself of the provisions of this chapter or any other section relating to usury to avoid or defeat the payment of interest, or any other sum, upon a loan made to a person by a bank, savings institution or credit union as defined in § 6.1-2.1, provided the initial principal amount of the loan is $5,000 or more.

§ 6.1-330.62. Loans of up to one year.–Any bank, savings institution, or any broker duly licensed to transact business as a stockbroker or as a broker dealing in options and futures under the provisions of Title 58.1, may loan money or discount bonds, bills, notes or other paper payable on demand or for periods of up to one year, and such loan or discounting may be lawfully enforced as agreed in the contract of indebtedness. An interest rate charged in advance upon the entire amount of the loan or discount shall be lawful.

§ 6.1-330.63. Charges by banks or savings institutions; revolving credit.–A.1. Any bank or savings institution may impose finance charges at such rates as may be agreed by the borrower under a contract for revolving credit or any plan which permits an obligor to avail himself of the credit so established. Any charges computed by application of a rate to outstanding balances shall be computed at the option of the bank or savings institution on:

a. The average daily balance for the period ending on the billing date;

b. The balance existing on the billing date of the month; or

c. Any other balance which does not result in the lender charging or receiving any sum in excess of what would be charged or received under subdivision 1a or 1b of this subsection.

2. No finance charge shall be imposed unless the bill is mailed not later than eight days (excluding Saturdays, Sundays and holidays) after the billing date, except that such time limitation shall not apply in any case where the lender has been prevented, delayed, or hindered in mailing or delivering the bill within such time period because of an act of God, war, civil disorder, natural disaster, strike, or other excusable or justifiable cause.

3. In the event of the extension of credit by a bank or savings institution hereunder to be effected by the use of a credit card for the purchase of merchandise or services, no finance charge shall be imposed upon the cardholder or borrower on such extension of credit if payment in full of the unpaid balance owing for extensions of credit for merchandise or services is received at the place designated by the creditor prior to the next billing date (which shall be at least twenty-five days later than the prior billing date).

4. Any payment, in full or in part, received by the bank or savings institution shall be credited within two banking days of its receipt.

5. As used in this section "average daily balance" means, for any billing period, that amount which is the sum of the actual amounts outstanding each day during the billing period divided by the number of days in the billing period.

B. The higher rate in excess of that permitted prior to July 1, 1982, shall not take effect as to balances existing on or before April 1, 1983, unless:

1. Such creditor shall notify the borrower in writing of the proposed change, that the higher charge on existing balances and balances incurred prior to the effective date of the change is accepted by use of the revolving credit after the giving of the notice, and such borrower is given at least nine months prior to the effective date of such change to pay off balances existing on the date of such notice;

2. Such borrower accepts the proposed change and modification of rate by using the revolving credit at any time thirty days or more after the giving by the creditor of the notice.

C. Beginning after April 30, 1987, in the case of any plan in which the charge authorized by this section is imposed on the average daily balance and such balance is calculated under the plan without excluding purchases incurred during the billing period, the issuer shall disclose to all new cardholders and, annually thereafter, to all active accounts, the following:

NOTICE

Unless the New Balance shown on your statement is paid in full by the next billing date, new purchases you make in the current month will be subject to Finance Charges that will be billed on the next month's statement.

Article 7.

Exception to Contract Rate of Interest;

Charges by Credit Unions.

§ 6.1-330.64. Credit union loans.–A. A credit union may make loans to its members and to other credit unions. Notwithstanding any other statute or provision relating to interest or usury, any credit union may charge interest as agreed by the borrower provided such interest is not charged in advance.

B.1. Any credit union contract for revolving credit or any plan which permits an obligor to avail himself of the credit so established may provide for computation of any finance charges by application of a rate, at the option of the credit union, to:

a. The average daily balance for the period ending on the billing date;

b. The balance existing on the billing date of the month; or

c. Any other balance which does not result in the credit union charging or receiving any sum in excess of what would be charged or received under item a or b of this subdivision.

2. No finance charge shall be imposed unless the bill is mailed not later than eight days (excluding Saturdays, Sundays and holidays) after the billing date, except that such time limitation shall not apply in any case where the credit union has been prevented, delayed, or hindered in mailing or delivering the bill within such time period because of an act of God, war, civil disorder, natural disaster, strike, or other excusable or justifiable cause.

3. In the event of the extension of credit by a credit union hereunder to be effected by the use of a credit card for the purchase of merchandise or services, no charge shall be imposed upon the member or cardholder on such extension of credit if payment in full of the unpaid balance owing for the extension of credit for merchandise or services is received at the place designated by the credit union prior the next billing date, which shall be at least twenty-five days later than the prior billing date.

4. As used in this section, "average daily balance" means, for any billing period, that amount which is the sum of the actual amounts outstanding each day during the billing period divided by the number of days in the billing period.

Article 8.

Exceptions to Contract Rate of Interest;

Charges by Non-Depository Lenders.

§ 6.1-330.65. Extension of credit under Securities and Exchange Act.–A broker-dealer licensed by the State Corporation Commission and registered with the Securities and Exchange Commission who extends credit to a customer on pledged securities as permitted under the provisions of the Securities and Exchange Act of 1934, may charge the customer on his debit balances that are payable on demand interest not exceeding an annual rate of one and three-quarters percent above the higher of:

1. The interest rate charged such broker-dealer by a bank doing business in this Commonwealth on loans collateralized by securities or

2. The interest rate charged such broker-dealer by a bank doing business in this Commonwealth on loans for business purposes.

§ 6.1-330.66. Charges by private colleges and universities.–Loans made by a private college or university in Virginia to defray educational expenses of its students for educational expenses, including but not limited to tuition, fees, books, supplies, room, board and personal expenses, may be enforced as agreed in the contract of indebtedness. For purposes of this section, the term "private college or university" shall mean a private, accredited and nonprofit institution of collegiate education in the Commonwealth whose primary purpose is to provide collegiate or graduate education.

§ 6.1-330.67. Loans by pension plans to participants.—Loans by a pension plan to an individual participating in such pension plan, including an "employee pension benefit plan" or "pension plan" as defined in § 3 (2) of the Employee Retirement Income Security Act of 1974, are not subject to the provisions of this chapter. No such participating individual shall, by way of defense or otherwise, avail himself of the provisions of this chapter, or any other law relating to interest or usury, to avoid or defeat the payment of interest or any other sum on any loan made by such pension plan. Nothing contained in any such law shall be construed to prevent the recovery of such interest or other sum though it is more than otherwise lawful interest and though that fact appears on the face of the contract.

§ 6.1-330.68. Charges by industrial loan associations.—A. Notwithstanding any statute or law relating to interest or usury, loans made by industrial loan associations payable in weekly, monthly or other periodic installments may be enforced as agreed in the contract of indebtedness. In addition to the foregoing, a loan fee not exceeding two percent of the principal amount of the loan may also be charged or collected in advance from the borrower. An interest rate charged in advance upon the entire amount of the loan or pursuant to a written modification agreement shall be lawful.

B. An industrial loan association may charge interest at an annual rate not exceeding eighteen percent on loans payable on demand or in a single payment. In addition, such association may impose on such loans the same loan fee allowed by subsection A of this section.

Article 9.

Exceptions to Contract Rate of Interest;

Real Estate Loan Transactions.

§ 6.1-330.69. Certain contracts enforced as agreed therein; definition of terms for this section and §§ 6.1-330.81 and 6.1-330.71.—A. Notwithstanding the provisions of §§ 6.1-330.53, 6.1-330.55 and 6.1-330.62 or any other law relating to interest or usury, contracts made for the loan of money, secured or to be secured by a first deed of trust or first mortgage on real estate, or by a first priority security interest in the stock of a residential cooperative housing corporation, may be enforced as agreed in the contract of indebtedness, or other agreement signed by the borrower.

B. For the purpose of this section and §§ 6.1-330.71 and 6.1-330.81:

1. Real estate shall be deemed to include a leasehold estate of not less than twenty-five years.

2. An interest rate which varies in accordance with any exterior standard, or which cannot be ascertained from the contract without reference to any exterior circumstances or documents, shall be enforceable as agreed in the contract of indebtedness or other signed agreement.

3. The terms "first deed of trust" or "first mortgage" shall include all deeds of trust and mortgages, and amendments thereto, which are made by the same grantor or mortgagor, secure notes held by the same holder, convey substantially the same real estate, and are superior to all other deeds of trust or mortgages on the real estate.

4. The terms "grantor" or "mortgagor" shall include an owner of the real estate, and spouse, who has assumed responsibility for the obligation secured by such deed of trust or mortgage.

C. Interest which is charged pursuant to a written agreement, whether or not recorded, shall be of equal priority with the principal debt secured by the mortgage or deed of trust and shall have priority as to third parties as provided in Title 55 of this Code.

D. Notwithstanding any other statute or rule of case law relating to compounding of interest, if regularly scheduled periodic payments on an obligation secured by a first mortgage or first deed of trust on real estate are insufficient to pay currently accruing interest on the then principal balance, an agreement in the contract of indebtedness, or other agreement signed by the borrower, providing for the addition of such unpaid interest *to the principal balance and the future accrual of interest on such balances, shall be enforceable as written.*

E. Disclosure of charges in a disclosure given to the borrower pursuant to federal disclosure laws or regulations and acceptance of the loan proceeds by the borrower shall be deemed an agreement signed by the borrower within the meaning of this section.

§ 6.1-330.70. Fees and charges in connection with loans by real estate lenders; certain borrowers not to be required to employ particular attorney, surveyor or insurer.—A. A lender engaged in making real estate mortgage or deed of trust loans, other than loans subject to the provisions of §§ 6.1-330.71 and 6.1-330.72, may charge or collect in advance from the borrower a loan fee as agreed between the parties. Such a lender also may require the borrower to pay the reasonable and necessary charges in connection with making the loan, including the cost of title examination, title insurance, recording and filing fees, taxes, insurance, including mortgage guaranty insurance, appraisals, credit reports, surveys, drawing of papers and closing the loan.

B. In the case of loans secured by deeds of trust or mortgages on one to four family residences, the lender may not require the borrower to use the services of a particular attorney, surveyor or insurer. However, the lender shall have the right to approve any attorney, surveyor, or insurer selected by the borrower, provided such approval is not unreasonably withheld. Any lender in compliance with the Federal Insurance Regulations of the Federal Home Loan Bank Board relating to loan services and fees as in effect on July 1, 1977, shall be deemed to be in compliance with this subsection.

C. The fees and charges permitted by this section and other sections of this chapter are in addition to those permitted by § 6.1-330.69 and may be added to the principal of the loan, and shall not be considered in determining whether a loan contract is usurious.

§ 6.1-330.71. Charges by other than supervised licensed lenders.—A. 1. Any person, other than lenders licensed by and under the supervision of the State Corporation Commission or the federal government or otherwise enumerated in § 6.1-330.73, may charge add-on interest that results in an annual yield of not more than eighteen percent upon loans secured in whole or in part by a subordinate mortgage or deed of trust on residential real estate improved by the construction thereon of housing consisting of one to four family dwelling units. For the purposes of this Chapter, a subordinate mortgage or deed of trust is one subject to a prior mortgage or deed of trust in existence at the time of the making of the loan secured by such subordinate mortgage or deed of trust. An add-on interest loan may be made only under this subsection and shall not exceed a period of ten years and two months.

2. The lender may also impose a loan fee not exceeding two percent of the principal amount of the loan provided that such loan fee shall not be imposed more often than once each eighteen months except to the extent that new money is advanced within such eighteen-month period by a renewal or additional loan. New money shall be money advanced in excess of the outstanding principal balance at the time such new advance is made. These provisions shall apply whether such loan fee is payable directly to the lender or to a third party in connection with such loan.

B. No charge, other than actual costs documented to the applicant and expended for a credit report and an appraisal of the real estate conducted in connection with the loan application, may be made if the loan is not made. Such charge shall not exceed one percent of the amount of the loan applied for; but in no event shall such charge exceed fifty dollars or one-half of such costs whichever is less. Such charge may be made only if the lender commits to make the loan. Such commitment shall be in writing and signed by the lender or a person the lender has authorized to execute such documents.

