Memorandum on the Disclosure of Cost of Consumer Credit 1995

1995 Quebec QC

Civil Section Documents - Memorandum on the Disclosure of Cost of Consumer Credit

By: Richard Bowes, Alberta Law Reform Institute

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ABOUT THIS MEMORANDUM

This memorandum discusses certain process-related and substantive issues regarding the Uniform Law Conference of Canada ("ULCC") project on cost of credit disclosure legislation ("ccdl"). It is intended to provide a framework for the discussion of cost of credit disclosure at the 1995 Conference.

This memorandum was completed on June 13, 1995. There are many references in this memorandum to proposals contained in a Consultation Paper prepared by a working group on cost of credit disclosure. The text of the Consultation Paper had not been finalized as of the June 13 completion date of this memorandum. Therefore, statements herein about the contents of the Consultation Paper are based on a **draft**, rather than the final version, of

the Consultation Paper. There is likely to be some variation between the final version of the Consultation Paper and the draft upon which statements in this memorandum are based. However, except where otherwise indicated, I do not anticipate major changes in the proposals referred to in this memorandum from the draft to the final version of the Consultation Paper.

This memorandum is intended to be read in conjunction with Draft 4.1 of the Cost of Credit Disclosure Act ("CCDA 4.1) and with the Consultation Paper. Copies of these two documents will be provided to delegates along with this memorandum. Several other documents referred to in this memorandum will not be included in the materials provided to delegates. Copies of these other documents are available upon request from the Alberta Law Reform Institute ("ALRI").

GLOSSARY

The following abbreviations are used in this memorandum.

1994 Memorandum	*Memorandum on Cost of Credit Disclosure* (ALRI, 1994) prepared for the 1994 Conference
AIR	annual interest rate
AIT	Agreement on Internal Trade, signed by all provinces and territories and the federal government in 1994
ALRI	Alberta Law Reform Institute
APR Paper	Paper entitled *Disclosure and Restriction of Non-Interest Charges* (ALRI, 1995) prepared for the CMC working group on cost of credit disclosure
APR	annual percentage rate _ a calculated value that measures the cost of borrowing, including both interest and non-interest charges
CCDA 3.2 CCDA 4.1	Cost of Credit Disclosure Act, Drafts 3.2 (1994) and 4.1 (1995)
ccdl	cost of credit disclosure legislation _ a generic reference to such legislation

CMC	Consumer Measures Committee _ a committee of government officials set up under the AIT
CRMS	Consumer Related Measures Sector, one of the areas covered by the AIT
FDS	final disclosure statement
PDS	preliminary disclosure statement
PIA 2.0	Proposed Interest Act, Draft 2.0 (1994)
RLRF	rebate or low-rate financing [program] _ a program under which consumers are offered a choice between a cash rebate and low-rate financing
ULCC	Uniform Law Conference of Canada
ULS	Uniform Law Section of the ULCC

THE PROCESS OF HARMONIZATION

A. Last Year's Conference

During the 1994 Uniform Law Conference the Uniform Law Section ("ULS") considered the following documents relating to the project on cost of credit disclosure:

1. Memorandum on Cost of Credit Disclosure ("1994 Memorandum");

2. Cost of Credit Disclosure Act, Draft 3.21, with Discussion Notes ("CCDA 3.2");

3. Proposed Interest Act, Draft 2.0 ("PIA 2.0").

CCDA 3.2 and PIA 2.0 had been circulated for comment by interested parties in the spring of 1994. Some of these comments were reflected in the 1994 Memorandum's discussion of substantive issues.

In addition to issues regarding the content of uniform ccdl, the 1994 Memorandum raised the issue of how the ULCC could best coordinate its process with the process for harmonizing ccdl envisioned by the Agreement on Internal Trade ("AIT"). The 1994 Memorandum mentioned that harmonization of ccdl was dealt with in the part of the AIT dealing with the consumer related measures sector ("CRMS"), and that the task of

implementing the AIT's commitment to harmonization would fall to the CRMS negotiators for each jurisdiction. The 1994 Memorandum discussed two approaches that the ULCC might take to the coordination problem. The recommended approach was as follows:

At this August's meeting the Uniform Law Section [should] take the following steps.

(a) Consider the issues raised by this report and make decisions that reflect the Uniform Law Section's current view as to the best approach to those issues.

(b) Appoint a drafting/liaison committee to represent the ULCC in continuing consultations with CRMS negotiators.

If the CRMS negotiators reach agreement on all outstanding issues relating to ccdl by the spring of 1995, the drafting/liaison committee [should] prepare a final draft of CCDA that reflects that agreement. This draft [should] be formally adopted at the 1995 Conference.

If the CRMS negotiators fail to reach agreement on all outstanding issues by the spring of 1995, the drafting/liaison committee [should] prepare a proposed final draft of CCDA for consideration at the 1995 Conference. The draft [should] reflect the consensus on those issues where a consensus has been achieved. On other issues, the draft [should] represent the recommended approach of the drafting/liaison committee. The draft CCDA [should] be adopted, with any changes considered desirable by the Uniform Law Section, at the 1995 Conference.

After considering the 1994 Memorandum and the two draft acts (CCDA 3.2 and PIA 2.0), the ULS adopted the following resolution:

That the principles of both Acts and the statutory language of the Uniform Cost of Credit Disclosure Act reflecting them be adopted, subject to further consideration of specified provisions and subject to minor adaptations of other parts of the draft statute to meet the needs of federal/provincial/territorial officials in the context of the internal trade agreement.

As will be explained below, coordinating the ULCC's efforts with those of the officials responsible for implementing the AIT's commitment to harmonization of ccdl has been somewhat more challenging than was envisaged during the 1994 Conference.

B. Developments Since Last Year's Conference(1)

The CMC and ULCC: Common Goals, Different Schedules The 1994 Memorandum identified the CRMS negotiators as the officials responsible for implementing the AIT's commitment to harmonization of ccdl. This function (amongst others) has now been assigned to an interjurisdictional committee of officials called the Consumer Measures Committee ("CMC"). Each jurisdiction has appointed one or more officials to represent it on the CMC. Although I have said that the CMC is responsible for implementing the AIT's commitment to harmonization of ccdl, it should be emphasized that the CMC's members are officials, not politicians. One assumes that any agreement on the details of harmonized ccdl reached at the level of the CMC will ultimately have to be approved by each jurisdiction at the political level.

The CMC held a conference call in late September of 1994 to discuss a number of issues relating to the implementation of the AIT, including the process for harmonizing ccdl. Before the conference call I provided members of the CMC with a 10-page memo that discussed a number of process and substantive issues. The memo suggested a timetable that would have a working group reach a consensus on all outstanding issues in time to draft a final version of the CCDA for this year's ULCC Conference. The memo also briefly discussed what I saw as being the major outstanding unresolved issues.

By the end of the September conference call it was apparent that the CMC's ideas about the process for achieving harmonized uccdl were not exactly congruent with the ULCC's view. The following are major points upon which the two bodies' views are not fully congruent with each other.

*Having undertaken the project in 1990, the ULCC viewed the project as being in its final stages. Having only recently focused their attention on the subject, the CMC regarded the project as having just got underway.

*At the time of the 1994 Conference, the ULCC was under the impression that there was a broad measure of agreement on the appropriate approach to most substantive issues addressed by the draft acts. The ULCC believed that there were only a few major outstanding issues upon which a consensus needed to be reached. The CMC thought that every substantive issue connected with ccdl should be open for discussion.

*The ULCC had done extensive consultation regarding its evolving proposals from 1991 through 1994 and did not consider that it was necessary or desirable to undertake yet another round of consultation on every issue addressed by uniform ccdl. At most, further consultation on a number of especially contentious issues might be desirable. The CMC considered that it was necessary to consult broadly on all issues that would be addressed by harmonized ccdl. The CMC considered that is was important for governments, as opposed to the ULCC, to be seen to be consulting on all issues relating to harmonization of ccdl.

*The ULCC thought that it was feasible and desirable to do any necessary consultation and reach final agreement (at least at the bureaucratic level) on all outstanding issues by the spring of 1995. This would give the ULCC time to do a final redraft of the CCDA in time for this year's Conference. Since the AIT calls for the parties to agree on the contents of harmonized ccdl by January 1, 1996 (with implementation by January 1, 1997), the CMC did not think it was necessary to reach final agreement on the contents of harmonized ccdl much before December 31, 1995.

