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The Legal History of Credit in Four Thousand Years (Or Less)

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THE LEGAL HISTORY OF CREDIT IN FOUR THOUSAND YEARS (OR LESS)

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It is easier to write about money than to acquire it; and those who gain it make great sport of those who only know how to write about it. - Voltaire[1]

I. IN THE BEGINNING, THERE WAS CREDIT. . .

Archeologists record the oldest known medium of currency as a 3,600-year-old clay tablet, found in Mesopotamia, which entitled the bearer to receive a quantity of barley at harvest time from a man named Amil-mirra.[2] Generally, it's wise to defer to Indiana Jones, especially when one's life depends on knowing which cup is the Holy Grail. Since my life is not in the balance, I can feel safe in disagreeing with Indy and asserting that a tablet is not money: it's a contract. But more specifically, a contract based on credit: the bearer supplied goods in the past relying on repayment in the future. Using terms with which we are familiar, the holder of the tablet was the creditor while Amil-mirra, was the debtor. Thus, it could be said this unwieldy chunk of rock may actually be the first credit card.

From our modern perspective, it may be surprising to recognize the concept of credit has existed since the dawn of civilization. Yes, the contract is graven in stone. Yes, the contract amounted to barter. Regardless of the context, it is inescapable that people were peaceably trading and basing those transactions on credit. This is not surprising. As Adam Smith noted, man seemed born with a "propensity to truck, barter and exchange one

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[1] VOLTAIRE, THE WORKS OF VOLTAIRE. *A Contemporary Version. A Critique and Biography by John Morley, notes by Tobias Smollett, trans. William F. Fleming* 21 vols. Vol. VI. Part II, p. 13 (New York: E.R. DuMont, 1901).

[2] NIALL FERGUSON, THE ASCENT OF MONEY 28 (Penguin Grp. 2008).

thing for another."[3] In the same way, it has been man's nature to regulate those transactions.

Even Amil-mirra's transaction was regulated, under Hammurabi's Code, famously known for the principle of *Lex Talonis*, an eye for an eye, interest rates were regulated and creditors were actually forbidden to seize a debtor's assets as restitution.[4] In fact, under the Code, if a creditor seized grain or livestock, not only must the creditor return it, but his illegal action forfeited his claim.[5]

While this seems enlightened, the reason for this liberality is somewhat less than progressive. In ancient times, debt was not secured by property or wealth: The debtor *was* security. Thus, if you could not pay, the creditor made you a debt-slave for a proscribed period of time to work off the obligation. That being said, a potential debt-slave *could* avoid servitude, by nominating his wife, kids or a slave to work it off.[6] As the Code artfully puts it: "If any one fail to meet a claim for debt, and sell himself, his wife, his son, and daughter for money or give them away to forced labor: they shall work for three years in the house of the man who bought them, or the proprietor, and in the fourth year they shall be set free."[7] Undoubtedly, this made for uncomfortable Thanksgiving dinners.

Obviously, lugging around rocks as contracts was not particularly efficient. Neither was it particularly easy to transact business. But man would find ways to make business easier. In fact, it can be said the story of mankind is the story of a steady evolution making trade simpler and more efficient. Likewise, throughout history, regulation evolved: sometimes helping that process and sometimes hurting it.

II. MAKING MONEY

It did not take long for man to devise a more portable medium of exchange: money. Money not only eliminates the need to tote around your wares and then chisel the deal into slabs of

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[3] ADAM SMITH, AN INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS13 (Edwin Cannan ed., 1976)

[4] *Hammurabi's Code of Laws,* L.W. King Trans., http://eawc.evansville.edu/anthology/hammurabi.htm (last visited Sept. 26, 2013).

[5] *Id.*

[6] *Id.*

[7] *Id.*

rock, it allows for efficient calculations of value, contracts to take place over greater distances and time, and creates a means of storing wealth that will not rot or spoil.

Initially, commodities themselves were a form of money, each culture creating their measures of value based on what mattered to them. Chocoholics might be pleased to know the Aztecs actually used cacao seeds as money, an interesting choice given historical records showing the Aztecs possessed gold in enough abundance to attempt to bribe Cortes, an unfortunate act which only served to fuel his greed.[8] But, as noted, the value of the seeds as 'money' was limited to the Aztec culture; European pirates seized a ship which happened to be full of cacao seeds.[9] Jack Sparrow dumped it overboard, thinking it rabbit dung.[10] Likewise, I am sure both pirates and Aztecs would look at our paper money and plastic debit cards with a jaundiced eye.