C. The provisions of this section shall not apply to any loan by any lender enumerated in § 6.1-330.73.

D. 1. Any loan secured by a subordinate mortgage or deed of trust on such residential real estate where the interest is charged at an annual interest rate on the unpaid balance thereof may be lawfully enforced at the annual interest rate stated in the contract of *indebtedness on the principal amount of the loan. Such annual interest rate may vary in accordance with an exterior standard.*

2. In addition to the annual interest rate permitted by subdivision 1 of this subsection, the lender may charge the borrower a loan fee not exceeding two percent of the principal amount of the loan. The lender may also charge the borrower with the actual costs of the loan as permitted by § 6.1-330.72.

3. In addition to the interest and loan fee permitted under subdivision 1 of this subsection and subdivision 2 of this subsection, no more than a three percent total charge for discount, initial interest, points or charges by any other name may be collected, charged or added to the instrument of indebtedness.

4. The loan fee permitted by subdivision 2 of this subsection and the additional charge permitted by subdivision 3 of this subsection shall not be imposed more often than once each eighteen months except to the extent that new money is advanced within such eighteen-month period by a renewal or additional loan. Such loan fee and charge may only be reimposed by the lender upon a borrower in connection with the refinancing of a loan made pursuant to this subsection.

E. Except as allowed in subsection D, above, no discount, initial interest, points or charges by any other name may be collected, charged or added to a loan secured by a subordinate mortgage or deed of trust upon such residential real estate.

F. Open-end credit may be extended under this section.

§ 6.1-330.72. Loans secured by subordinate mortgage; charges allowed; requirements relating to insurance.— A. Any lender making a loan secured by a subordinate mortgage or deed of trust may require the borrower to pay, in addition to the loan fee charge and interest permitted by § 6.1-330.71, the actual cost of title examination, title insurance, mortgage guaranty insurance, recording fees, surveys, attorney's fees, and appraisal fees. No other charges of any kind shall be imposed on or be payable by the borrower either to the lender or any other party in connection with such loan; provided, late charges in the amount specified in § 6.1-330.80 may be made and, upon default, the borrower may be subject to court costs, attorney's fees, trustee's commission and other expenses of collection as otherwise permitted by law. Broker's or finder's fees may be paid by the lender from the loan fee or interest permitted under § 6.1-330.71. A broker's fee, finder's fee or commission may be paid by the borrower not to exceed two percent of the principal amount of the loan if the total of the loan fee, charge, and broker's fees, finder's fees or commissions does not exceed five percent of the principal amount of the loan.

B. Evidence of fire and extended coverage insurance may be required by the lender of the borrower and the premium shall not be considered as a charge. Decreasing term life insurance, in an amount not exceeding the amount of the loan and for a period not exceeding the term of the loan, may also be required by the lender of the borrower and the premium shall not be considered as a charge. At the option of the borrower accident and health insurance may be provided by the lender, and the premium therefor shall not be considered a charge. Proof of all insurance issued in connection with loans subject to this chapter shall be furnished to the borrower within ten days from the date the loan is closed.

C. No charge may be imposed or collected, except as permitted by § 6.1-330.71, if the loan is not made.

D. This section shall not apply to any loan made by any lender enumerated in § 6.1-330.73.

§ 6.1-330.73. Applicability of §§ 6.1-330.71, 6.1-330.72 and 6.1-330.85.—Sections 6.1-330.71, 6.1-330.72 and 6.1-330.85 shall not apply to loans made by any lender licensed by, and under the supervision of the State Corporation Commission or the federal government, or to loans made by banks, savings institutions or state or federal credit unions.

§ 6.1-330.74. Limiting application of this chapter and other usury sections in actions for recovery of interest under certain contracts insured, etc., by governmental agencies.— A. No person shall, by way of defense or otherwise, avail himself of any of the provisions of

this chapter or any other law relating to usury or any statute or rule of case law relating to compounding of interest to avoid or defeat the payment of any interest or any other sum which he has contracted to pay on any loan:

1. Insured by the Federal Housing Administration, pursuant to the provisions of the National Housing Act;

2. Guaranteed by the Veterans Administration, pursuant to Title 38 of the United States Code; or

3. Insured or guaranteed by any similar federal governmental agency or organization, or made directly or indirectly by the Virginia Housing Development Authority pursuant to the provisions of Chapter 1.2 (§ 36-55.24 et seq.) of Title 36.

B. Nothing contained in this chapter shall be construed to prevent the recovery of such interest or fee from any person who has contracted to pay the same in connection with any loan described in this section.

Article 10.

Exceptions to Contract Rate of Interest;

Commercial Transactions.

§ 6.1-330.75. Defense of usury not applicable to certain business loans.—A. No person shall, by way of defense or otherwise, avail himself of the provisions of this chapter, or any other section or case law relating to usury or compounding of interest to avoid or defeat the payment of interest, or any other sum, in connection with a loan made to a person or entity for business or investment purposes, provided the initial amount of the loan is $5,000 or more.

B. For the purposes of this section, unless a loan is for family, household, or personal purposes which shall not include a passive or active investment, it shall be deemed to be for business or investment purposes.

§ 6.1-330.76. Corporations, partnerships, professional associations, real estate investment trusts and certain joint ventures not allowed to plead usury.—No corporation, partnership which is or was required to file a certificate pursuant to Chapter 2 (§ 50-44 et seq.), Chapter 2.1 (§ 50-73.1 et seq.) or Chapter 3 (§ 50-74 et seq.) of Title 50 or which is formed under laws other than those of this Commonwealth, professional association, or real estate investment trust, or joint venture organized for the purpose of holding, developing and managing real estate for profit, shall, by way of defense or otherwise, avail itself of any of the provisions of this chapter or any other section or case law relating to usury or compounding of interest to avoid or defeat the payment of any interest or any other sum which it has contracted to pay. Nothing contained in any of such sections shall be construed to prevent the recovery of such interest or any other sum, though it be more than contract rate of interest and though that fact appears on the face of the contract.

Article 11.

Exceptions to Contract Rate of Interest;

Certain Consumer Transactions.

§ 6.1-330.77. Charges by sellers and lessors of consumer goods; certain premiums not construed as additional charges; penalty for violations of section.—A. Any seller of consumer goods as defined in § 8.9-109 who extends credit under a closed-end installment credit plan or arrangement may impose finance charges at such rate or rates as may be agreed upon by the seller and the purchaser. Deferrals and extensions of the time for payment, if allowed by the seller or his assignee, may be subject to a finance charge, if agreed to in the original contract or at the time of the renewal or extension. No additional finance charge shall be made for the extension of credit under such a plan or arrangement. If the total finance charge on the transaction is precomputed according to the actuarial method, the finance charge shall be calculated on the assumption that all scheduled payments will be made when due. The balance on which such finance charge may be imposed may include the deferred portion of the sales price of the consumer goods and costs and charges incidental to the transaction, including any insurance premium financed in connection therewith. The debtor shall have the right to prepay in

full on precomputed transactions and receive a rebate determined in accordance with the Rule of 78, as illustrated in § 6.1-330.86, or other method elected by the seller under which the finance charge imposed does not exceed the amount that results from application of the Rule of 78. The seller may also condition such rebate upon receiving a minimum of twenty-five dollars in finance charges. This amount, to the extent not earned, may be withheld from the rebate required hereunder. A late charge pursuant to § 6.1-330.80 may be imposed.

B. 1. Any lessor of consumer goods as defined in § 8.9-109 may impose a finance charge not exceeding two percent per month on the balance at the end of the month next preceding each successive payment provided:

a. That the lease agreement is in the form of a bailment or lease of such goods;

b. It is stated in the lease that the lessee will become or has the option to become the owner of such goods for no other consideration or for nominal consideration if he fully complies with his obligations; and

c. The lessor extends credit under a closed-end installment credit plan or arrangement.

2. No additional charge, other than a late charge under § 6.1-330.80, may be imposed for the extension of credit under such lease.

C. Premiums for credit life insurance and credit accident and health insurance purchased by the debtor are not to be construed as an additional charge for the extension of credit if such insurance coverage is purchased voluntarily by the debtor. Premiums for property insurance on the goods purchased or leased are not to be construed as additional charges for extension of credit unless the seller or lessor requires the purchase of such insurance from or through the seller or lessor.

D. Where a finance charge is imposed by any lessor in excess of that permitted by this section, the provisions relating to usury set forth in §§ 6.1-330.56 and 6.1-330.57 shall apply.

§ 6.1-330.78. Open-end sales and loan plans.—A. Any seller or lender engaged in the extension of credit under an open-end credit or similar plan under which a finance charge is imposed upon the cardholder or consumer, if payment in full of the unpaid balance is not received at the place designated by the creditor prior to the next billing date (which shall be at least twenty-five days later than the prior billing date), may impose finance charges at such rate as may be agreed upon by the seller or lender and the cardholder or consumer. Such rate may be applied at the option of the seller or lender, to:

a. The average daily balance for the period ending on the billing date;

b. The balance existing on the billing date of the month; or

c. Any other balance which does not result in the seller or lender charging or receiving finance charges in excess of those which would be charged or received under subdivision a or b of this subsection. .

2. No finance charge shall be imposed unless the bill is mailed not later than eight days (excluding Saturdays, Sundays and holidays) after the billing date, except that such time limitation shall not apply in any case where the seller or lender has been prevented, delayed, or hindered in mailing or delivering the bill within such time period because of an act of God, war, civil disorder, natural disaster, strike, or other excusable or justifiable cause.

3. Notwithstanding the provisions of this section, a seller or lender may charge and collect a minimum finance charge of one-half dollar per month; however, no finance charge shall be charged against a zero balance.

4. For the purposes of this section the average daily balance for any billing period shall be that amount which is the sum of the actual amounts outstanding each day during the period, divided by the number of days in the period.

B. Notwithstanding the provisions of § 6.1-330.71 and subject to the provisions of § 8.9-204.1, any loan made under this section may be secured in whole or in part by a subordinate mortgage or deed of trust on residential real estate improved by the construction thereon of housing consisting of one to four family dwelling units.

C. Unless the contract of indebtedness provides that the rate of finance charge shall vary in accordance with an exterior standard, no increase in finance charge rate shall take effect unless at least thirty days prior to the effective date of such increase a written notice of the increase has been mailed or otherwise delivered to the cardholder or consumer explaining that the making of additional charges under the plan on or after the effective date of the increase shall be deemed to constitute acceptance of such higher charge on existing balances and any subsequent extension of credit under the plan.

§ 6.1-330.79. Compliance with federal law.—Every person subject to the provisions of 15 USC 1601 et seq. and Regulation Z, Truth-in-Lending, promulgated by the Board of Governors of the Federal Reserve System shall comply with such statutes and regulations when offering or extending consumer credit as defined therein. A lender who fails to comply with this section shall not be subject to any liability or penalty beyond those imposed by such federal statutes and regulations.

Article 12.

Late Charges; Prepayment and Acceleration Laws;
Certain Rights of Borrowers and Consumers.

§ 6.1-330.80. Amount of late charge; when charge can be made.—A. Any lender or seller may impose a late charge for failure to make timely payment of any installment due on a debt, whether installment or single maturity, provided that such late charge does not exceed five percent of the amount of such installment payment and that the charge is specified in the contract between the lender or seller and the debtor. For the purposes of this section, "timely payment" is defined as one made by the date fixed for payment or within a period of seven calendar days after such due date. Late charges shall not be deemed to include charges imposed upon acceleration of the entire debt or to include costs of collection and attorney's fees as otherwise permitted by law by reason of a default by the debtor.

B. If any federal governmental agency or organization shall adopt any rules or regulations dealing with the application of late penalties as to loans insured or guaranteed by such federal agency or organization, then such rules and regulations shall control as to such loans insured or guaranteed by them.

C. Any provision for late charges in excess of the amount permitted by this section shall be void as to such excess but shall not otherwise affect the validity of the obligation.

§ 6.1-330.81. Certain contracts to permit prepayment; amount of prepayment penalty.—A. Every loan contract, except as provided in subsection C of this section, secured by a first deed of trust or first mortgage on real estate, where the principal amount of the loan is less than $75,000, shall permit the prepayment of the unpaid principal at any time and no penalty in excess of 1% of the unpaid principal balance shall be allowed.

B. Any prepayment penalty provision in violation of this section shall be unenforceable as to the amount in excess of one percent of such balance.