After the September CMC conference call, Peter Lown, John Gregory and I attempted to persuade the CMC to streamline its process somewhat. However, as time went by, it became apparent that the CMC would not conclude its deliberations in time to incorporate the CMC's final position in a definitive CCDA that could be adopted at this year's Conference. I have had to scramble to complete an interim redraft of the CCDA reflecting (on most issues, at least) the tentative views of the CMC working group. The working group's views are expressed in the soon-to-be finalized Consultation Paper.

The Annual Percentage Rate Controversy At this point I am going to discuss a point that might seem to belong not here but in the part of this memorandum dealing with substantive issues. To be sure, the "APR controversy" is a crucial substantive issue, but the stage at which the controversy arose has also created an interesting issue of process.

You will recall from previous materials and Conferences that the centre-piece - or sacred cow, as I would put it - of existing ccdl in Canada (and most other countries) is a requirement that lenders calculate and disclosure the annual percentage rate ("APR"), for fixed loans.(2) The functional difference between the APR and the annual interest rate ("AIR") for a loan is that, unlike the AIR, the APR accounts for the effect of non-interest charges on the overall cost of borrowing for a loan.(3) The 1991 Issues Paper tentatively proposed to retain APR disclosure in uniform ccdl or, more accurately, assumed that uniform ccdl would continue to require APR disclosure. However, the 1992 Principles Paper essentially proposed to abandon the calculated APR(4). The Principles Paper proposed that lenders be required to disclose the AIR and the dollar amount of non-interest charges. In addition, and crucially, it was proposed to put certain express restrictions on the type of non-interest charges that lenders could impose in connection with consumer loans. These restrictions were designed to ensure that non-interest charges imposed in connection with loans would not be so high as to distort the value of the AIR as a relative measure of the cost of different credit arrangements.

The general approach proposed in the 1992 Principles Paper, which for convenience I will refer to throughout this memorandum as the "AIR approach", was refined in CCDA 2 (1993) and CCDA 3.2 (1994). Our consultation from 1992 through the first half of 1994 did not suggest that there was a lot of opposition to the general AIR approach, although there was considerable debate about its details. In particular, the CCDA's the concept of a "flat charge" proved to be particularly controversial. Essentially, a flat charge is a non-interest charge that is the same for all loans within a certain lender-defined category, regardless of the amount of a particular loan within that category.

Through the first half of 1994, commentators expressed the following sorts of concerns regarding the CCDA's method of dealing with flat charges.

*A few commentators, particularly government commentators, argued that lenders should not be entitled to impose a flat charge in connection with fixed credit. Any expenses that would otherwise be covered by a flat charge should instead be covered by an appropriate adjustment to the interest rate.

*Some commentators thought that there should be a legislated cap on the amount of flat charges, while other commentators thought we should rely on market forces to keep flat charges at competitive levels.

*There was some debate as to what constraints, if any, the CCDA should place on the criteria lenders could use to categorize loans for the purpose of setting flat charges. The main issue here was whether lenders should be able to use the amount advanced to the borrower as a criterion for categorizing loans.

Both shortly before and shortly after last year's Conference, the ALRI received comments from a couple of credit grantors' organizations that made a different sort of argument. They argued that uniform ccdl should not restrict non-interest charges at all. Rather, ccdl should simply ensure that any charges that are imposed are properly disclosed to consumers. My response to these arguments is that CCDA's restrictions on the types of non-interest charges that lenders may impose are intended to do transparently and directly what existing ccdl does opaquely and indirectly. Certain restrictions on non-interest charges (whether direct or indirect) are inherent in the longstanding Canadian policy that allows consumers to prepay non-mortgage loans without penalty. Moreover, the proposed restrictions on non-interest charges were designed to facilitate meaningful disclosure of the cost of credit, and would not impair lenders' ability to structure the pricing for their loans in a manner that reflects the costs of setting up, funding and administering different loans.

During the September 1994 CMC conference call several CMC members suggested that perhaps mandatory APR disclosure should be retained in harmonized ccdl after all. By the time the call ended it was apparent to me that this horse, which I had assumed was dead, was very much alive. In fact the CMC working group ("CMC working group"), whose activities I will describe more fully in a moment, has decided to propose in its Consultation Document that mandatory APR disclosure continue to be required in uniform ccdl. This is a fundamental change from the approach of that the ULCC has been proposing since 1992. I will come back to the implications of this change later in this memorandum.

The Federal-Provincial Working Group You may recall that early in 1994, after learning that harmonization of ccdl had been put on the agenda for the internal trade negotiations, John Gregory invited the CRMS negotiator from each jurisdiction to nominate a representative to serve on a cost of credit working group. It was contemplated that the working group would try to resolve outstanding issues in time for the ULCC to approve a uniform act at the 1994 Conference. Most jurisdictions took up the invitation, and the working group met for two days in Toronto in early March of last year. Although the group did not reach a consensus on all issues, its deliberations were reflected in CCDA 3.2, which was considered at last year's Conference.

The working group referred to in the preceding paragraph was organized by the ULCC, but most of its members were nominated by the CRMS negotiators. Nevertheless, during its September 1994 conference call the CMC decided to set up its own working group, which is the one I have been referring to as the CMC working group(5). Although John Gregory and I have participated actively in the CMC working group's deliberations, it is the CMC's working group, and its proposals are those of the CMC. The proposals in the CMC Consultation Paper will be advanced as proposals of the CMC, rather than as joint proposals of the CMC and the ULCC.

The CMC working group had its first meeting in late November 1994, but the purpose of that meeting was to deal with process issues, rather than substantive issues. During that meeting it was decided that the group would develop a policy paper that would set out detailed proposals (in non-statutory language) for harmonized ccdl that would be circulated

for comment to "stakeholders" in the spring of 1995. The first substantive meeting was scheduled for early February.

Before the CMC working group's first substantive meeting I provided its members with two documents:

*a 60-page paper entitled *Disclosure and Restriction of Non-Interest Charges in Existing and Proposed Cost of Credit Disclosure Legislation* ("APR Paper").

This paper dealt with the advantages and disadvantages of mandatory APR disclosure, and argued that the approach suggested by the ULCC would be less complicated and would provide consumer borrowers with effective disclosure of the cost of credit.

*an 80-page memorandum entitled *Policy Memorandum on Harmonized Cost of Credit Disclosure Legislation*.

This memorandum described a series of issues that have to be addressed by uniform ccdl. Each issue was followed by one or more propositions as to how it should be addressed in uniform ccdl. For the most part, the propositions were formulated so as to reflect (in non-statutory language) the text of CCDA 3.2, modified as necessary to reflect comments that we have received on CCDA 3.2.

During the course of the CMC working group's deliberations I have supplied its members with a few additional documents:

*a 22-page memorandum entitled *Supplementary Policy Issues*.

This memo dealt with some issues that I had not had time to deal with in the main policy memorandum. It followed the same format: a description of issues and propositions about each issue.

*a 22-page memorandum entitled *APR Calculation and Disclosure Issues*.

When it became obvious that many members of the CMC working group were not going to be easily convinced to abandon APR disclosure, I prepared this memorandum to raise a number of issues that would have to be addressed if the APR approach was going to be continued in uniform ccdl. One purpose of this memorandum was to impress upon working group members the complexity of the issues raised by mandatory APR disclosure. Unfortunately, I am not sure that it made much of an impression in this regard.

*an 8-page memorandum entitled *Balance Calculations*.

The working group decided that not only should non-interest charges be included in a calculated APR, but some of these charges should be partially refunded when a loan is prepaid. This made it necessary to determine how the rebateable portion of these refundable charges should be calculated. The *Balance Calculations* memorandum discussed this issue.

N.B.The documents mentioned above are not included in the package of materials for the Conference, but are available on request from the ALRI.

The first substantive CMC working group conference call took place on February 27, 1995. As of June 8 the group has held a total of 11 conference calls (each of about 2 hours duration) as well as a 3 day face-to-face meeting in Toronto.(6) I have participated in all the calls and meetings and John Gregory has participated in most of them.

The CMC's Ongoing Process The working group has reviewed several drafts of the CMC Consultation Paper, and the paper is almost ready to be circulated. However, even as late as the conference call of June 8, the working group's proposals on several important issues (such as how to calculate the APR) had still not been finalized. As already discussed, the Consultation Paper will propose that harmonized ccdl continue to required APR disclosure for fixed credit. In most other respects, the working group's proposals are consistent with the general thrust, if not all the details, of CCDA 3.2.