C. The provisions of this section shall not apply to secured or unsecured notes evidencing installment sales contracts. The provisions of this section relating to prepayment penalty shall not apply to loan contracts subject to § 6.1-330.83 or § 6.1-330.84 or to loan contracts governmentally regulated as to prepayment privilege.

§ 6.1-330.82. Property owner entitled to written statement of payoff amount.—A. Where a lien on real estate is secured by a deed of trust or mortgage, the owner of such real estate, if entitled to prepay the obligation secured by such deed of trust or mortgage, shall be entitled to receive from the bank, savings institution or other corporate entity holding such obligation, a written statement setting forth the total amount to be paid as of a particular date in order to obtain a release of the deed of trust or mortgage. The holder of the obligation secured by said deed of trust or mortgage shall mail or deliver such written statement of the payoff amount to the property owner or his designee within ten business days of the receipt of a written request for such payoff information from the property owner or his designee if the request contains the loan number and the address or other description of the location of the subject premises. Upon payment in full of the

obligation, the holder shall promptly cause the cancelled loan documents to be forwarded to the owner or his designee. An inadvertent error made in the calculation of the payoff amount shall not release the party liable for payment of the obligation from the requirement to pay the full amount due under the contract of indebtedness, nor shall it release the holder of the contract of indebtedness from the requirement to return any overpayment to such party or his designee.

B. A request for payoff information under this section may be made one time within a twelve-month period without charge, and a fee not exceeding fifteen dollars may be charged for each additional request made within such period.

§ 6.1-330.83. Prepayment penalty for loan secured by home occupied by borrower.– The prepayment penalty in the case of a loan secured by a mortgage or deed of trust on a home which is occupied or to be occupied in whole or in part by a borrower shall not be in excess of two percent of the amount of such prepayment.

§ 6.1-330.84. Prepayment by borrower from industrial loan association; rebates for unearned interest; prepayment penalty.–Any natural person borrowing from an industrial loan association shall have the right to anticipate payment of his debt at any time. In cases where interest has been added to the face amount of the note, such person shall have the right to receive a rebate by way of credit for any unearned interest, which rebate shall be computed in accordance with the Rule of 78 as illustrated in § 6.1-330.86 or by using any other method that is at least as favorable to such borrower. In addition, the industrial loan association may charge a prepayment penalty not to exceed two percent of the amount of the prepayment, provided such prepayment penalty, including the percent thereof, is set forth in the contract of indebtedness and is disclosed to the borrower pursuant to the federal interest disclosure laws.

§ 6.1-330.85. Prepayment of loan described in § 6.1-330.71; rebates for unearned interest.–A. Any borrower under any loan described in § 6.1-330.71 shall have the right to anticipate payment of his debt in whole or in part at any time without penalty. In cases where interest has been added to the face amount of a note payable in installments, the borrower shall have the right to a rebate of any unearned interest, which rebate shall be computed in accordance with the Rule of 78 as illustrated in § 6.1-330.86.

B. The provisions of this section shall not apply to any loan made by any lender enumerated in § 6.1-330.73.

§ 6.1-330.86. The Rule of 78.–A. The Rule of 78 is so named because the months of one year, i.e., one through twelve added together, total seventy-eight.

B. To determine the amount of the rebate of unearned interest under the Rule of 78 on a loan where payment is anticipated:

1. Determine the number of months over which the loan is to be repaid according to its terms. Write the numbers in sequence and add (for example, for a four-year loan write the numbers one through forty-eight). The total will be the denominator of a fraction to be determined below.

2. Determine the number of months remaining on the loan after payment is anticipated. Write in inverse sequence and add (for example, for a four-year loan anticipated after the third month, write the numbers forty-five back to one). The total will be the numerator of the fraction of which subdivision 1 of this subsection is the denominator.

3. Multiply the original amount of interest that would have been paid over the life of the loan by the fraction derived in subdivisions 1 and 2 of this subsection. Such figure, so determined, is the amount to be rebated.

C. Payment anticipated between scheduled payment dates shall not be considered but instead the succeeding scheduled payment date shall be used in determining the rebate under subsection B of this section.

§ 6.1-330.87. Prepayment penalties not to be collected in certain circumstances.–No lender shall collect or receive any prepayment penalty on loans secured by real property comprised of one to four family residential dwelling units, if the prepayment results from

the enforcement of the right to call the loan upon the sale of the real property which secures the loan. If the loan is prepaid because of sale to a person whom the lender has refused to approve for purposes of assuming the loan or failed to approve within fifteen days after receipt by it of written request for approval, such prepayment shall be presumed to result from enforcement of the right to call the loan.

§ 6.1-330.88. Mortgage, etc., to contain notice that debt is subject to call or modification on conveyance of property.–Where any loan is made secured by a mortgage or deed of trust on real property comprised of one to four family residential dwelling units, and the note, or mortgage or deed of trust evidencing such loan contains a provision that the holder of the note secured by such mortgage or deed of trust may accelerate payment of or renegotiate the terms of such loan upon sale or conveyance of the security property or part thereof, then the mortgage or deed of trust shall contain in the body or on the margin thereof a statement, either in capital letters or underlined, which will advise the borrower as follows: "Notice –The debt secured hereby is subject to call in full or the terms thereof being modified in the event of sale or conveyance of the property conveyed."

§ 6.1-330.89. Acceleration clause in note evidencing installment loan; effect of acceleration.–Any note evidencing an installment loan with add-on interest may provide that the entire unpaid loan balance, at the option of the holder, shall become due and payable upon default in payment of any installment without impairing the negotiability of the note, if otherwise negotiable. Upon such acceleration, the holder of the contract of indebtedness shall not be entitled to judgment for unearned interest, but the balance owing shall be computed as if the borrower had made a voluntary prepayment and obtained as of the date of acceleration an interest credit based upon the Rule of 78 as defined in § 6.1-330.86. Such accelerated balance shall bear interest at the rate shown, or which should have been shown if a consumer credit transaction were involved, as the annual percentage rate under a truth-in-lending disclosure pursuant to federal law.

§ 6.1-330.90. Right of buyer of consumer goods to refinance certain payments; agreements as to fluctuation in schedule of payments.–A. In any sales transaction, except one pursuant to an open-end account, involving exclusively consumer goods as defined in subdivision (1) of § 8.9-109 wherein credit is extended and a security interest in consumer goods is taken, any installment payment, other than a down payment made prior to or contemporaneously with the execution of an agreement evidencing the transaction, which is more than ten percent greater than the regular or recurring installment payments, shall be subject to the buyer's right to refinance such a payment on the basis of an extended period of time. Such additional payments shall be in amounts which shall allow the unpaid balance to be paid in as few periodic payments, not more than ten percent greater than the regularly scheduled installment payments, as are required to pay such balance. Such additional payments shall be considered and treated as part of the original transaction.

B. The parties may agree in a separate writing that one or more payments or the intervals between one or more payments shall be reduced or expanded in accordance with the desires or needs of the buyer, if such fluctuations in the schedule of payments are expressly arranged to coincide with the anticipated fluctuations in the buyer's capability to make such payments.

C. No seller who has refused to refinance in compliance with the provisions of this section shall be entitled (i) to return or repossession of the goods involved in the transaction or (ii) to a judgment for the unpaid balance involved in the transaction at the time of his failure to do so.

2. That §§ 6.1-330.6 through 6.1-330.46 and 6.1-330.47:1 of the Code of Virginia are repealed.

3. That the provisions of §§ 6.1-330.47 and 6.1-330.48 of the Code of Virginia shall continue to apply, and apply only to loans secured by subordinate deeds of trust or mortgages closed prior to July 1, 1986. For the purposes of this act, a loan shall be

deemed closed upon the original recordation of the deed of trust or mortgage securing such loan.

Official Use By Clerks

Passed By The House of Delegates		Passed By The Senate	
without amendment	☐	without amendment	☐
with amendment	☐	with amendment	☐
substitute	☐	substitute	☐
substitute w/amdt	☐	substitute w/amdt	☐

Date: ____________ Date: ____________

Clerk of the House of Delegates Clerk of the Senate

SECTION I

SCOPE OF STUDY

OBJECTIVE

A general lack of knowledge exists on the part of the public about the costs retail stores incur to provide customers with credit services. A national study to determine these costs and the finance charge revenues was performed in 1963 and updated in 1968. It was with this background that, in the fall of 1985, the National Retail Merchants Association engaged Touche Ross to undertake a detailed study based on 1984 results (the latest available at the commencement of this study), with the counsel of NRMA's Accounting Principles and Credit Management Committees. Since the 1985 results have recently become available, this report, therefore, also comments on the impact of the two most volatile variable costs - interest and bad debt expense. As well, a comparison between 1984 and 1985 interest rates and bad debt expense is provided. The principal purpose of this Study was to determine whether retailers' finance charge revenues were sufficient to cover the costs of providing the necessary services associated with the extension of credit.

The breadth of the 1984 Study includes 20 retailers representing $38.9 billion of credit sales and $66.4 billion of total retail sales. The total retail sales represented approximately 51% of total sales for all department stores in the United States in 1984 as cited in the Statistical Abstracts of the United States, published by the U.S. Department of Commerce, Bureau of the Census, December 1985.

APPROACH

Number of Companies and Accounting Period

Retailers from various geographic locations and of varying sizes have been selected to participate in the 1984 Study. They include a combination of large and small retailers with annual credit sales ranging from $4.9 million to several billion dollars. Each of these retailers provided detailed data for its fiscal year ended January 1985 or July 1984 (both defined as fiscal 1984). The retailers also provided fiscal 1985 data for interest and bad debt expenses. This data allowed Touche Ross to compare the 1984 Study results with the retailers' most recent experiences. The retailers participating in the 1984 Study include most of the nation's largest chains as well as smaller independents. Many of the larger retailers operate numerous divisions with more than one credit function. Data collection for these retailers was completed on a composite basis; one set of data was collected for each retailer's total credit activity regardless of the number of divisions within the company.

Finance Charge Revenues and Credit Costs Analysis

In order to complete the study questionnaire mailed to each retailer, the companies identified those operating costs from internal accounting records that were incurred to provide services to credit customers using their proprietary cards, as distinguished from services available to all customers. These proprietary credit costs were found by each company after identifying those costs that could be eliminated if the store credit function were discontinued and if there were no change in total sales volume.

The participants were asked to identify their credit sales, finance charge revenues and credit costs by type of account: 30-day, revolving and installment. The Study results show that credit sales using 30-day accounts represent only 1.4% of total credit sales, and installment sales represent only 1.7% of total credit sales reported. In 1984, revolving accounts represented 96.9% of total credit sales. Since the amounts of 30-day and installment account sales were not significant in 1984, only a single set of revenue and cost figures is shown for all retail credit activity.

In addition to the finance charge revenues and credit costs associated with providing credit services, a number of statistics related to credit operations for fiscal 1984 were provided by the participating retailers.

Finance Charge Revenues

Retailers receive revenue for providing credit services in the form of monthly finance charges. These charges are based on the amount owed by the customer to the retailer. Finance charge revenue for the 1984 Study participants totaled $4.1 billion in 1984. Revolving account finance charge revenue represented 98.7% of total finance charge revenue. Credit account terms and finance charge rates vary by retailer and by state. The typical account, however, provides for no finance charge revenue if an account is fully paid within the current billing period. Therefore, even though nominal finance charge rates are generally higher, the effective finance charge rate (finance charge revenue divided by average accounts receivable) was 16.0% in 1984.

Credit Cost Categories

In this report, cost data corresponding to five major categories have been furnished by all participating retailers.

The first cost grouping, Account Processing Costs, represents those costs directly identifiable with the credit operation. They include new account costs, account servicing costs, and account collection costs. They depict the costs of obtaining and processing new customer accounts, the costs of the day-to-day servicing of active customer accounts, and the costs of the collection effort required on accounts with payments in arrears. Only out-of-pocket costs (costs that could be eliminated if the credit function were discontinued) have been included in these three categories.

The second category, Bad Debt Expense, includes both bad debts on accounts receivable and fraudulent credit purchases.

The third cost category is Data Processing Personnel, Systems and Equipment. This category includes that portion of data processing costs associated with the operation of the credit function.

The fourth cost category covers "Other Costs"; this includes in-store credit costs associated with providing in-store credit services, credit space costs, and that portion of general management expense that is assignable to the credit operation. In-store credit costs include the portion of total in-store costs that should be allocated to the credit function. Credit space costs include all space utilized by the credit, collection, accounts receivable, and other back office departments, as well as in-store space costs. These costs are included because space used for credit activities would be available for alternative store use if credit services were discontinued. Management costs represent the costs of services provided to the credit departments by senior level managers and by various other service activities within the store. It is reasonable to assume that if the credit function was eliminated and the services were no longer required, the departments performing these services would be able to eliminate the cost related thereto or to provide additional services to other departments.

The fifth cost category is the Cost of Financing the Investment in Accounts Receivable. Businesses are financed through a combination of debt and equity. Therefore, it is appropriate to assume that each asset is financed partially by debt and partially by equity. The 1968 Study, which received wide acceptance, recognized that the accounting model used to reflect credit costs did not represent the true total cost of credit operations, since the accounting model calculated the cost of financing the accounts receivable investment based solely on the assumption of debt financing. The 1984 Study presents the true economic cost associated with financing the accounts receivable investment by utilizing a representative industry average blended debt and equity rate. This method was developed in conjunction with the NRMA's Accounting Principles and Credit Management Committees. The Study also shows, as supplemental information, the relationship of credit costs to revenues, utilizing a representative debt-related industry rate for the cost of financing the accounts receivable investment.

To determine the rate to be used to calculate the cost of financing the retailer's average investment in accounts receivable, an industry study was performed to ascertain the percentage of financing by debt and equity as well as the rates to be assigned to the two financing sources. The ratio of debt and equity based on a representative industry average was 41.8% debt and 58.2% equity. An average interest rate for all debt for this representative industry sample was determined - this debt rate was 11.2%. This blended debt rate was determined by using an average of short-term and long-term debt and their respective interest rates. Short-term debt made up 17.9% of total debt, with an average 14.2% interest rate, while long-term debt made up the remaining 82.1% of total debt, with a 10.5% average interest rate.

The cost of equity rate is generally recognized as the investor's expected return on equity investment, defined for purposes of this study as the current dividend divided by market price, plus anticipated dividend growth. This rate was calculated for the representative industry sample and applied to the results for the study participants. The rate used was 15.0%. A blend of debt and equity rates in proportion to the average industry debt-equity ratio was used as the rate applicable to the study participants' average investment in customer accounts receivable, less the average deferred taxes applicable to installment sales accounting for tax purposes. This blended rate of 13.4% was used in the 1984 Study.

To provide simply an accounting presentation of the total credit costs, rather than the true economic costs, an alternative computation displays total credit costs using the 11.2% debt rate for financing the total accounts receivable investment.

In this type of analysis it is difficult to capture all costs associated with providing credit services. In addition to those costs specifically identified in the five categories, there are some costs that, although not readily susceptible to specific measurement, are incurred with the existence of the credit function. No data has been provided for these costs in this report.

SECTION III

STUDY FINDINGS AND CONCLUSIONS

The principal purpose of this Study was to determine whether retailers' finance charge revenues are sufficient to cover the costs of providing the necessary services associated with the extension of credit. Th 1984 Study indicated that total credit costs for the retailers studied exceed finance charge revenues.

Sales Activity - (Exhibit I)

As shown in Exhibit I, the 20 retailers included in this Study had total sales in 1984 of $66.4 billion. Of these sales 58.5%, or $38.9 billion, involved extensions of credit by the retailer. Revolving credit accounts mad up 96.9% or $37.6 billion of this total. Cash sales represented 36.3% of tota sales and third-party credit (bank and travel and entertainment cards) represented 5.2%.

Finance Charge Revenues and Credit Costs - (Exhibit II)

Exhibit II illustrates total finance charge revenues and costs. For the 20 stores in the sample, the costs of extending credit exceeded finance charge revenues by approximately $603 million. Even if the cost of capital t finance the accounts receivable investment was assumed to be 11.2% (the debt-related rate), the aggregate deficiency of revenues over costs was still $118 million. All deficiencies of revenues over costs indicated are on a e-tax basis.

Finance Charge Revenues and Credits Costs: Percentage Analysis - (Exhibit III)

The following highlights have been drawn from Exhibit III:

	Percent of Credit Sales	Percent of Finance Charge Revenues	Percent of Average Accounts Receivable	Dolla per Activ Accou
Finance charge revenues	10.6%	100.0%	16.0%	$45.9
Total Credit Costs - cost of financing accounts receivable at blended cost of capital rate of 13.4%	12.2%	114.6%	18.4%	$52.6
Deficiency of finance charge revenues over credit costs - cost of financing accounts receivable at blended cost of capital rate of 13.4%	(1.6%)	(14.6%)	(2.4%)	$(6.7
Deficiency of finance charge revenues over credit costs - cost of financing accounts receivable at blended debt rate of 11.2%	(0.3%)	(2.9%)	(0.5%)	$(1.3

The 1984 Study shows that, similar to 1968, the cost of providing credit services exceeds finance charge revenues. As a percentage of finance charge revenue, for the 20 stores in the sample, the costs of extending credit exceeded finance charge revenues by 14.6%. On a per active account basis, there is a deficiency of $6.72.

Exhibit III also indicates the costs of providing credit services as a percent of credit sales, finance charge revenues and average accounts receivable. Total credit costs accounted for 12.2% of credit sales, 114.6% of finance charge revenue and, on a per active account basis, it cost the retailers $52.64 in 1984 to provide credit services. Credit costs before the cost to finance the investment in accounts receivable in 1984 were 6.9% of average accounts receivable.

Account Processing Costs - (Exhibit IV)

Exhibit IV illustrates additional detail of account processing costs. Account processing costs are broken down into new account costs, account servicing costs and account collection costs. Some retailers were unable to provide the breakdown by major expense category; this portion of total account processing costs was included as nonallocated costs.

Account Processing Costs:
Percentage Analysis - (Exhibit V)

In Exhibit V, account processing costs are illustrated as a percent of credit sales, finance charge revenues, average accounts receivable and on a dollar per account basis.

Supplementary Statistics - (Exhibit VI)

Exhibit VI provides a number of supplementary statistics. These include the amount of the average cash and credit sale, new account approval rates, average individual customer account balance, bad debt recovery rates, and the turnover of accounts receivable.

Summary 1985 Results

After examining fiscal 1985 results for interest and bad debt expenses for the companies included in the industry study to determine the blended cost of capital rate, we have found that interest rates for total debt have dropped by .3%, from 11.2% in 1984 to 10.9% in 1985. Even though short-term interest rates dropped significantly from 1984 to 1985, the blended rate for total debt was not reduced in the same proportion, since the study participants' total debt structure included approximately 82% of long-term debt.

Bad debt expense increased by 31.9% in 1985 as compared to 1984. The primary cause for such a large increase was the higher bankruptcy experience in 1985.

If the 1985 experience for these two variables were substituted for the 1984 figures, the deficiency of revenues over cost would be increased by $108 million (to the nearest million).

SALES ACTIVITY

ALL STORES

(Dollars in thousands)

	$	%
NET SALES BY TYPE:		
Cash	$24,073,690	36.3%
Store credit:		
30-day	547,180	.8
Revolving	37,636,278	56.7
Installment	672,897	1.0
Total	38,856,355	58.5
Third-party credit:		
Bank card	2,368,048	3.6
T&E card	1,084,978	1.6
Total	3,453,026	5.2
TOTAL NET SALES	$66,383,071	100.0%

Exhibit II

FINANCE CHARGE REVENUES AND CREDIT COSTS

ALL STORES

(Dollars in thousands)

Net credit sales	$38,856,355
Finance charge revenues	$ 4,124,020
Credit costs:	
Account processing costs	923,773
Bad debt expense	476,245
Data processing personnel, systems and equipment	129,039
Other costs	240,557
Cost of financing accounts receivable - 13.4% blended cost of capital rate*	2,957,531
Total credit costs	4,727,145
(Deficiency) of revenues over costs	$(603,125)

Cost of financing accounts receivable - 11.2% debt rate*:	
(Deficiency) of revenues over costs	$ (117,561)

*Calculated industry average rate used for all stores. Industry average rate applied to average accounts receivable investment for study participants, less average deferred taxes applicable to installment sales accounting for tax purposes.

Exhibit III

FINANCE CHARGE REVENUES AND CREDIT COSTS - PERCENTAGE ANALYSIS

ALL STORES

	Percent of Credit Sales	Percent of Finance Charge Revenues	Percent of Average Accounts Receivable	Dollars per Active Account
Net credit sales	100.0%		150.8%	$432.70
Finance charge revenues	10.6	100.0%	16.0%	45.92
Credit costs:				
Account processing costs	2.4	22.4	3.6	10.29
Bad debt expense	1.2	11.5	1.9	5.30
Data processing personnel, systems and equipment	.3	3.1	.5	1.44
Other costs	.6	5.8	.9	2.68
Cost of financing accounts receivable - 13.4% blended cost of capital rate*	7.7	71.8	11.5	32.93
Total credit costs	12.2	114.6	18.4	52.64
(Deficiency) of revenues over costs	(1.6%)	(14.6%)	(2.4%)	$ (6.72)
Cost of financing accounts receivable - 11.2% debt rate*:				
(Deficiency) of revenues over costs	(.3%)	(2.9%)	(.5%)	$ (1.31)
Average accounts receivable (dollars in millions)			25,751	
Number of active accounts (in thousands)				89,800

*Calculated industry average rate used for all stores. Industry average rate applied to average accounts receivable investment for study participants, less average deferred taxes applicable to installment sales accounting for tax purposes.

Exhibit IV

ACCOUNT PROCESSING COSTS

ALL STORES

(Dollars in thousands)

New account costs:	
Salaries	$ 58,698
Credit investigation	41,634
Promotion	34,628
Other	50,082
Total new account costs	185,042
Account servicing costs:	
Salaries	126,151
Postage	138,980
Other	71,153
Total account servicing costs	336,284
Account collection costs:	
Salaries	157,852
Collection agencies	42,805
Other	88,271
Total account collection costs	288,928
Nonallocated costs	113,519
Account processing costs	$923,773

Exhibit V

ACCOUNT PROCESSING COSTS - PERCENTAGE ANALYSIS

ALL STORES

	Percent of Credit Sales	Percent of Finance Charge Revenues	Percent of Average Accounts Receivable	Dollars per Active Account
New account costs:				
Salaries	0.15%	1.42%	0.23%	$ .65
Credit investigation	0.11	1.01	0.16	.46
Promotion	0.09	0.84	0.13	.39
Other	0.13	1.22	0.19	.56
Total new account costs	0.48	4.49	0.71	2.06
Account servicing costs:				
Salaries	0.32	3.06	0.49	1.40
Postage	0.36	3.37	0.54	1.55
Other	0.18	1.72	0.28	.79
Total account servicing costs	0.86	8.15	1.31	3.74
Account collection costs:				
Salaries	0.41	3.83	0.61	1.76
Collection agencies	0.11	1.04	0.17	.48
Other	0.23	2.14	0.34	.98
Total account collection costs	0.75	7.01	1.12	3.22
Nonallocated costs	0.29%	2.76	0.44	1.27
Account processing costs	2.38%	22.41%	3.58%	$10.29

SUPPLEMENTARY STATISTICS

ALL STORES

Average cash sale*	$ 22.30
Average store credit sale	$ 37.22
Average new account approval rate	59.4%
Average monthly balance of customer accounts receivable	$286.76
Number of months' write-offs in reserves	15
Average bad debt recovery rate	28.5%
Turnover of accounts receivable	1.5x

*Includes both cash and third-party credit transactions.

Statement By Paul Luttkus,

Vice President for Credit, Thalhimers, Inc.,
To Legislative Subcommittee Studying
Credit Card Rates and Practices
September 16, 1986

Good morning. My name is Paul Luttkus and I live and work in Richmond. I am Vice President in charge of the Credit Department for Thalhimers Department Stores. I have served in this position for 6 years and have been involved in the field of retail credit throughout my business career.

You have heard testimony this morning concerning an important study of the costs of retail credit recently completed by Touche, Ross & Company. Thalhimers was a participant in that study, supplying to Touche, Ross extensive data concerning our own credit operations, costs and experiences. I can say without qualification that the conclusion of that study--that retailers do not rake in profits from credit card plans--accurately reflects our experience as well as the entire retail credit industry in Virginia.