Once the working group is satisfied with the Consultation Paper it will be submitted for approval by the CMC itself. It will then be circulated to stakeholders, who will be asked to provide written comments by the middle of August. After evaluating the written comments, the CMC working group will attempt to reach a consensus on all outstanding issues by early in the fall. It is envisaged that some outstanding issues might have to be resolved by higher officials or at the political level. The CMC's ultimate objective is to reach agreement at the political level on the content of harmonized ccdl by the January 1 deadline set out in the AIT.

CCDA 4.1 and the CMC's Consultation Paper Drafting CCDA 4.1 has been an interesting process, to say the least. By March it was apparent that the CMC working group was not going to be persuaded to propose the AIR approach in the Consultation Paper, and was likely to propose the APR approach.(7) Nevertheless, the ULCC steering committee decided that the draft of the CCDA to be presented at this year's Conference should be based on the approach that the ULCC has been proposing and developing since 1992. That is, the draft would continue the approach of requiring disclosure of the AIR and the dollar amount of non-interest charges, as well as placing certain qualitative restrictions on non-interest charges. The decision to continue drafting to the AIR approach was made on the basis that the CMC's consultation process may lead it to reconsider its rejection of the AIR approach.

Of course, consideration should be given to what uniform ccdl would look like if the APR approach recommended in the CMC Consultation Document is ultimately adopted by those who have the final say in such matters. In fact, I originally intended to include "alternative provisions" in CCDA 4.1 that would actually implement the APR approach. However, I abandoned that idea when it became apparent that the CMC working group would not have reached a consensus on the details of the APR approach in time to put those details in statutory language. However, Appendix 1 of this memo indicates which provisions of CCDA 4.1 would have to be modified (or deleted entirely) to accommodate the APR approach, as proposed by the CMC working group.

Apart from the fact that it does not implement the APR approach, and with a couple of other exceptions I will mention later, I believe that CCDA 4.1 is a fair reflection of most of the proposals in the Consultation Paper. I say this with some trepidation, because the working

group's exact position on a number of issues had not been crystallized at the time I was drafting CCDA 4.1. I had a pretty good idea what the Consultation Paper's position on most issues was likely to be, but its exact position on certain issues was not absolutely clear. Indeed, even when the Consultation Paper is circulated, I suspect that the details of the CMC working group's position on certain issues will be somewhat ambiguous.

Before leaving CCDA 4.1 (for the time being), it is worth emphasizing that on most major issues, the working group's proposals follow the general course charted by CCDA 3.2. Implementing the working group's proposals regarding open credit, leasing and compliance has required relatively minor changes from CCDA 3.2 to CCDA 4.1. Even in the context of fixed credit, apart from the APR issue, implementation of the working group's proposals did not require major changes to the provisions of CCDA 3.2.

The Interest Act You may have noticed that I have hardly mentioned the PIA. At last year's Conference the consensus seemed to be that the ULS should not adopt a text of a proposed replacement for the *Interest Act*. This was probably just as well, because it appears that the federal government is not convinced that it is necessary to replace or make wholesale changes to the *Interest Act* in order to fulfil its commitments under the AIT.(8) For the time being, all the government intends to do is to amend sections 4 and 6 of the *Interest Act* to allow the Governor in Council to prescribe the method of calculating the annual interest rate to be disclosed under those two sections.

It is indeed true that, so far as the harmonization of ccdl is concerned, sections 4 and 6 are the two crucial sections of the *Interest Act*. By repealing those two sections and replacing them with a broad regulation-making power (and then passing the appropriate regulations), the federal government could harmonize the *Interest Act* with other ccdl and accomplish most of what was intended to be accomplished through the PIA.(9) Unfortunately, I believe that the federal government's proposed amendments to sections 4 and 6 do not really address those sections' fundamental problems, nor do the amended sections create a broad enough regulation-making power to permit the sort of regulations that are necessary to make the *Interest Act* a truly useful complement to general-purpose ccdl.

The amendments are contained in Bill C-88, the *Agreement on Internal Trade Implementation Act*, which received second reading on May 29. Section 17 of the Bill amends sections 4 and 6 of the *Interest Act* to read as follows (the amended parts are in bold print):

4(1)Except as to mortgages on real property, whenever any interest is, by the terms of any written or printed contract, whether under seal or not, made payable at a rate or percentage per day, week, month, or at any rate or percentage for any period less than a year, no interest exceeding the rate or percentage **prescribed by regulation** shall be chargeable, payable or recoverable on any part of the principal money unless the contract contains an express statement of the yearly rate or percentage of interest to which the other rate or percentage is equivalent, **calculated in accordance with the regulations.**

(2)The Governor in Council may make regulations for the purposes of subsection (1).

6(1)Whenever any principal money or interest secured by mortgage on real property is, by the mortgage, made payable on a sinking fund plan, on any plan under which the payments of principal money and interest are blended or on any plan that involves an allowance of interest on stipulated repayments, **or on any fund or plan described in the regulations**, no interest whatsoever shall be chargeable, payable or recoverable on any part of the principal money advanced, unless the mortgage contains **an express** statement showing the amount of the principal money and the rate of interest chargeable **on that money**, calculated **in accordance with the regulations**.

(2)The Governor in Council may make regulations for the purposes of subsection (1).

Obviously, the amendments would preserve most of the text _ and most of the problems _ of the present sections 4 and 6.

After Bill 88 received first reading, I wrote to the Department of Finance and pointed out that the amendments to section 4 and 6 failed to address many of the problems presently associated with those sections. I argued that sections 4 and 6 could be combined in a single section that gives the Governor in Council a broad power both to define the classes of contracts to which the regulation would apply and to prescribe the method of calculating and disclosing interest for such contracts. I have not received a response to my letter.

C. Issues of Process

Suggested Process for Finalizing Uniform Act There is no doubt that the AIT and the role of the CMC in implementing the AIT's commitment to harmonization complicates things for the ULCC. Obviously, the AIT-related process wrought havoc with the ULCC's timetable for adopting a uniform act. But timetable considerations aside, there is a question of how far, if at all, the ULCC should defer to other organizations on the resolution of contentious issues that affect the content of the CCDA (as finally adopted by the ULCC). Should the ULCC reach its own conclusions about the appropriate approach to various contentious issues and adopt a CCDA that reflects those conclusions, regardless of whether those who are ultimately responsible for implementing the AIT's commitment to harmonization are likely to reach the same conclusions? Or should the ULCC attempt to convince those who have the final say of the wisdom of the ULCC's conclusions on contentious issues, but ultimately adopt a CCDA that implements the conclusions of those who have the final say on the contents of harmonized ccdl? I believe that the latter is a more constructive approach and should be adopted by the ULCC.

Later, this memorandum briefly discusses and makes recommendations about a number of substantive issues regarding the content of harmonized ccdl. For the most part, these are issues that arise out of the CMC Consultation Paper. These are issues where I have serious concerns about the utility or practicality of the approach proposed by the Consultation Paper. It would be useful for the Uniform Law Section to discuss these issues and decide whether to recommend that the CMC reconsider its position on them. Having made these recommendations, however, the Section would acknowledge that on certain issues, such as the APR issue, the CCDA might not reflect the approach favoured by the ULCC.

Recommendation 1

1.1The ULS should consider and reach a position on the substantive issues identified in this memorandum or raised for discussion at the Conference.

1.2The ULS's position on the substantive issues should be communicated to the CMC working group by the committee referred to in Recommendation 1.3.

1.3The ULS should delegate a committee to communicate with the CMC and to finalize the text of the Uniform Cost of Credit Disclosure Act ("UCCDA") by not later than January 15, 1996.

1.4The UCCDA should implement the final agreement of the parties to the AIT regarding the content of harmonized cost of credit disclosure legislation, even where this does not reflect the preferred approach of the ULS.

1.5The UCCDA should be circulated to all jurisdictions as soon as possible after January 15, 1996. Unless two or more objections are received by the Executive Director of the Conference by February 28, 1996, the UCCDA should be taken as adopted as a Uniform Act and recommended to the jurisdictions for enactment, and the text should appear in the 1995 Proceedings.

II SUBSTANTIVE ISSUES

The issues identified below do not constitute an exhaustive list of all the issues arising out of the CMC's Consultation Paper or CCDA 4.1 that might be worthy of discussion. The issues mentioned below are those that seem particularly important for the Uniform Law Section to consider, with a view to making recommendations to the CMC or confirming or changing CCDA 4.1's approach to certain issues. In identifying issues for discussion, I have been mindful of the limited amount of time that will be available for discussion of ccdl at the Conference. Of course, delegates are encouraged to review the CMC Consultation Paper and CCDA 4.1 and raise for discussion any additional issues they believe should be considered during the Conference.