Historical Context

At the outset, I think it is important to put the concept of revolving credit and credit cards in their historical context. Revolving credit began in the retail industry. You may recall the open account or 30-day charge plan under which regular customers were permitted to "charge" their purchases, being billed at the end of the month for the total of their purchases during that month. Under these plans, customers were expected to pay their accounts in full within 30 days of that billing. Many retailers in Virginia continue to offer such plans. In our case, the vehicle for such charges is the plastic Thalhimers charge card.

In the late 1960s, the bank credit card plans such as VISA and MasterCard began to develop and the popularity of revolving credit and credit card plans began to take off. Today, two-thirds of all American families have at least one credit card. Although most of the attention has been on bank card plans, 57 percent of such families have retail cards as compared to 42 percent having at least one bank card.

Throughout the 1960s and most of the 70s, the prime rate of interest was below 10 percent. During that period, the typical credit card finance charge rate was 18 percent. Indeed, Virginia law at the time limited the finance charge rate to 18 percent. Beginning in 1979, the prime rate began a s eep climb, peaking at near 20 percent between 1981 and 1982. Nevertheless, retail credit card rates remained at the 18 percent maximum until the Virginia statutory ceiling was lifted in 1982. Today, the Thalhimers rate in Virginia is 21 percent APR. The prime rate has since declined, it is true, but still not to the lower levels of the 1960s and 1970s. This is significant, I think, as the spread between the prime rate and the credit card finance charge rate was actually greater in the 1960s and 1970s than it is today. Yet, there was no great outcry then that finance charge rates were too high.

Other Costs Have Risen

The reason credit card rates have not declined with the drop in the prime rate is that the cost of money is only part of the total cost of extending open-end credit. This is the main message of the Touche,Ross study. It is also the message of a study that was presented to Congress this summer by the staff of the Federal Reserve Board. That study, in response to federal legislative proposals to cap credit card finance card rates, fully confirms the Touche, Ross conclusions you have heard about this morning. Indeed, this summer the Comptroller of the Currency (Robert Clarke) testified to Congress that comparisons of credit card rates to rates on other loan plans are misleading because "funding costs are a much smaller share of the total cost of offering credit cards". American Banker, June 3, 1986, at 12.

Our own experience at Thalhimers bears this out. During 1985, our cost of funds represented less than half of our cost for extending open-end credit. Other cost factors have increased substantially since the 1970s: Postage is up 230 percent. We have also seen cost increases in supplies, purchase of services such as computer technology and communications, salaries,occupany, utilities and bad debt and collection expenses. Our bad debt losses have increased over the last two years. This is due in part to the threefold acceleration in consumer bankruptcy filings.

Why We Continue Our Credit Card Plan

The finance charge revenue produced on retail credit card plans does not carry or offset the cost of such plans. It does not for Thalhimers and it does not for retailers in general. So why do retailers continue to offer such plans? Our market surveys show beyond question that a customer with a Thalhimers charge card in his or her wallet is more likely to shop at one of our stores than a customer that does not have our card. Our charge card and the monthly billing statements related to it are a significant medium for our advertising. The charge plan also provides us a method for recognizing purchasing patterns and helping us to target market merchandise to various consumer groups in our trading areas. Without question , the Thalhimers credit card plan is good for our business, but not because of alleged profits derived from finance charge revenues.

The Effects of Finance Charge Ceilings

The reimposition of finance charge ceilings would not be good for us or our customers. The application of rate ceilings to credit plans is not unlike the experience of lying on a waterbed. As you press down on one side of the bed, the water being displaced has to go somewhere. It moves to another part of the bed and pops up where you are not applying pressure. Credit costs work the same way. By pushing down on finance charge revenues, something must give somewhere else to cover the cost of the credit plan. This may be in the tightening of credit standards, denying to all but the very best credit risks the convenience of credit card shopping. It may be in the imposition of certain types of fees which are not now typically charged by retail creditors. It may be in changes to the method of calculating balances to which finance charges are applied. Or, as an end result, it may be in the increase of merchandise prices in general, thus penalizing the cash paying customer as well as the credit buyer. The point is that the costs must be covered by some means. Anyone who pretends that restrictive finance charge ceilings will benefit consumers is engaging in misconceptions.

Competition and Customer Satisfaction

Since 1982 when finance charge ceilings were eliminated in Virginia, free and open competition has flourished in this State. Some card issuers charge 21 percent; others are at 18 percent; one Virginia bank I have heard about (Dominion in McLean) charges 10.5 percent to its better credit risk customers. There is competition as to how balances are calculated, with some creditors using an ending balance and others using the average daily balance. Some card plans offer additional services such as travel insurance, a lost card notification service and traveler's checks. Some plans offer rebates on the volume of purchases made. In short, the variety of competitive benefits offered on card plans today far exceeds the "standard sameness" in plans that existed 10 years ago when statutory rate ceilings were in effect.

In our experience, our customers understand and appreciate the benefits of the competition that exists in the marketplace today for credit card plans. When comparing the types and numbers of customer inquiries we receive at Thalhimers, very few complaints about our plan, either as to the finance charge rate or the manner in which we calculate the balance are recognized. Unfortunately, a few members of Congress and State Legislators appear determined to try and excite the public on this issue. However, I feel their basis for concern is unfounded or due to a misunderstanding of the dynamics of consumer credit.

I appreciate the opportunity to present these comments. Thank you for your consideration.

VIRGINIA BANKERS ASSOCIATION

Credit Card Rates

Summary

To legislate rates would restrict credit availability to the consumer, force many consumers who still want a card to even higher out-of-state rates, create an incentive for Virginia institutions to move their card operations out of state, adversely impacting jobs, tax base, and the economy. And, out-of-state institutions could still import decontrolled rates into Virginia. We would disadvantage our own state and award an advantage to out-of-state competition.

1. The credit card business is national in scope. Card issuers and card users are not restrained by geographic or political boundaries. It is a highly competitive business. Over 15,000 depository institutions, primarily banks, S&Ls, and credit unions, issue over 130 million cards. Retailers issue an estimated 350 million cards and gasoline companies another 113 million. And, new entrants continue to enter the market. (The Sears Discover Card, for example). Competition abounds. And, Virginia banks are on the cutting edge of that competition. Most out-of-state institutions are importing rates into Virginia in the 19-21% range. No Virginia bank is in excess of 18% on standard credit cards and none increased rates when the lid was lifted. And, some Virginia banks offer premium cards in the 11-12% range for which credit standards are more restrictive.

2. With other forms of credit, an individual pays interest on all funds extended to him. With card credit, a person pays no interest on the funds he uses if he pays his bill at the end of the billing cycle (the free period). Approximately one third of card holders do pay in full and have free use of funds for 30-60 days. As a result, the real rate of interest being earned by the bank on its total outstanding funds is actually in the 15% range.

3. For card operations to stay in business over the last couple of years, a major adjustment in rates had to occur. In the early 70's when the prime rate was 5.25%, card rates then were in the 18% range, resulting in a spread of 12-13% between the prime and card rates. By 1980, with the run up in rates, this spread had disappeared and the prime exceeded card rates by 1-2%. Had card rates gone up with other rates, one would expect them to now come down with other rates. But, card issuers did not increase rates when other rates were going up, and waited for the market correction which subsequently took place. The spread between the prime and card rates has now returned closer to the norm of the 1970's and is in the 8-9% range, but still lower than the 12-13% spread of the earlier 70's.

4. Credit card rates are of necessity higher than rates on other forms of credit that are most frequently secured, administratively simple, and largely driven by the cost of funds. The prime rate to which card credit is frequently compared, for example, is the rate banks charge their <u>best</u>, most <u>credit-worthy</u> customers for <u>secured</u> short-term credit. Card credit is unsecured, susceptible to difficult collection, bankruptcy losses, and a higher incident of fraud. It is administratively costly, requiring extensive computer networks and telecommunications, and large labor pools because of the necessity of accounting for purchases on a daily basis, providing the customer with an individual record of all his transactions, accepting slips from merchants as cash deposits even though they originate from various parts of the country, routing slips and tapes to banks of origin, etc.

And, all of these costly procedures are in place to handle individual credit balances that average less than $1000, compared to the larger amounts frequently associated with other forms of credit that are administratively less costly. In fact, according to a recent Federal Reserve "functional cost analysis" only 42% of the total cost of providing card credit consisted of cost of funds.

5. Because the cost of funds is less than half the total cost of card credit, it is also inappropriate to legislate a link between card rates and T-bills or other fund rates. Such an approach illogically ignores the other major cost factors uniquely associated with credit cards.

6. If rate controls are good for the consumer, card credit provided by banks in regulated states should have grown faster than in unregulated states. But, just the opposite has occurred because interest rate controls constrict the availability of credit to the consumer. In states with no controls, card credit grew 14% as a portion of national revolving bank credit from 1980-84, while credit in moderate control states fell 20% and credit from strict control states fell 14%. It is particularly interesting to note that Arkansas, the state with a rate cap closely parallelling that proposed in H.B. 803, has experienced a 41% decline in bank card credit as a percent of national revolving credit. Two factors caused this result. One, with lower rates, banks impose stricter criteria for qualifying for a card, and two, the fact that banks tend to move their card operations to states where controls do not exist since they can export decontrolled rates to other states. The fact that a Virginia imposed rate ceiling would not apply to out-of-state banks is critical. Card holders that are not in the upper income brackets that now hold 18% Virginia bank cards could not qualify for a card at the mandated lower rate and would be forced to even higher out-of-state rates to obtain a credit card.

7. It would be very unfortunate if Virginia placed her own card banks, and the employees who earn a $21 million dollar payroll at a competitive disadvantage with out-of-state banks that could still import a decontrolled rate into Virginia. As already noted, noncontrol states like Virginia, have obtained much of their growth in card operations at the expense of the control states. It is clear that more than credit availability is at stake. An incentive to move card operations out of Virginia would be created by controls, adversely impacting jobs, tax base, and the economy generally. To know that this is a real and not an imaginary concern one only has to look at the number of banks that have moved their card operations to Delaware and other free states. All but two card issuers in Maryland have moved to Delaware, for example. Seventeen out-of-state card operations have either already moved to Delaware or are in the process of doing so. While Virginia was a bit late in joining the effort to attract out-of-state card operations, we have held all that we had and attracted one Kentucky bank.

8. With card credit, the consumer has the final vote. He does not have to choose to use a card to function in our economy. If he does, he can choose to pay in full at the end of each billing cycle and avoid all interest charges. Only if he chooses, does he activate the credit feature of the card and the convenience it provides. Based on the growth in the number of card holders, I believe the consumer has already voted that the cost of the card is reasonable in relationship to the service it provides. I do not believe, then, that it is necessary for the legislature to displace the vote the consumer is casting each day in the marketplace.

BANKS THAT HAVE MOVED OR ARE MOVING BANK CARD OPERATIONS TO DELAWARE:

Maryland

Equitable Bank
First National Bank of Maryland
Maryland National Bank
Suburban Bank
(only two banks left in Maryland)

New York

Bank of New York
Chase Manhattan Bank
Marine Midland Bank

Pennsylvania

Core State Bank
Provident National Bank

Texas

M Bank
Republic Bank (in process)
Texas Commerce Bank (in process)
Interfirst Corporation (in process)
Texas American Bankshares (pending)

Michigan

National Bank of Detroit
Manufacturers National Bank (pending)

Arkansas

Union Bank of Arkansas (pending)

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Table 3

GROWTH IN BANK REVOLVING CREDIT, BY STATE GROUPS, 1980-1984

	Real Growth, 1980-84	Share of U.S. Revolving Credit 1980	1984	% Change
States with No Interest Rate Controls	83.5%	54.9%	62.5%	13.8%
States with Moderate Interest Rate Controls	30.5%	21.5%	17.3%	-19.5%
States with Strict Interest Rate Controls	39.7%	23.6%	20.2%	-14.4%
(Arkansas	-4.8%	.17%	.10%	-41.2%)
All States	62.7%	100.0%	100.0%	

Source: Federal Reserve Board, Consumer Price Index, and The AECS Review No. 247-48 (June-July 1985) 18-19 (Table 6).

Note: "No control" states are AZ, CA, DE, IL, MT, NH, NJ, NM, NV, NY, OR, SC, SD, VA.

"Moderate control" states are AL, CO, DC, IA, ID, IN, KS, KY, MA, MD, ME, MS, OH, OK, RI, TN, TX, WI, WY.

"Strict control" states are AK, AR, CT, FL, GA, HI, LA, MI, MN, MO, NC, ND, NE, PA, UT, VT, WA, WV.

Breakdown is as of August 1982. Subsequently, three additional states (IA, ID, and NE) abolished rate controls on credit cards and one additional state (UT) relaxed its controls from 18 percent to a higher ceiling.

Table 4

GROWTH IN VISA CARD CREDIT, BY STATE SHARES, 1980-1985

	Real Growth, 1980-85(2dQ)	Share of U.S. Revolving Credit 1980	1985	% Change
States with No Interest Rate Controls	135.0%	57.3%	62.0%	13.4%
States with Moderate Interest Rate Controls	81.8%	19.7%	17.3%	-12.2%
States with Strict Interest Rate Controls	58.4%	23.0%	17.7%	-23.0%
(Arkansas	11.3%	.23%	.10%	-47.8%)
All States	106.5%	100.0 %	100.0 %	

Source: Visa U.S.A. and Consumer Price Index.

Note: State breakdown same as on Table 3.

Texas American Joins Credit Card Flight to Delaware

By MICHAEL WEINSTEIN

NEW YORK — Texas American Bancshares Inc., Fort Worth, has announced that it is moving its credit card operation to Delaware, joining other banking companies that have fled Texas' restrictions on credit card interest rates and fees.

Texas American, with $6.2 billion in assets and about 150,000 credit card accounts, also revealed that it expects its new consumer credit bank to be operational by the spring.

"Texas laws unrealistically limit interest charges and also prohibit the charging of fees," said Lewis H. Bond, chairman of Texas American.

Texas law limits credit card interest rates using a formula based on the six-month T-bill rate. The maximum allowable rate in Texas is now a bit over 14.4%, while most banks charge 18% to 20% on credit card balances.

Also, Texas law prohibits annual fees and other charges, such as late-payment fees. Most banks charge annual fees of $15 to $20 for their standard credit cards.

"These restrictions inhibit our ability to provide enhanced services to our customers and to compete effectively with out-of-state card issuers," Mr. Bond said in a statement.

Texas American will consolidate its existing card operations — scattered among its 33 member banks — in its

➜ Texas: Page 15

Texas . . .

Continued from Page 9

new Delaware bank. The bank also plans to add new services to its standard MasterCard and Visa cards, and to begin offering premium MasterCard and Visa cards, said Paul A. Clinkscales, senior vice president at Texas American Bank Fort Worth, the company's lead bank.

He declined to say what the bank will charge for its Delaware-issued cards.

Mr. Clinkscales said the new rate will be somewhere between Texas American's existing rate, about 14.4%, and 19.8%, a common rate in the industry.

Also, Texas American will begin charging an undisclosed annual fee, he said.

There are no limits on credit card interest rates or annual fees imposed by Delaware law, which attracted Texas American to the state. "It offers one of the more favorable consumer credit laws," Mr. Clinkscales said.

Delaware's liberal credit laws, initially passed in 1981, already have attracted the credit card operations of about a dozen out-of-state banking companies, including two from Dallas — RepublicBank Corp. and MCorp.

A Dallas-based credit card processor, Southwestern States Bankcard Association, also is starting a Delaware operation.

Texas American has issued credit cards primarily to Texans, but Mr. Clinkscales said the banking company may expand its marketing efforts outside Texas. Many banks have promoted and issued credit cards around the country. ■

APPENDIX 6

Ladies +
GENTLEMEN (INTRODUCTION)

WE ARE A SMALL INDEPENDENT BANK IN SOUTHSIDE VIRGINIA WITH SEVEN BRANCHES AND ASSETS OF $107 MM. GEOGRAPHICALLY WE RANGE FROM PETERSBURG TO EMPORIA ALONG THE INTERSTATE 95 CORRIDOR. OUR BRANCHES ARE IN MOSTLY SMALL RURAL TOWNS, SUCH AS PRINCE GEORGE, STONY CREEK, AND EMPORIA AND DATE BACK TO THE EARLY 1900'S AS WE ARE AN OLDER BANK. WHILE OUR COMMERCIAL LOANS HAVE GROWN RECENTLY, WE ARE PRIMARILY A RETAIL BANK. THAT IS TO SAY, WE SEE OUR BREAD AND BUTTER CUSTOMER AS THE INDIVIDUAL RATHER THAN THE CORPORATION. WE CURRENTLY SERVE AROUND 14,000 INDIVIDUAL CUSTOMERS, SO WHILE WE ARE SMALL, WE ARE NOT INSIGNIFICANT.

SEVERAL YEARS AGO OUR BANK BEGAN USING AN AUTOMATED CREDIT REPORT SYSTEM, WHICH MADE IT EASIER TO CHECK THE CREDIT HISTORY OF ANYONE APPLYING FOR A LOAN. OUR OFFICERS NOTICED A District TREND TOWARDS REVOLVING CREDIT OR CREDIT CARDS, AND AWAY FROM THE TRADITIONAL INSTALLMENT LOAN. THIS CONCERNED US BECAUSE OBVIOUSLY WE ARE IN THE LOAN BUSINESS AND AT THAT POINT IN TIME COULD NOT OFFER CREDIT CARDS.

IN EARLY 1985 WE BEGAN INVESTIGATING THE FEASIBILITY OF OUR BANK ISSUING MASTERCARD AND VISA. PRELIMINARY PROJECTIONS SHOWED THAT WE COULD BREAK EVEN AT AROUND 1,000 CARDS AND 18 MONTHS INTO THE PROCESS. MANY OF YOU KNOW THAT 18 MONTHS IS A LONG TIME TO WAIT BEFORE RETURNING ANY PROFIT. INDEED OUR MOST RECENT BRANCH INVESTMENT TOOK LESS TIME THAN THIS TO BREAK EVEN. THE SHEET THAT I HAVE PASSED OUT IS A VERY SIMPLE BREAKDOWN OF OUR DIRECT PROFIT AND EXPENSE FOR THE PROGRAM SO FAR THIS YEAR. IT DOES NOT INCLUDE "INDIRECT" OR "SOFT"

COSTS THAT WE FEEL SHOULD BE CHARGED AGAINST PROFIT TO GET A FULLY ABSORBED COST FIGURE. AT THIS POINT, WE ARE LOOKING ONLY AT THE INCREMENTAL BUSINESS PROFITABILITY. AS ONE CAN PLAINLY SEE, WE HAVE QUITE A WAY TO GO BEFORE MAKING A PROFIT USING ONLY DIRECT EXPENSES.

WE ARE FOLLOWING ALONG REASONABLY CLOSE TO OUR ORIGINAL PROJECTIONS IN PART [redacted] BECAUSE OUR COST OF FUNDS HAS DECLINED, HOWEVER, IN OUR SITUATION [redacted] ADMINISTRATIVE AND PROCESSING EXPENSE IS MUCH MORE IMPORTANT THAN COST OF FUNDS. This [redacted] CAN BE SEEN ON THE HANDOUT. WE DO EXPECT AS OUR CARD BASE GROWS, THAT INCOME WILL RISE AT A FASTER RATE THAN EXPENSES ALLOWING US TO BECOME PROFITABLE.

MY POINT IN SHOWING YOU THESE NUMBERS IS NOT TO CONFUSE YOU, RATHER IT IS TO SHOW YOU THAT ONLY RECENTLY HAS IT BECOME FEASIBLE FOR A LOCAL COMMUNITY BANK LIKE OURSELVES TO BECOME A CARD ISSUING INSTITUTION.

IMPROVING TECHNOLOGY IS ONE REASON AS WE HAVE BEEN ABLE TO DEVELOP THIS PROGRAM WITH ONLY ONE FULL-TIME EMPLOYEE. I EXPECT THAT WE CAN GROW TO 2,000 TO 3,000 CARDS BEFORE I WILL NEED ANOTHER FULL-TIME PERSON.

ANOTHER REASON IS THE IMPROVED SPREAD BETWEEN ADMINISTRATIVE AND INTEREST COSTS VERSUS THE AVERAGE YIELD ON OUR CARDS. WE DID NOT GET TO WHERE WE ARE TODAY BY OFFERING A NON-COMPETITIVE PRODUCT. TO ATTRACT CARD BUSINESS AWAY FROM OTHER BANKS SUCH AS THE LARGE HOLDING COMPANIES WE HAD TO DEVELOP A COMPETITIVE ADVANTAGE. OUR CARDS ARE STRUCTURED AS FOLLOWS: VISA CLASSIC AND REGULAR MASTERCARD BOTH HAVE 18% INTEREST RATES WITH NO

ANNUAL FEES ASCESSED. VISA PREMIERE AND MASTERCARD GOLD REQUIRE $5,000 CREDIT LINES AND ARE PRICED AT PRIME PLUS 2% WITH A $40.00 ANNUAL FEE. THERE IS A FLOOR OF 9% ON THESE cards.

WE CHOSE TO COMPETE ON FEES WITH THE REGULAR CARDS, AND ON RATES WITH THE PREMIUM CARDS AND IT HAS WORKED. COMPETITIVE PRESSURES IN THE MARKET MAY FORCE US TO CHANGE. AN <u>INTEREST RATE CAP</u> WOULD FORCE US TO USE FEES TO OFFSET THE REVENUE LOSS AND WOULD DECREASE OUR FLEXIBILITY IN PRICING THE PRODUCT. INDEED I BELIEVE A CAP WOULD SOON BECOME A FLOOR.

AT THIS POINT, WE <u>ARE</u> BEING CONSERVATIVE. [redacted] AS YOU MIGHT HAVE NOTICED THERE IS NO PROVISION FOR LOSSES IN OUR HANDOUT. THAT IS SIMPLY BECAUSE WE HAVEN'T HAD ANY AS OF YET. AT THIS STAGE SERIOUS LOSSES COULD STILL TERMINATE THE PROJECT. THE AVERAGE LOSS RATIO IS NOW APPROACHING 5% NATIONALLY AND THIS ALARMS US. WE DO KNOW OUR CUSTOMERS AND FEEL WE CAN MAKE BETTER CREDIT DECISIONS THAN OUR LARGER COMPETITORS.

IN SUMMATION, I WOULD LIKE TO SUGGEST THAT PROFITS ARE NOT OBSCENE, RATHER, THEY FOSTER HEALTHY COMPETITION WHICH IN TURN BENEFITS THE CONSUMER. WE ARE A SMALL BUT GROWING PART OF THAT COMPETITION THAT WILL SURVIVE IF WE ARE GIVEN THE FLEXIBILITY TO COMPETE. IF YOU ARE GOING TO RESTRICT WHAT WE CAN CHARGE FOR OUR PRODUCTS, THEN YOU ARE GOING TO HAVE TO PROTECT US FROM CITICORP, SEARS, AMERICAN EXPRESS AND THE DOZENS OF OTHER COMPETITORS WHO CAN CHARGE WHAT THEY WISH. WE BOTH KNOW THAT THOSE DAYS OF ARTIFICIAL CONTROLS ARE GONE SO PLEASE LOOK TO THE FUTURE AND ALLOW THE MARKET TO DECIDE WHO SURVIVES.

I WILL TRY TO ANSWER ANY QUESTIONS YOU MAY HAVE AT THIS TIME.

THE BANK OF SOUTHSIDE VIRGINIA

Bankcard Report

	August	July	Year-to-Date
Cardholder Outstanding	185,869	145,157	
First Citizens Bank	35,352	9,334	
Merchant Deposits in Transit	41,894	37,281	
Total Funds Employed	263,115	191,772	
Cardholder Interest & Fees	1,953	1,572	4,982
Processing Income (Interchange)	1,122	909	3,426
Merchant Income	4,985	3,882	16,154
Total Income	8,060	6,363	24,562
Processing Expense (Interchange)	5,106	7,882	28,751
General Expense & Other	1,140	1,269	5,380
Total Expense	6,246	9,151	34,131
Profit before tax	1,814	(2,788)	(9,569)
Losses	-0-	-0-	-0-
Cost of funds	856	688	2,514
Profit or (loss) *	958	(3,476)	(12,083)

* Does not include approximately $450 per month in float and an estimated $10,000 additional in overhead per year. These are what we consider soft costs.