The following discussion does not raise issues that are incidental to the working group's proposal to require disclosure of the APR for fixed credit. For example, there is no discussion of how the APR should be calculated or what sorts of charges ought to be included in the APR. These are crucial issues if you are going to require APR disclosure. They are also complex. Given that for the past few years the ULS has been advocating an approach that does not involve APR disclosure, and that it continues to advocate such an approach, I do not think it is necessary or appropriate at this stage of the project for the ULS to immerse itself in the mechanics of APR disclosure.

A. The APR Approach Versus the AIR Approach

As mentioned earlier in this memorandum, the CMC working group proposes that harmonized ccdl should continue to require lenders to calculate and disclose the APR for

fixed loans. In contrast, the ULCC has proposed the AIR approach, which would require lenders to disclose the AIR and dollar amount of non-interest charges, and would place express limits on the types of non-interest charges that can be imposed by lenders.

It is worth emphasizing that the ULCC's approach is not based on the premise that the APR is a useless piece of information in consumer credit transactions. In many cases, knowing the respective APRs for two alternative loan arrangements could help a consumer decide which loan is really less expensive. However, it is one thing to acknowledge that the APR may be a useful piece of information and another to argue that lenders should be required to disclose the APR for their loans. One of the arguments in the APR Paper is that there may be more efficient means of conveying the APR for loans to consumers than by requiring lenders to calculate and disclose the APR.

I am convinced that the AIR approach is a better approach than the APR approach. The reasons for that conclusion are set out in the APR Paper. Since the APR Paper is a 60-page document, it would be rather difficult to describe its arguments in this memorandum, and I will not attempt to do so. The APR Paper is available and speaks for itself. In any event, I do not think that it would be especially productive for the ULS to engage in another discussion of the relative merits of the contending approaches. The ULS decided a couple of years ago (at least) to reject the APR approach in favour of the AIR approach, and the reasons that were advanced for doing so are as valid now as they were then. I would suggest that the ULS simply confirm that it continues to be of the view that the AIR approach is a superior alternative to the APR approach.

Taken on their own, I doubt that any further arguments the ULCC might make regarding the relative merits of the AIR approach and the APR approach would persuade the CMC working group to change its position on this fundamental issue. However, based on the responses we have received to our own consultation, I would not be surprised if the working group's consultation process reveals substantial support for the AIR approach. I would assume that such support, combined with whatever arguments are advanced by the ULCC, would influence the final decision on this issue. Thus, I think it is important to affirm that the ULCC is unrepentant on this issue.

Recommendation 2

The ULS should confirm its support for an approach to cost of credit disclosure that does not require lenders to disclose an APR for fixed loans, but which contains the following elements:

(a) disclosure of the annual interest rate;

(b) disclosure of the dollar amount of non-interest charges;

(c) express restrictions on the types and number of non-interest charges that may be imposed in connection with consumer loans.

B. Restrictions on Non-Interest Charges Under AIR Approach

The issues discussed in this section arise out of the AIR Approach, rather than out of anything proposed in the Consultation Paper.

As you know, express restrictions on non-interest charges are a key element of the AIR approach. The restrictions serve two broad purposes. The first is to ensure the usefulness of the annual interest rate as a measure of the cost of credit. It does so by making it difficult for lenders to state misleading interest rates by loading a large chunk of the cost of borrowing into non-interest charges. The second purpose of the restrictions relates to prepayment of loans. Here the CCDA's restrictions on non-interest charges are designed to make it difficult to for lenders to load an unduly large portion of the total cost of borrowing for a loan into "front-end" charges, which would largely negate the advantage to consumers of prepaying such loans.

We have received many comments on the proposed restrictions on non-interest charges. As mentioned earlier, a few commentators have objected to the whole concept of placing restrictions on non-interest charges. However, most commentators have focused on the issue of how, rather than whether, ccdl should restrict non-interest charges. Most of the discussion has focused on the concept of the permitted flat charge for fixed loans.

Flat Charges In the CCDA's terminology, a flat charge is a charge that is the same for all loans within a certain category. Lenders would be allowed to impose flat charges in connection with fixed loans. Although neither CCDA 3.2 nor CCDA 4.1 expressly ties flat charges to any particular expense incurred by the lender, the rationale for allowing lenders to impose a flat charge is that imposing such a charge is the most efficient and accurate way for a lender to recover internal costs that do not vary with the size and duration of a loan.

Under CCDA 3.2, for the purpose of setting the amount of their flat charges for loan categories, each lender would have been free to categorize its loans according to any criteria the lender considered relevant. But there was one constraint: a lender could use the amount of the loan as a criterion for categorizing loans only if this reflected a material difference in the procedure (and, hence, the cost) for setting up loans in the different categories. In other words, a lender would have to charge the same flat charge for loans which differed only in their amount, unless this difference was reflected in a different procedure for setting up the loans or administering them.

The comments on CCDA 3.2's approach to flat charges fall into four rough categories. First, there were commentators who thought that lenders should not be allowed to impose a flat charge at all. Second, there were commentators who thought that if flat charges were permitted, they should be subject to explicit monetary caps to ensure that the charges are "nominal" and do not significantly affect the cost of borrowing. (10) Thirdly, some commentators thought that the restrictions on flat charges, or the permitted methods of categorizing loans, were too restrictive. Finally, there were even some commentators who thought that CCDA 3.2's restrictions on flat charges were quite reasonable.

When I was writing the APR paper, it was apparent that the main concern of some CMC working group members was that CCDA 3.2's approach would give some lenders too much scope for inflating the flat charge, thereby making the annual interest rate unreliable as a measure of the relative cost of credit. To address this concern, the APR paper suggested that permitted flat charges might be explicitly tied to lenders' cost of setting up and administering loans. The suggested provision read as follows:

(X) The flat charge for any category of fixed loan must not exceed the lender's reasonable estimate of the approximate cost of setting up and administering, or renewing and administering, a typical loan within the relevant category.

(Y) For the purpose of subsection (X), the cost of setting up, renewing or administering a loan does not include

(a) any cost that depends on the amount and duration of the loan;

(b) any cost that is recovered otherwise than through a flat charge.

I was concerned that this restriction on flat charges might be viewed as too restrictive, but I anticipated that it would meet the objection that the definition of permitted flat charge in CCDA 3.2 would allow lenders to inflate flat charges. However, some members of the working group were concerned that this formulation would still allow lenders to impose non-interest charges that would distort the cost of borrowing.

CCDA 4.1 does not incorporate provisions "X" and Y" set out above. In fact, section 8 of CCDA 4.1 is much closer to the corresponding provision in CCDA 3.2 than it is to provisions X and Y. Strictly speaking, section 8 of CCDA 4.1 is less restrictive than section 8 of CCDA 3.2, because the former removes any constraints on how lenders may categorize loans for the purpose of setting flat charges. The only official constraints on the creation of loan categories are the disclosure and record-keeping requirements of section 8. The lender must keep a record of its loan categories and the flat charge imposed within each category, and must disclose to **any person** who requests such information how the lender categorizes its loans and the flat charge for each category of loan. In other words, CCDA 4.1 imposes no explicit or implicit restrictions on the amount of flat charges for any given category of loans but attempts to ensure that those charges will be as transparent as possible. Like CCDA 3.2, CCDA 4.1 would authorize regulations placing explicit monetary limits on flat charges for specific types of loan, but such regulations are viewed as a backstop.

Recommendation 3

The ULS should confirm its support for the approach to flat charges embodied by CCDA 4.1 section 8, which contains the following elements:

(a) every lender should be free to categorize loans for the purpose of setting flat charge according to whatever criteria the lender considers relevant;

(b) lenders should be required to keep a record of their loan categories and the flat charges for each category;

(c) lenders should be required to disclose to any person who requests such information their loan categories and the flat charges for each category;

(d) the CCDA should not impose monetary limits on flat charges, but should authorize regulations to that end.

Required Payments to Third Parties Section 6(3)-(4) of CCDA 4.1 is based on a provision that was proposed and explained in the 1994 Memorandum. Essentially, the purpose of this provision is to prevent lenders from getting around the restrictions on non-interest charges(11) by requiring the borrower to make a payment to a third party. Time constraints during the 1994 Conference did not allow for a discussion of this provision, so I mention it here to draw delegates' attention to its inclusion in CCDA 4.1.

Recommendation 4

The ULS should confirm its support for the restrictions on mandatory payments to third parties set out in section 6(3)-(4) of CCDA 4.1.

Refund of Certain Non-Interest Charges on Prepayment of Loan under CMC Approach

Although CCDA 3.2 placed express restrictions on non-interest charges, there was only one circumstance in which CCDA 3.2 would have required a lender to refund a permitted non-interest charge that had been properly imposed. This was where the borrower withdrew a loan application or paid off a loan within two business days after receiving the initial disclosure statement. The borrower would then be entitled to a refund of any flat charge paid prior to the withdrawal or prepayment.(12) The purpose of this cooling-off period was to give the borrower a chance to evaluate the information in the disclosure statement before being irrevocably committed to paying a flat charge. Once the cooling-off period had expired, however, a borrower who prepaid a loan would not be entitled to a rebate of any portion of a flat charge paid at the beginning of a loan. If the borrower paid a $50 administration fee at the outset of a one-year loan but repaid the loan after six months, the $50 would be gone.

For prepayment purposes, the CMC Consultation Paper divides non-interest charges into two broad classes: non-refundable charges and refundable charges. The former class includes disbursement charges, brokerage fees and the "rebate-not-taken" under a rebate or low-rate financing ("RLRF") program.(13) The latter class includes all other non-interest charges. Thus, any lump-sum charge, such as application fee or administration fee, imposed at the beginning of a fixed loan is partially refundable upon a prepayment, unless the charge relates to a specific external expense incurred by the lender and passed on to the borrower. If the lender imposes a $50 fee to cover its internal costs of setting up a loan, half of that fee would be refundable if the borrower prepays the loan half-way through the term.

During the CMC working group meetings I argued that if a charge imposed at the beginning of a loan relates to an expense incurred by the lender at the outset of the loan, it is reasonable for the lender to retain the relevant payment even when the loan is prepaid. It

should not matter whether the expense is incurred internally or externally. Whether internal or external, it is incurred by the lender even if the loan is prepaid, so it is difficult to discern the principle upon which the charge should be refunded upon a prepayment. Moreover, if forced to refund a portion of such charges to borrowers who prepay, lenders will have to recover the relevant expenses from other borrowers. Thus, the policy of requiring lenders to refund charges that may relate to expenses already incurred by the lender at the time of a prepayment amounts to a cross-subsidization of borrowers who prepay by borrowers who pay their loans according to the agreed schedule.

I do not think that the CMC working group raise any objection, in principle, to lenders retaining charges that relate to expenses they have already incurred at the time a loan is prepaid. However, it was concerned that, for prepayment purposes, it would be too difficult to distinguish between the portion of an "administrative charge" that genuinely relates to expenses already incurred by the lender and the portion that is more accurately characterized as unearned cost of borrowing. Therefore, to avoid having to make this distinction, the Consultation Paper proposes to require a proportionate refund of all non-interest charges other than disbursement charges and brokerage fees. However, I am not convinced that a policy of allowing lenders to retain non-interest charges that cover internal expenses incurred before a loan is prepaid will undermine the policy that borrowers who prepay loans should not have to pay the portion of the cost of borrowing that has not been earned at the time of the prepayment. The two policies can co-exist if a mechanism is provided that ensures that front-end charges bear a reasonable relationship to front-end expenses. CCDA's flat charge mechanism is intended to fulfil this function.

Recommendation 5

The ULS should recommend that, except for privileges under a "cooling-off" period following the delivery of a disclosure statement, when a borrower prepays a loan a lender should not be required to refund any charges that cover internal or external expenses incurred by the lender before the loan is prepaid.

D. RLRF Programs

You will recall that there has been an ongoing debate as to the most appropriate method of dealing with RLRF programs in harmonized ccdl. Sections 14 and 14.1 of CCDA 3.2 represent alternative approaches to such programs. Section 14 would essentially have required that anyone who gives a rebate to cash customers give the same rebate to credit customers.

Section 14.1 would have drawn a distinction between rebates offered by the seller of merchandise and rebates offered by third persons (i.e. a manufacturer who does not sell the goods directly to consumers). Section 14.1 would have taken the same approach as section 14 to rebates offered by sellers; any rebate given to cash customers would also have to be given to credit customers. Otherwise, sellers could easily use the device of rebates to completely undermine restrictions on non-interest charges and the usefulness of the AIR as a measure of the relative cost of credit. For example, the proprietor of Joe's Used Furniture could make offers like this:

Cash customers: Buy this sofa for $500 and get a $100 rebate. Credit customers: buy this sofa for $500 and get 0% financing for 1 full year.

Of course, Joe would really be selling the chair for $400 and disguising the cost of borrowing as a rebate given to cash customers. Section 14.1 would require Joe to give the rebate to credit customers as well as to cash customers, so the initial outstanding balance on the supplier loan would be $400. If Joe wants to collect interest, he would have to reveal the interest rate as an interest rate.

Section 14.1's approach is different where a third party offers the rebate. A rebate offered to cash customers must also be **offered** to credit customers, but it can be offered as an **alternative** to low-rate financing. In other words, a manufacturer could offer credit customers a choice between (1) a rebate and financing at the going market rate and (2) no rebate (or a smaller rebate) and low-rate financing. A print advertisement that offered credit customers such a choice would have to include a table setting out comparative payment information for each of the alternatives, based on a representative transaction.

Most commentators who commented on the alternative provisions in CCDA 3.2 expressed a preference for the approach of section 14.1. Most commentators thought that the comparative payment table contemplated by section 14.1 would allow consumers to make a reasonably informed choice between the two alternatives. Given the strong support for section 14.1, section 15 of CCDA 4.1 is based on section 14.1 rather than section 14 of CCDA 3.2. As compared to section 14.1 of CCDA 3.2, section 15 contains several cosmetic modifications and two substantive modifications. The first substantive modification is in section 15(5)(i), which requires an additional item of information in the comparative table. This is a statement of how much the borrower would have to pay to prepay the loan half-way through its term under each alternative. This is intended to give prospective customers some idea of the negative implications for prepayment of choosing the low-rate alternative over the rebate alternative (assuming the rebate would be applied to reduce the initial loan balance).

The second substantive modification is found in section 15(2). It provides that the requirement for a comparative table does not apply to a radio or television advertisement if the ad refers to a contemporaneous newspaper advertisement where the relevant information can be found.

It should be noted that the special disclosure requirements in section 15 of CCDA 4.1 only deal with advertisements. There is no provision in CCDA 4.1 that would impose special disclosure requirements at the time a consumer enters into a low-rate financing arrangement and foregoes a rebate. Arguably, the disclosure statement for such a transaction should contain the same type of comparative table that would have to be provided in an advertisement. One possible drawback of such a requirement is that it might be more challenging for a seller (e.g. a car dealer) to provide a comparative table for a specific transaction than for an advertiser to provide a comparative table for a representative transaction. Presumably, the necessary calculations would be done by a computer, but the seller would have to be careful to enter the correct data not only for the

actual transaction (with low-rate financing), but also for other option (a rebate and regular-rate financing).

Since the CMC working group is proposing to require lenders to disclose the APR for fixed credit, it must address an issue that does not arise under the AIR approach. Should the rebate foregone by a credit customer in order to get low-rate financing be counted as part of the cost of borrowing and be taken into account in calculating the APR for the relevant credit arrangement? The working group has proposed that it should. This approach will almost certainly be controversial, because it is the approach that has already proved to be controversial under some provinces' existing legislation. It must be said, however, that if you are going to require disclosure of the APR for fixed credit, it seems logical to require the amount of the rebate-not-taken to be included in the APR for the low-rate loan.

Recommendation 6

6.1The ULS should confirm CCDA 4.1's approach to RLRF programs, which consists of the following major elements:

(a) Sellers should be required to give the same rebate to credit customers that they give to cash customers.

(b) A person other than the seller (such as a manufacturer or its "captive" finance company) should be able to offer credit customers a choice between a rebate and low-rate financing.

(c) Any print advertisement relating to a RLRF program should contain a table setting out comparative payment information for the two options.

(d) The comparative payment information should include the amount that would be outstanding under each alternative if the loan were to be prepaid at some point during the term of the loan.

(e) A radio or television advertisement regarding a RLRF program need not contain the comparative table of payment information if it refers to a concurrently published newspaper advertisement.

6.2 The ULS should consider whether the same comparative payment information that must be provided for advertisements should also be provided in the disclosure statement for a specific transaction in which the customer foregoes a rebate in favour of low-rate financing.