RECAP OF BANKCARD ACTIVITY

1986	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC
Number of Merchant Accounts			69	83	112*	117	122	123				
Number of VISA Cardholders			38	117	211	278	364	405				
Amount of VISA Outstanding			$9,155	$17,781	$37,731	$65,272	$89,192	$107,318				
Amount of VISA Credit Line			$76,800	$202,100	$340,200	$421,200	$540,300	$607,500				
Number of VISA PREMIER Cardholders			14	21	23	26	30	30				
Amount of VISA PREMIER Outstanding			$8,222	$10,270	$19,405	$23,122	$25,623	$29,626				
Amount of VISA PREMIER Credit Line			$75,000	$147,500	$160,000	$177,000	$197,000	$197,000				
Number of MASTERCARD Cardholders			10	64	113	156	208	238				
Amount of MASTERCARD Outstanding			$1,102	$5,075	$18,394	$30,031	$41,435	$57,396				
Amount of MASTERCARD Credit Line			$11,800	$75,800	$142,700	$192,000	$265,400	$310,600				
Number of MASTERCARD GOLD Cardholders			2	3	3	4	7	9				
Amount of MASTERCARD GOLD Outstanding			$1,456	$1,519	$1,332	$753	$988	$974				
Amount of MASTERCARD GOLD Credit Line			$10,000	$20,000	$20,000	$25,000	$40,000	$50,000				

*Locations of chain merchants counted separately, beginning with May report

BANKCARD HOLDERS OF AMERICA

333 PENNSYLVANIA AVE., S.E., WASHINGTON, D.C. 20003, 202/543-5805

the consumers association dedicated to protecting the interests of bank card holders.

TESTIMONY OF ELGIE HOLSTEIN
ASSOCIATE DIRECTOR
BANKCARD HOLDERS OF AMERICA
BEFORE THE
HOUSE COMMITTEE ON CORPORATIONS,
INSURANCE AND BANKING
OF THE
VIRGINIA GENERAL ASSEMBLY

FEBRUARY 4, 1986

I am pleased to present testimony to the Committee today on behalf of the approximately 120,000 members of Bankcard Holders of America (BHA).

BHA is a national, non-profit consumer organization dedicated to educating the public on their rights and responsibilities as credit card users. BHA is the only consumer group working exclusively on credit card issues. Founded in 1980, BHA is completely independent, supported solely by membership dues and receives no corporate, government or foundation support. We are not a lobbying organization and have no connection with any bank, credit card company or financial institution. Our membership consists of individual consumers from every state.

We are submitting our comments because BHA believes that consumers are paying far too much interest on their credit card balances. Furthermore, we have come to the somewhat unfortunate conclusion that legislation is necessary because banks have been unwilling to adjust consumer rates to the real cost of money in the economy.

As a consumer education organization, we have always focused on what action the consumer can and should take in order to get the most out of the credit card marketplace; we believe that the most effective way to make the credit card industry sensitive to consumers' needs is to create a consumer constituency that is informed enough to shop for the best credit card account. What we have found, however, is a credit card industry that refuses to compete for customers on the basis of interest rates. Banks continue to argue that consumers are not sensitive to changes in credit card interest rates. The truth, however, is that because of inadequate information and a lack of real choice, consumers just don't know where to turn.

We are pleased to see that this Committee is considering solutions to this problem. My comments today will focus on the need to resort to a legislative remedy to protect consumers from unreasonably high interest rates on credit cards. I will conclude with some specifics on what we believe should be included in consumer protection legislation for credit card users.

After polling our members and looking at industry trends, we are convinced that there are five strong reasons why protections are needed in this area.

FIRST, CONSUMERS WANT CREDIT CARDS THAT OFFER LOWER INTEREST RATES AND THEY ARE WILLING TO SWITCH IN ORDER TO GET THEM

The banks have suggested that consumers will not choose to subscribe to cards that will save them money. Our members tell us differently.

We recently polled our 100,000 members in the "1985 Credit Card Users Survey". Three-thousand-five-hundred (3,500) members responded with specific information about their concerns as credit card users. We asked them "What do you feel is the most important issue facing credit card consumers?". High interest rates were rated number one on their list. We also asked if they would switch to another Visa or Mastercard if it offered a lower interest rate, and 66% -- two out of three -- said yes. Seventy-nine percent of these card users reported paying 18% or more on their credit card balances and 69% said they carry over some balance on their card--with 38% maintaining a monthly balance of over $500.

Credit cards are no longer a luxury for the rich. They are a necessity for the millions of consumers who have grown to depend on them as an alternative payment mechanism. Seventy percent of all consumers have at least one credit card. We challenge the credit card industry to start providing credit cards that reflect more equitable interest rates for consumers and more reasonable profit margins for banks.

SECOND, EVEN THE MOST INFORMED CONSUMERS FIND THEMSELVES WITH FEW CHOICES IN THE CREDIT CARD MARKETPLACE.

Much of our educational effort is designed to inform consumers about what a credit card actually is. A credit card is a personal loan that you access with a piece of plastic. As with any loan, it is important to shop around to make sure you are getting the best rate on the money you are borrowing. Few of us accept the first car loan or mortgage offer we can find. Wise consumers research loan rates first and then apply for the loan that best fits their needs. The same should be true with credit cards. Consumers need to shop in order to get the best rates.

However, as we communicate this message to consumers with pamphlets on such topics as "How To Shop For A Bank Card" and our "No Annual Fee List", we receive responses like the following:

"...I know I am supposed to look around for the best interest rate, but where do those deals exist? I certainly can't find them in my area..." or "...I am receiving all sorts of offers on credit cards but I can't seem to figure out how to get an offer for a card with decent rates...do you know where I can find one?"

The banks are clearly benefitting from the fact that many consumers are unaware that different banks can charge different rates for the same type of card. Yet even those informed consumers who are aware of the possibility of lower interest rates must look far and wide -- often beyond their state's borders -- to find a fair rate.

We are pleased to note that recently there have been a few weak signs of responsible credit card pricing policy among a handful of banks. This is an encouraging sign, but rates are still far too high, nationally averaging 18.6%.

<u>THIRD, BANKS HAVE SHOWN US THAT THEY WILL NOT BE RESPONSIVE TO CHANGES IN THE ECONOMY ON A VOLUNTARY BASIS.</u>

In the last four years, three major economic indices (discount, prime and three-month treasury bill rates) have all fallen by 50%. With them, the banks' cost of money has also fallen, yet interest rates on credit cards have actually increased: from 17.8% up to 18.6%. In response to the drop in the cost of funds, interest rates on auto loans, mortgages and commercial loans have all declined. Why haven't credit card loans followed suit? Obviously, because they haven't had to. Instead, the banks compete by offering book-of-the-month club memberships, travel insurance, rebates, credit card protection, and other so-called "benefits".

In addition, interest rates are just one way in which banks make money on credit cards. There are annual fees (which vary between $15 and $25 for a standard card), there is the merchant discount fee (which ranges between 1% to 5% on each purchase made), and in many cases there are transaction fees, service fees, late fees and, increasingly, accrual of interest from the date of posting. Finally, initial credit limits range between $500 and $2,000 per card, (a relatively small loan amount by bank standards) but because of the economies of scale involved, credit card "loans" are much cheaper to administer than small, individual consumer loans.

<u>FOURTH, THERE ARE BANKS CURRENTLY MAKING PROFITS AT INTEREST RATES FAR LOWER THAN THE NATIONAL AVERAGE OF 18.62%</u>

Arkansas, where state law keeps credit card interest rates at five points over the discount rate, is a case in point. Banks located there, such as Union National Bank and Simmons First National Bank, that are currently charging 12.5% on their credit cards and admit to making a fair profit.

Washington State has interest rates averaging 15%. Ranier National Bank in Seattle is one bank which charges 15%. Chevy Chase Savings and Loan in Maryland now offers a variable rate credit card currently at 14%, with no annual fee. In New York, Apple Bank offers a rate of 15.8%.

These rates all come from relatively small banks that do not benefit from the savings associated with the economies of scale enjoyed by the larger card issuers. (Experts in the field agree that the more cards an issuer processes, the lower the unit cost of processing each card.) If Chevy Chase Savings & Loan or Union National Bank of Little Rock or Ranier National Bank in Seattle can charge below average rates, why don't the larger money center banks even come close? We believe the answer is because the large money center banks are cashing in on consumers' inability to find low-rate cards by pumping out plastic in national marketing campaigns.

FIFTH, CONSUMERS WILL ONLY BE PROTECTED FROM UNREASONABLY HIGH INTEREST RATES ON CREDIT CARDS IF LEGISLATION IS PASSED.

Legislation is no one's first choice as the best way to bring down high credit card interest rates. We fear, however, that without legslation, banks will continue to take advantage of consumers' lack of informaton about and access to reasonable-rate credit cards.

I would now like to answer some of the claims made by the banking industry in defense of high interest rates on credit card balances:

CLAIM: Roughly 30% of consumers take advantage of the "free ride" by paying off their credit card bills in full each month. Therefore, consumers who maintain balances must pay higher interest rates in order to subsidize those who do not carry over charges.

RESPONSE: The banks used this argument very effectively in the late 70's and early 80's. They lobbied state legislatures to allow annual fees for credit cards to pay for the administrative costs associated with the card. We'd like to ask what the annual fee is now being used for, if not to pay for those administrative costs.

CLAIM: Credit card operations have only recently begun to make a profit and are now recouping the heavy losses incurred during the late 70's and early 80's, when the cost of money exceeded interest rate ceilings.

RESPONSE: First, it simply isn't fair to penalize consumers today for losses incurred and written off in years past. Second, if the cost of money was the major determinant of credit card profitability several years ago, why do banks now claim -- after their cost of money has dropped by 50% -- that administrative costs are a more important factor? Third, banks some time ago began collecting revenues through means other than the interest rate: the merchant discount fee, annual fees, transaction fees, service fees, late fees and, increasingly, interest charged from the date of purchase. How much is enough? We believe that failure to lower rates to fair levels can be attributed more to the banks' desire to make increased profits than to efforts to make up for previous losses.

CLAIM: Lower-income consumers will be pushed out of the credit card market if interest rates are lowered.

RESPONSE: We appreciate the banks' concern but in reality the situation that now exists is that many consumers have been given far too <u>much</u> credit. Credit overextension has become a significant problem in our economy. The Foundation for Consumer Credit (a non-profit organization that counsels consumers with credit problems) reports an increase in the requests for counseling on problems related to credit card overextension. At the same time, they report that banks are less inclined to refer delinquent customers to them and more inclined to refer problem cases directly to debt collectors. The solution to freezing out higher risk consumers is not to charge higher interest rates to all cardholders; rather, such higher risk prospective cardholders can be offered collateralized accounts or accounts with lower credit limits.

<u>CLAIM</u>: Credit card fraud is on the rise; therefore, higher interest rates are necessary to cover the extra costs associated with these losses.

<u>RESPONSE</u>: Fraud and credit losses together account for less than 1.2% of total losses, barely above the average levels of the last thirty years. According to the Wall Street Journal, the banks suffering higher losses are those which are so anxious to make big credit card profits that they're sending out cards without making sure of the creditworthiness of the recipients. It is important to note here that the bulk of losses from credit card fraud involve organized criminal activity. The two largest sources of fraud include: (1) the so called "white plastic" scheme in which real credit card numbers are embossed onto phony white plastic cards and then pushed through the system with the help of willing merchants, and (2) the scam involving phony telephone marketers who call with an offer and then use the card number for other purposes. Both types of fraud require large scale operations that have nothing to do with the average consumer's misuse of credit. Banks and their regulators must devise ways to address fraud where it exists at meaningful levels--penalizing organized crime, not ordinary citizens. We do not consider it an appropriate solution to simply pass those costs on directly to the consumer who is not responsible for such abuses.

* * *

As an organization representing credit card holders, we recognize the importance of ensuring that the credit card industry remains profitable; it is in all our interests to make credit available to the people who need it. We do not want to inhibit banks from competing. Our main concern is that consumers' legitimate needs are calculated into any profit equation.

In any legislation intended to protect consumers from unreasonably high credit card interest rates, we urge that you address the following issues:

1) Credit card interest rates should be tied to some economic index that reflects the cost to the banks of borrowing money, plus some margin allowing for costs and profits.