E. Timing of Disclosure

Non-Mortgage Loans CCDA 3.2 sections 24 and 27 provided a two day "cooling-off period" following a consumer's receipt of the disclosure statement for a supplier loan or non-mortgage cash loan. If the consumer withdrew the loan application or prepaid the loan (presumably with funds provided by another lender at a better rate), the borrower would have been entitled to a refund of any flat charge paid by the borrower in connection with the loan. As mentioned earlier, the purpose of this provision was to give the borrower a reasonable opportunity to evaluate the information in the disclosure statement and possibly obtain equivalent (but cheaper) financing elsewhere.

Commentators' comments on these sections ranged from very negative to mildly positive. One commentator thought that in the context of supplier credit transactions (e.g. conditional sales contracts) it would be more useful to provide consumers with a real cooling-off period, during which they could cancel the entire transaction without liability.(14) On the other hand, some commentators thought this provision was too generous. They thought lenders should be compensated for thrown-away expenses, whether internal or external, when a borrower withdraws from a credit arrangement after receiving the disclosure statement.

The CMC working group concluded that, in the context of non-mortgage credit, it is unnecessary to give consumers the sort of cooling-off period contemplated by CCDA 3.2. In the context of their proposals regarding prepayment of non-mortgage loans, the working group's conclusion on this point seem correct. As discussed earlier, the working group has proposed that a borrower who prepays a non-mortgage loan should be entitled to a proportionate refund of all non-interest charges other than disbursement charges or brokerage fees. Under this general proposal, a borrower who prepaid a loan a few days after it was advanced would be entitled to a refund of virtually the whole of any administration charge imposed at the outset of the loan. A cooling-off period along the lines of the one provided by CCDA 3.2 would be redundant where consumers have the generous prepayment right proposed by the CMC working group.

In accordance with the working group's proposals, CCDA 4.1 has eliminated the cooling-off periods for non-mortgage loans. However, CCDA 4.1's general prepayment right for non-mortgage loans is not as generous as that proposed by the working group, in that CCDA 4.1 would not provide for a proportionate refund of a properly imposed flat charge. (15) It is certainly arguable that given the difference in the general prepayment rights afforded by CCDA 4.1 and the CMC Consultation Paper, CCDA 4.1 should have retained the same sort of cooling-off period for non-mortgage loans that was contemplated by CCDA 3.2.

Recommendation 7

The ULS should consider whether borrowers should have a "cooling-off" period after receiving a disclosure statement for a non-mortgage loan, as contemplated in CCDA 3.2. If during the cooling-off period a consumer either withdrew the credit application (if the loan had not already been advanced) or prepaid the loan in full, the consumer would not be liable for any non-interest charges other than disbursement charges for expenses already incurred by the lender.

Brokered Loans CCDA 3.2 section 12 required a loan broker to provide the borrower with a brokerage fee disclosure statement on or before the day the borrower received the lender's disclosure statement. The brokerage fee disclosure statement would disclose the dollar amount of the brokerage fee as well as the APR for the loan.(16) A borrower who withdrew the loan application or paid off the loan within the cooling-off period would not be liable for the brokerage fee.

The working group proposes more onerous disclosure requirements for brokers than were proposed in CCDA 3.2. The Consultation Paper proposes that a broker be required to

provide a preliminary disclosure statement ("PDS") and a final disclosure statement ("FDS"). The PDS would have to be given to the borrower when the borrower applies for the loan and before the borrower incurs any obligations or makes any payments in connection with the prospective loan. The PDS would have to contain information such as the amount and term of the loan, the maximum interest rate, the brokerage fee, the APR and the target date for obtaining a written commitment from a lender to provide a loan on terms at least as favourable as those set out in the PDS. If the broker does not obtain such a commitment by the target date, the borrower would not be liable for any portion of the brokerage fee.

The timing and consequences of the FDS would depend on whether the loan is a mortgage loan or non-mortgage loan. For a mortgage loan, the Consultation Paper proposes that the broker be required to provide a FDS at least 14 days before the loan is advanced, although the borrower could waive this right "on the advice of an independent professional stipulated by regulation". This would tie in with the working group's proposal regarding the timing of delivery of disclosure statements for mortgage loans generally. The Consultation Paper does not expressly discuss what happens if the borrower declines the mortgage loan after receiving the disclosure statement. Presumably, the working group intends that the borrower would not be liable for the brokerage fee if the borrower declines the mortgage within a certain period (a day or two) after receiving the disclosure statement. Otherwise, it would be difficult to see any point in requiring the broker to provide the FDS 14 days before the loan is advanced.

For a non-mortgage loan, the FDS must be given before the borrower incurs any obligations under the loan. The Consultation Paper says that "a borrower who prepays a non-mortgage loan within 24 hours of receiving the [final] disclosure statement from the broker should not be liable for the brokerage fee." Presumably, this is intended to apply not only where the borrower prepays the loan, but also where the borrower declines to accept the loan after seeing the disclosure statement.

I am not sure that the working group has a firm idea of exactly how its proposed approach would work in practice. I certainly do not. In particular, I am unclear as to the exact relationship between the PDS and the CDS. My questions about the proposed approach include but are not limited to the following:

1. Suppose that a broker provides a PDS, but does not provide a written commitment from a lender until a few days after the target date set out in the PDS. Despite the broker's tardiness, the borrower is prepared to accept the loan, and in fact does so. The Consultation Paper says that if the broker does not provide a written commitment by the target date, the borrower should not be liable for any portion of the brokerage fee. Does the broker's failure to deliver a commitment by the target date mean the broker cannot receive a brokerage fee from the borrower even if the latter accepts and receives the loan? Or can the broker still receive a brokerage fee so long as the borrower receives the FDS and accepts the loan. The latter approach seems reasonable, but it would then appear that the broker's failure to deliver a signed commitment by the target date would have no discernible legal consequences.

2. On a similar note, suppose the broker is unable to arrange a loan on terms as favourable as those set out in the PDS (perhaps because a credit check reveals that the borrower does not have a stellar credit record) but is able to arrange a loan on less favourable terms. If the borrower is prepared to accept a loan on the less favourable terms, is the broker nevertheless prohibited from receiving a brokerage fee for arranging that loan, because its terms are less favourable than those set out in the PDS?

3. How is it determined whether the terms of the loan arranged by the broker are as favourable as the terms set out in the PDS? For example, if the PDS refers to a 3-year loan at an APR of 12% and the broker ultimately arranges a 2-year loan at an APR of 10%, are the terms of the actual loan more or less favourable than those set out in the PDS?

Recommendation 8

The ULS should recommend that the CMC working group consider whether the proposed disclosure requirements for loans arranged by brokers, especially the requirements regarding a "preliminary disclosure statement" are clear and practical.

Renewals CCDA 3.2 section 33 provided that a lender who was willing to enter into a renewal agreement [for a balloon payment loan] had to provide the borrower with a disclosure statement at least 15 days before the end of the term of the existing agreement. The renewal statement would have to provide information such as the interest rate and the amount of the periodic payments, and could provide this information for several different renewal options. A couple of commentators thought that the requirement to provide advance disclosure of the renewal terms was onerous or impractical. One of these commentators argued that the lender could be locked in to a below-market rate if rates rose between the time the disclosure statement was delivered and the actual renewal date. But if silence can be interpreted as agreement, most commentators seemed to agree with the approach taken by CCDA 3.2.

The Consultation Paper's approach to renewal statements is similar to CCDA 3.2's with a few important differences:

*The lender would be required to provide the disclosure statement **sixty** days before the renewal date.

*The interest rate quoted in the renewal statement would be the current interest rate as of the date of the disclosure statement, and the statement could indicate that the rate is subject to change.

*The renewal statement would have to contain "the same categories of cost information as the disclosure statement for the loan."

*A lender who did not intend to renew a loan would be required to so advise the borrower at least sixty days before the end of the term.

*If the lender did not provide the renewal statement at least 60 days in advance of the renewal date, the loan would be prepayable without penalty at any time within 60 days of when the disclosure statement is delivered to the borrower.

My main concern with the working group's proposals relates to the timing of the disclosure statement. I do not think it would be reasonable to require lenders to offer a firm interest rate at least 60 days before the renewal date. The general level of interest rates could change quite considerably over a 60 day period. Therefore, if the lender is required to deliver the disclosure statement 60 days before the renewal date, then I believe it is necessary _ as the working group proposes _ to allow the lender to quote a rate that is subject to change. In my view, however, consumers would be better off getting a firm rate two weeks before the renewal date than getting a rate that is subject to change sixty days before the renewal date.

Recommendation 9

The ULS should recommend that the CMC working group reconsider whether the proposal to require lenders to provide a disclosure statement 60 days before the renewal date will actually be more beneficial to consumers than a requirement to provide a disclosure statement with firmer information a shorter period (such as 15 days) before the renewal date.

APPENDIX 1
CCDA 4.1 COMPARED TO
CMC CONSULTATION PAPER

This Appendix briefly summarizes the similarities and major differences between CCDA 4.1 and the proposals in the CMC's draft Consultation Paper. As mentioned in the main body of this memorandum, the steering committee decided that CCDA 4.1 should continue the existing AIR approach, which does not require lenders to calculate and disclose an APR for their loans. This is the one area in which it was consciously decided that CCDA 4.1 should not implement the proposals of the CMC Consultation Paper. This decision affects a number of provisions throughout CCDA 4.1 In addition to APR-related differences, there are a few other subjects upon which no attempt was made to bring CCDA 4.1 into conformity with the working group's proposals. In most cases this was because the working group had not reached a firm position on the relevant issue by the time CCDA 4.1 was completed.

The following analysis proceeds on a section-by-section basis through CCDA 4.1, but is not a detailed analysis. It simply indicates in general terms the extent to which each section is consistent or inconsistent with the proposals in the Consultation Document.

In many cases there is a statement that the section implements a specific proposal of the working group. It should be kept in mind that the provisions of the CCDA are almost invariably more detailed than the proposals that they implement. So even where a section of CCDA 4.1 "implements a specific proposal" of the Consultation Paper, the former is likely to deal with certain details that the latter does not address.

Unfortunately, the draft Consultation Paper does not number its proposals, so I have been unable to provide cross-references to these proposals. I have not even included page

number references to the proposals, because I suspect that the page numbers in the draft Consultation Paper will not be the same as the page numbers in the final version.

Part 1 - Application

Section 1 - Definitions

*The definitions in CCDA 4.1 are not directly affected by the proposals in the Consultation Paper.

Section 2Persons considered to be associates of each other

*The Consultation Paper uses the term "associate of a lender" but does not purport to define it. Presumably, this definition is along the lines of what the Consultation Paper has in mind.

Section 3 - Application

*This section is consistent with but more detailed than the Consultation Paper. All the latter says regarding application is that harmonized legislation will deal with loans to individuals for non-business purposes.

Section 4 - Loans arranged by broker

*This section is consistent with the Consultation Paper, but the subject of the section is not specifically addressed by the Consultation Paper.

Part 2 - General

Section 5 - Cancellation of optional services

*This section implements a specific proposal of the Consultation Paper.

Section 6 - Restriction of non-interest charges

*This section limits non-interest charges to the categories it identifies, and would be eliminated under the approach proposed in the Consultation Paper. The Consultation Paper's approach would substitute implicit limitations for explicit limitations.

Section 7 - Permitted disbursement charges

*The Consultation Paper uses the concept of disbursement charges, although not in quite the same way as CCDA 4.1. Although all non-interest charges, including disbursement charges would have to be included in the APR for a loan under the working group's proposals, disbursement charges would enjoy a special status in the context of prepayments. Unlike other non-interest charges, disbursement charges are not refundable or rebateable on a prepayment.

Section 8 - Permitted flat charges

*The Consultation Paper does not use the concept of a flat charge, so this section would be eliminated under the approach proposed in the Consultation Paper.

Section 9 - Permitted prepayment charges

*This section is consistent with the approach proposed in the Consultation Paper, which is that non-mortgage loans should be prepayable without penalty, and that mortgage loans should be governed by the *Interest Act*.

Section 10 - Prepayment of non-mortgage loans

*This section is consistent with the proposals of the working group regarding prepayment of non-mortgage loans. However, an additional provision would be required to deal with the following aspects of the working group's proposals:

*Exactly what non-interest charges are partially refundable when a loan is prepaid?

*How is the refundable portion of a non-interest charge calculated?

Section 11 - Permitted default charges

*This section, with the possible exception of subsection (1)(c) implements a specific proposal of the working group.

*The Consultation Paper makes no mention of charges for dishonoured payments (an "NSF Charge"), but I believe this could be an oversight, rather than a conscious decision by the working group that such charges should not be allowed.

Section 12 - Brokerage fees

*This section is intended to implement the working group's proposals regarding brokerage fees. However, the draft Consultation Paper does not appear to address the issue addressed by the last part of section 12(2): the circumstances in which a brokerage fee may be imposed. This issue was discussed by the working group, and I believe that section 12(2) represents the decision of the working group, even if the decision is not recorded in the Consultation Paper.

Section 13 - Determination of outstanding balance

*This section deals with some technical issues that are not specifically addressed by the Consultation Paper. It is consistent with the approach proposed by the CMC working group.

Section 14 - Definitions

*These definitions are not affected by the Consultation Paper.

Section 15 - Rebates and discounts

*This section is **not** consistent with the approach proposed by the working group. To accommodate the Consultation Paper's proposals, this section would have to be rewritten to require that any rebate not taken by the credit customer be included in the APR.

Section 16 - Disclosure where payment waived

*This section implements a specific proposal of the working group.

Section 17 - Form of disclosure

*This section implements a specific proposals of the working group, except that the point addressed by subsection (3) is not addressed by the Consultation Paper.

Section 18 - Estimates in disclosure statements

*This section implements a specific proposal of the working group.

Section 19 - Disclosure of timing of payments and advances

Section 20 - Delivery of disclosure statements

Section 21 - Multiple borrowers

*These sections deal with technical issues that are not addressed by the Consultation Paper.

Section 22 - Disclosure of brokerage fee

*This section is **not** consistent with the Consultation Paper's approach to disclosure by brokers. This is partly because the working group had not reached a firm position on disclosure by brokers by the time CCDA 4.1 was completed. However, even if the Consultation Paper had been finalized before CCDA 4.1 was completed, the former's position on disclosure by brokers might have been too uncertain to implement in the draft act.

Part 3 - Fixed Credit

Division 1 - Disclosure Relating to Interest Rate

Section 23 - Application of this Part

*This section is not affected by the Consultation Paper

Section 24 - Interest rate information

*This section deals with the interest rate information that must be provided for a constant-rate loan (the easy case) and for loans in which the interest rate may vary during the term of the loan. This section is consistent with the Consultation Paper but deals with the subject in more detail.

Section 25 - Payment disclosure where interest rate is variable

*This section is consistent with the Consultation Paper.

Division 2 - Advertisements

Sections 26 - 29

*These sections are inconsistent with the Consultation Paper to the extent that the latter requires disclosure of the APR whenever an advertisement mentions any specific information about the cost of borrowing. As well, references in these provisions to disclosing the amount of flat charges are not consistent with the APR approach advocated by the Consultation Paper.

*Apart from the fact that they do not require disclosure of an APR, these sections are generally consistent with the Consultation Paper's proposals.

*Unlike the Consultation Paper, this Division does not set out special (less onerous) disclosure requirements for radio and television advertisements. The disclosures required by this Division are not so onerous as to be inappropriate for radio or television advertising.

Division 3 - Supplier Loans

Section 30 - Simplified disclosure for certain supplier loans

*This implements a specific proposal of the working group.

Section 31 - Supplier Loans Generally

*For the most part, this section implements specific proposals of the Consultation Paper. Where it does not implement specific proposals, it is consistent with the working group proposals except, except as noted below.

*This section does not require disclosure of the APR.

*CCDA 4.1 does not have a specific requirement to disclose the date from which interest begins to accrue, as was provided by CCDA 3.2 and proposed by the working group. This provision should have been included in CCDA 4.1.

*CCDA 4.1 omits a few disclosure items that are mentioned in the consultation paper but which seem unnecessary. For example, the Consultation Paper requires disclosure of "the method of calculating any rebate on the cost of borrowing if the borrower makes a prepayment". Since the Consultation Paper proposes a statutory formula for calculating the amount of such a rebate, it seems pointless to set it out in a disclosure statement.

Division 4 - Cash Loans

Section 32Timing of disclosure for non-mortgage loans

*This section implements a specific proposal of the Consultation Paper.

Section 33 - Timing of disclosure for mortgage loans

*This section implements a specific proposal of the Consultation Paper but is more detailed.