2) There should be improved disclosure laws in order to ensure the added competition that we feel should come as a result of this legislation. One possible danger we see in requiring banks to lower their rates is that they

may seek to make up for the change by imposing "hidden fees". In reviewing several credit card applications, we have found that it is often very difficult to find the interest rate. It can also be difficult to discover when interest begins to accrue and when other charges may apply. We would like to see some requirement that banks make information more clearly evident in promotional material, including the annual fee, the interest rate, the method of calculation and the date upon which interest will begin to accrue.

Finally, I would like to thank the members of this Committee for recognizing the importance of ensuring an equitable credit card marketplace for the millions of consumers who have come to depend on credit cards as an alternative payment mechanism. The very fact that you are holding this hearing sends a strong signal to the public and to the banking industry that this issue will not be ignored.

HOUSE BILL NO. 1486

Offered January 27, 1987

A BILL to amend and reenact §§ 6.1-330.19:1 and 6.1-330.20 of the Code of Virginia, relating to credit cards.

Patrons—Parker, Jones, Grayson, Cohen, Heilig, Almand, Creekmore, Stambaugh, Brickley and Keating

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Referred to the Committee on Corporations, Insurance and Banking

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Be it enacted by the General Assembly of Virginia:

1. That §§ 6.1-330.19:1 and 6.1-330.20 of the Code of Virginia are amended and reenacted as follows:

§ 6.1-330.19:1. Charges by banks.—A. 1. Any bank may charge a rate as agreed between it and the borrower under a contract for revolving credit or any plan which permits an obligor to avail himself of the credit so established. Any charge computed on the basis of a rate shall be charged at the option of the bank on either (1) the average daily balance for the period ending on the billing date or (2) the balance existing on the billing date of the month, or (3) any other balance which does not result in the seller or lender charging and receiving any sum in excess of what would be charged and received in (1) or (2). No service charge shall be charged unless the bill is mailed not later than eight days (excluding Saturdays, Sundays and holidays) after the billing date, except that such time limitation shall not apply in any case where the seller or lender has been prevented, delayed, or hindered in mailing or delivering the bill within such time period because of an act of God, war, civil disorder, natural disaster, strike, or other excusable or justifiable cause.

2. In the event of the extension of credit by a bank hereunder to be effected by the use of a credit card for the purchase of merchandise or services, no charge shall be imposed upon the cardholder or borrower on such extension if payment in full of the unpaid balance owing for extensions for merchandise or services is received at the place designated by the creditor prior to the next billing date (which shall be at least twenty-five days later than the prior billing date).

3. Any payment, in full or in part, received by the bank shall be credited against such extension of credit within two banking days of its receipt.

B. The higher rate in excess of charges permitted prior to July 1, 1982, shall not take effect as to balances existing on or before April 1, 1983, unless (1) such creditor shall notify the borrower in writing of the proposed change, that acceptance of the higher charge on existing balances and balances incurred prior to the effective date of the change is accepted by use of the revolving credit after the giving of the notice, and such borrower is given at least nine months prior to the effective date of such change to pay off balances existing on the date of such notice, and (2) such borrower accepts the proposed change and modification of interest rates by using the revolving credit at any time thirty days or more after the giving by the creditor of the notice.

C. Beginning after ~~April 30, 1987~~ *September 30, 1987* , in the case of any plan in which the charge authorized by this section is imposed on the average daily balance and such balance is calculated under the plan without excluding purchases incurred during the billing period, the issuer shall disclose to all new cardholders and ~~, annually thereafter, to all active accounts, the following~~ *thereafter on the upper one-third of the periodic statement, the following in letters at least equal in size to the letters used in the wording of the minimum payment terms* :

~~NOTICE~~

~~Unless the New Balance shown on your statement is paid in full by the next billing date, new purchases you make in the current month will be subject to Finance Charges that will be billed on the next month's statement.~~ *To avoid additional finance charges* *being applied to your current purchases on next month's statement, pay the new balance on this statement in full by the due date.*

§ 6.1-330.20. Open-end sales and loan plans.–A. Any seller or lender engaged in the extension of credit under an open-end credit or similar plan under which a service charge is imposed upon the cardholder or consumer if payment in full of the unpaid balance is not received at the place designated by the creditor prior to the next billing date (which shall be at least twenty-five days later than the prior billing date), may charge and collect a service charge at such rate or rates as may be agreed upon by the seller or lender and the cardholder or consumer, computed at the option of the seller or lender on either (1) the average daily balance for the period ending on the billing date or (2) the balance existing on the billing date of the month, or (3) any other balance which does not result in the seller or lender charging and receiving any sum in excess of what would be charged and received in (1) or (2) above. No service charge shall be charged unless the bill is mailed not later than eight days (excluding Saturdays, Sundays and holidays) after the billing date, except that such time limitation shall not apply in any case where the seller or lender has been prevented, delayed, or hindered in mailing or delivering the bill within such time period because of an act of God, war, civil disorder, natural disaster, strike, or other excusable or justifiable cause. Notwithstanding the provisions of this section, a seller or lender may charge and collect a minimum service charge of one-half dollar per month; however, no service charge shall be charged against a zero balance. For the purposes of this section the average daily balance for any period shall be that amount which is the sum of the actual amounts outstanding each day during the period, divided by the number of days in the period.

B. Notwithstanding the provisions of § 6.1-330.16 ~~of the Code of Virginia~~ , any loan made under this section may be secured in whole or in part by a subordinate mortgage or deed of trust on residential real estate improved by the construction thereon of housing consisting of four or less family dwelling units. For the purposes of this chapter relating to money and interest, a subordinate mortgage or deed of trust is one subject to a prior mortgage or deed of trust in existence at the time of the making of the loan secured by such subordinate mortgage.

C. No increase in service charge rate shall take effect unless at least thirty days prior to the effective date of such increase a written notice of the increase has been mailed or otherwise delivered to the cardholder or consumer explaining that the making of additional charges under the plan on or after the effective date of the increase shall be deemed to constitute acceptance of such higher charge on existing balances and charges incurred thereafter under the plan.

D. Beginning after September 30, 1987, in the case of any plan in which the charge authorized by this section is imposed on the average daily balance and such balance is calculated under the plan without excluding purchases incurred during the billing period, the issuer shall disclose to all new cardholders and thereafter on the upper one-third of the periodic statement, the following in letters at least equal in size to the letters used in the wording of the minimum payment terms:

To avoid additional finance charges being applied to your current purchases on next month's statement, pay the new balance on this statement in full by the due date.

2. That an emergency exists and the provisions of this act shall become effective April 30, 1987.

Official Use By Clerks

Passed By The House of Delegates		Passed By The Senate	
without amendment	☐	without amendment	☐
with amendment	☐	with amendment	☐
substitute	☐	substitute	☐
substitute w/amdt	☐	substitute w/amdt	☐

Date: ____________________ Date: ____________________

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Clerk of the House of Delegates Clerk of the Senate

LD6324484

HOUSE BILL NO. 1079

Offered January 20, 1987

A BILL to amend and reenact § 6.1-194.41 of the Code of Virginia, relating to foreign savings institutions.

Patron—Heilig

Referred to the Committee on Corporations, Insurance and Banking

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Be it enacted by the General Assembly of Virginia:

1. That § 6.1-194.41 of the Code of Virginia is amended and reenacted as follows:

§ 6.1-194.41. Foreign savings institutions; certificate of authority.—A. A foreign savings institution shall not transact a savings institution business in the Commonwealth unless it first receives from the Commission a certificate of authority to do so.

B. A foreign savings institution may apply to the Commission for a certificate of authority by paying the filing fee prescribed by the Commission and filing an application which shall include:

1. A copy of its articles of incorporation and bylaws certified as a true copy by the public officer having custody of the original articles and bylaws;

2. Evidence satisfactory to the Commission that its accounts are insured by the Federal Savings and Loan Insurance Corporation, Federal Deposit Insurance Corporation or other federal agency satisfactory to the Commissioner; and

3. Such other information as the Commission may require.

C. The Commission shall issue a certificate of authority to the foreign savings institution when:

1. The Commissioner has examined the application of the institution and investigated and determined that the institution meets the requirements of § 6.1-194.12;

2. The Commissioner has verified the financial status of the institution by conducting such examination of its assets and its records as the Commission shall deem appropriate for the purpose of ascertaining whether they meet the requirements of this chapter with regard to state associations;

3. The Commissioner is satisfied that the institution is in sound financial condition, and that it is conducting its business, and will conduct its business in the Commonwealth, in a manner consistent with the laws of the Commonwealth; and

4. The Commissioner is satisfied that the laws, regulations or administrative actions of the state or territory where the principal office of the applicant is located do not prohibit or unfairly impede a state association from transacting business in such state or territory.

D. In meeting the requirements set out in subdivisions 1, 2 and 3 of subsection C of this section, the Commissioner may rely on examinations, audits and other information provided by the federal and state supervisory authorities charged with the responsibility of regulating and supervising savings institutions in the state where the applicant's principal place of business is located. Prior to issuing a certificate of authority to the foreign savings institution, the Commission shall enter into cooperative agreements with the appropriate regulatory authorities for the periodic examination of the foreign savings institution. The Commission may accept reports of examination and other records from such authorities in lieu of conducting its own examinations.

E. No foreign mutual savings institution shall be authorized to transact a savings institution business in the Commonwealth unless at least eighty percent of the deposits of such foreign savings institution were initially deposited in offices of the savings institution located in a geographic region consisting of the states of Alabama, Arkansas, Florida, Georgia, Kentucky, Louisiana, Maryland, Mississippi, North Carolina, South Carolina, Tennessee, Virginia and West Virginia, and the District of Columbia. No foreign stock savings institution shall be authorized to conduct a savings institution business in the Commonwealth except as a result of the acquisition of a state stock association under the provisions of Article 11 (§ 6.1-194.96 et seq.) of this chapter. ~~No~~ *Except as permitted by the provisions of Article 11 (§ 6.-194.96 et seq.) of this chapter, no* foreign savings institution which is a subsidiary as defined in § 6.1-194.96, of a savings institution holding company, shall be authorized to conduct a savings institution business in the Commonwealth unless such savings institution is a subsidiary of a Virginia savings institution holding company, as defined in § 6.1-194.96.

Official Use By Clerks	
Passed By The House of Delegates	**Passed By The Senate**
without amendment ☐	without amendment ☐
with amendment ☐	with amendment ☐
substitute ☐	substitute ☐
substitute w/amdt ☐	substitute w/amdt ☐
Date: ______________	Date: ______________
Clerk of the House of Delegates	Clerk of the Senate

LD6650484

HOUSE BILL NO. 1272

Offered January 26, 1987

A BILL to amend the Code of Virginia by adding in Article 11 of Chapter 3.01 of Title 6.1 a section numbered 6.1-194.107 and by adding a section numbered 6.1-399.1, relating to interstate acquisitions of certain financial institutions.

Patron–Heilig

Referred to the Committee on Corporations, Insurance and Banking

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Be it enacted by the General Assembly of Virginia:

1. That the Code of Virginia is amended by adding in Article 11 of Chapter 3.01 of Title 6.1 a section numbered 6.1-194.107 and by adding a section numbered 6.1-399.1 as follows:

§ 6.1-194.107. A bank or bank holding company seeking to acquire a savings institution or savings institution holding company.–For purposes of this article, any bank or bank holding company seeking to acquire a savings institution or savings institution holding company, shall be deemed to be a savings institution or savings institution holding company, as the case may be, for purposes of determining whether such bank or bank holding company is permitted to acquire the savings institution or savings institution holding company in question.

§ 6.1-399.1. A savings institution holding company seeking to acquire a bank or bank holding company.–For purposes of this article, any savings institution holding company seeking to acquire a bank or bank holding company, shall be deemed to be a bank holding company, for purposes of determining whether such savings institution holding company is permitted to acquire the bank or bank holding company in question.

Official Use By Clerks

Passed By The House of Delegates		**Passed By The Senate**	
without amendment	☐	without amendment	☐
with amendment	☐	with amendment	☐
substitute	☐	substitute	☐
substitute w/amdt	☐	substitute w/amdt	☐

Date: ____________________ Date: ____________________

Clerk of the House of Delegates   Clerk of the Senate