*There is one point upon which this section and the draft Consultation Paper are inconsistent, but I think it is because of an error in the latter. Section 33(2) gives the borrower two business days after receiving the during which to decide whether to accept the loan or not. If the borrower declines the mortgage during that period, the borrower is not liable for non-interest charges other than disbursement charges relating to expenses already incurred by the lender. The draft Consultation Paper takes a similar approach, but it does not attach any specific consequences to delivery of the disclosure statement. It does not purport to give the borrower a short period after receiving the disclosure statement during which the borrower can decline the loan and avoid certain non-interest charges. The Consultation Paper makes the time at which the borrower signs "the agreement"

(presumably, the mortgage), the critical time. Given that the borrower might well sign the mortgage before getting the disclosure statement, the draft Consultation Paper seems to miss the point of providing the disclosure statement 14 days before the loan is advanced.

Section 34 - Timing of disclosure in special cases

*This implements a specific proposal of the Consultation Paper.

Section 35 - Contents of initial disclosure statement for cash loan

*The preceding comments regarding section 31 apply to this section, as well. For example, this section does not implement the working group proposal to require disclosure of the APR for all fixed loans.

*The disclosure requirements for "readvanceable loans" in section 35(3) implement a specific proposal of the Consultation Paper.

*Section 35(5) provides special disclosure requirements for fixed loans that do not provide a schedule of payments (e.g. a demand loan). The Consultation Paper does not address the possibility that fixed loans will not necessarily have a predetermined schedule of payments.

Division 5 - Subsequent Disclosure

Section 36 - Variable-rate loans

*This section implements a specific proposal of the Consultation Paper.

Section 37 - Supplementary disclosure statement

*This section implements specific proposals of the Consultation Paper, although the draft Consultation Paper seems to contain a substantial drafting error, which I presume will be rectified in the final version.(17)

*Section 37(4) takes a different approach than the Consultation Paper on the issue of what sort of inaccuracies trigger the disclosure requirement. The latter requires a supplementary disclosure statement where the corrected information results in an increase in the APR of at least 1/8 of one percent. That particular trigger is not appropriate under CCDA 4.1, which is not based on APR disclosure. So section 37(4) requires the lender to deliver a supplementary disclosure statement except where the inaccuracy consists of an overestimate of the amount of a disbursement charge.

Section 38 - Renewal agreements

*This section implements a specific proposal of the working group, except that it does not require disclosure of the APR for the renewed loan, as contemplated by the working group.

Part 4 - Open Credit

Section 39 - Application of this Part

*This section is not affected by the Consultation Paper

Section 40 - Simplified disclosure in certain cases

*This section implements a specific proposal of the Consultation Paper.

Division 1 - Open Credit Generally

Section 41 - Advertising for open credit

*Terminology aside ("flat charge"), this section implements a specific proposal of the Consultation Paper.

Section 42 - Initial disclosure statement

*This section implements a specific proposal of the Consultation Paper.

Section 43 - Contents of initial disclosure statement

*This section implements a specific proposal of the Consultation Paper.

Section 44 - Statement of account

*This section implements a specific proposal of the Consultation Paper.

Section 45 - Contents of statement of account

*This section implements a specific proposal of the Consultation Paper.

Section 46 - Notice of changes

*This section implements specific proposals of the Consultation Paper.

Division 2 - Credit Cards

Section 47 - Early disclosure of cost information

*This section implements specific proposals of the Consultation Paper.

Section 48 - No unsolicited cards

*This section implements a specific proposal of the Consultation Paper.

Section 49 - Contents of initial disclosure statement for credit card

*Subsection (1) implements a specific proposal of the Consultation Paper. Subsection (2) does not relate to a specific proposal, but is consistent with the Consultation Paper.

Section 50 - Limitation of liability on loss of credit card

*This section is **not** full consistent with relevant proposal ofthe Consultation Paper. This section limits the borrower's liability to $50 if the borrower reports the loss or theft of the credit card within a reasonable time of discovering it. The Consultation Paper proposes an absolute limit of $50 on the cardholder's liability for unauthorized use of a lost or stolen card. I prefer the approach of section 50.

Part 5 - Leases of Goods

Section 51 - Definitions

*These definitions are not affected by the Consultation Paper.

Section 52 - Application of this Part

*Clause (d) implements a specific proposal of the Consultation Paper, and the rest of the section is consistent with the Consultation Paper.

Section 53 - Advertisements

*This section implements a specific proposal of the Consultation Paper.

Section 54 - Disclosure statement for lease

*This section implements a specific proposal of the Consultation Paper.

Section 55 - Implicit annual interest rate

*This subject of this section is not specifically covered by the Consultation Paper. I assume that if the Consultation Paper had addressed this issue it would have been inconsistent with this section in one respect. The effect of subclause (1)(a)(ii) is to exclude "non-interest" charges from the implicit annual interest rate. I presume that, to be consistent with the APR approach for other forms of credit, the Consultation Paper would have required such charges to be included in the APR for the lease.

Section 56 - Lessee's prepayment right

*This section implements a specific proposal of the Consultation Paper. However, since the Consultation Paper does not employ the concept of a permitted flat charge, some adjustments would be necessary to make the section and the proposals fully consistent.

Section 57 - Guaranteed residual value leases

*This section implements a specific proposal of the Consultation Paper, but the reference in subsection (1) to "realizable value" would have to read "anticipated wholesale value" to make the section fully consistent with the proposal.

Section 58 - Penalties for early termination

*This section implements a specific proposal of the Consultation Paper.

Part 6 - Compliance

Section 59 - Definitions

*Clause (b) defines a compliance procedure. The Consultation Paper uses this concept without defining it.

Section 60 - Recovery of payments and compensation

*This section implements a specific proposal of the Consultation Paper.

Section 61 - Inconsistency between disclosure statement and contract

*This section implements a specific proposal of the Consultation Paper.

Section 62 - Excusable error

*This section implements a specific proposal of the Consultation Paper.

Section 63 - Other contraventions

*This section implements as specific proposal of the Consultation Paper.

Section 64 - Assignee

*This section is to implements a specific proposal of the Consultation Paper.

Section 65 - Offences

Section 66 - Compliance orders

Section 67 - Investigations

*The subjects addressed by these sections are not addressed by the Consultation Paper.

Part 7 - Regulations and Transitional Provisions

*The subjects dealt with in this Part are not addressed by the Consultation Paper.

FOOTNOTES

1. For convenience, I will speak in this memo as if the CMC is a monolithic entity that speaks with one voice on any given matter. In fact, the views I attribute to the CMC are not necessarily shared by each member of the CMC. This is also true of later references in this memorandum to the views of the CMC working group.
2. In some jurisdictions some form of APR disclosure is also required for certain types of open credit.
3. The difference between the APR and the AIR is reasonably analogous to the difference between the yield and coupon rate on a marketable bond.
4. I say "essentially" proposed to abandon the APR because the Principles Paper was not as clear on this point as it could have been. The Principles Paper still required disclosure of the APR, but anyone who pid close attention to the arguments in the paper would have realized that the APR was essentially the interest rate, and that permitted non-interest charges would not have been included in the APR. In retrospect, the Principles Paper should have been blunter about this point and abandoned "APR language" altogether. This did not occur until CCDA 2 and the Commentary on CCDA 2 were circulated in early 1993.
5. Coincidentally enough, most members of the CMC working group were also members of the working group organized by the ULCC in the spring of 1994.
6. The Toronto meeting was attended by representatives of the federal government and every province except for Newfoundland and P.E.I.

7. The other alternative that was contemplated was for the Consultation Paper to describe the two approaches but not take a position on them. But the working group ultimately decided to take a position favouring disclosure of the APR for fixed loans.
8. The *Interest Act* is mentioned in the AIT as one of the federal statutes coming within the scope of the commitment to harmonize cost of credit disclosure legislation.
9. In fact, PIA 2.0 itself contemplated that the "balance calculation method" would be determined by regulations.
10. CCDA 3.2, section 8 would allow caps to be prescribed by regulations. However, such caps were regarded as a backstop that would be resorted to only if experience suggested that disclosure and market forces would not keep flat charges at reasonable levels.
11. A non-interest charge is defined in CCDA 4.1 as charge payable to the lender, an assignee, or an associate of the lender or assignee. It would not include an amount payable to an "unassociated" third party.
12. The position under CCDA 4.1 is discussed below in section II.E.1.
13. This is an incentive program, usually but not necessarily associated with the marketing of automobiles, in which consumers are offered a choice between low-rate financing and a cash rebate.
14. You will recall that we decided not to deal with cooling-off periods of that type in this project.
15. CCDA 4.1's general prepayment right would not provide for the refund of any portion of a flat charge imposed at the outset of a loan.
16. This was the only situation where CCDA 3.2 would have required disclosure of an APR.
17. When I refer to a drafting error in the Consultation Paper, I will have brought it to the attention of the drafter.