Likely due to durability, precious metals served a similar function until governments began to mint coins. In the western world, Herodotus credits the ancient kingdom of Lydia, located in what is now western Turkey, as being first nation to coin money.[11] Not that Herodotus heralded this economic revolution with much fanfare. Disappointingly, the creation of money is relegated an offhanded comment in a paragraph dominated by denigrating comments about the Lydian's predilection to prostitution as a significant source of national revenue.[12] With what may be the first recorded left-handed compliment, Herodotus charitably noted the Lydian way of life was not unlike the Greeks, "[a]part from the fact that they prostitute their daughters."[13]

This perspective on commerce is reflective of contemporaneous Greek attitudes. Both Plato and Aristotle condemned charging interest. In Plato's *Laws* he stated "no one shall . . . lend upon interest; and the borrower should be under no obligation to repay either capital or interest."[14] Plato ascribed to

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[8] "Cortes vs. the Aztecs", June 30, 2011, John Keko http://www.examiner.com/article/cortes-vs-the-aztecs

[9] JACK WEATHERFORD, THE HISTORY OF MONEY 17 (Crown Publ'g 1997).

[10] *Id.*

[11] HERODOTUS, THE HISTORIES 44 (Carolyn Dewald ed., Robin Waterfield trans., Oxford Univ. Press 2008).

[12] *Id.*

[13] *Id.*

[14] PLATO, *Book V*, *in* LAWS 9-10, Benjamin Jowett trans., http://classics.mit.edu/Plato/laws.5.v.html (last visited Sept. 26, 2013).

the philosophy that one should only lend to one's friends. While a grand suggestion, not repaying your pals generally led to the ancient practice of "unfriending."

His student, Aristotle, took an even stronger position. To Aristotle, there were two types of wealth-gathering: household management and retail trade. Becoming wealthy through the work of your own hands was "necessary and honorable." On the other hand, it was:

> [U]nnatural . . . [for] men gain from one another. The most hated sort, and with the greatest reason, is usury, which makes a gain out of money itself, and not from the natural object of it. For money was intended to be used in exchange, but not to increase at interest. And this term interest, which means the birth of money from money, is applied to the breeding of money because the offspring resembles the parent. Wherefore of any modes of getting wealth this is the most unnatural.[15]

After reading that, who doesn't want to skip the Super Bowl and tune in for the Adam Smith versus Aristotle grudge-match debate?

Despite Herodotus' disparagement and Platonic/Aristotelian snobbery, the Lydian invention was widely accepted and copied by governments in the region and beyond. Government sponsorship allowed an impartial standard to be set which also served as source of revenue: the difference of the stated value of the coin versus the actual metal content. For example, using modern measurements, an ounce of gold may be worth $600.00 therefore a newly minted one ounce gold coin should be worth $600.00. However, when ancient governments produced the coin, they would debase it by replacing some of that gold with another metal. It still weighed an ounce but it was not an ounce of gold. Not surprisingly, the unused gold ended up in the government's pocket.[16]

III. People Prefer Profits to Plato

We have seen that the ancients, in rapid fire succession,

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[15] ARISTOTLE, *Book 1, in* POLITICS, *Part X* , Benjamin Jowett trans., http://classics.mit.edu/Aristotle/politics.1.one.html (last visited Sept. 26, 2013).

[16] DAVID S. EVANS & RICHARD SCHMALENSEE, PAYING WITH PLASTIC 27 (2nd ed. MIT Press 2005).

created contracts, regulated creditor/debtor relationships and cast off the last shackles of the Stone Age by creating coins. These developments were timed almost perfectly for the rise of Rome. With its vast size, comparable peacefulness and efficient road network, trade over vast distances became possible.

As is well known, the Romans unashamedly ripped off the entire Greek pantheon and its culture, contriving to cover up this plagiarism by changing everyone's names. That being said, the Romans were all about practicality and not about philosophy for, unlike the Greeks, they did not condemn commerce. Instead, they differentiated between productive credit, used for business growth and investment, and consumptive debt, which were personal loans for consumer goods.[17] The former was praiseworthy while the latter was not. In the later stages of the Roman Empire, their views on interest were codified in Justinian's Code which proscribed their maximum legal rates.[18]

IV. The New Math

When Rome fell, Europe fractured along warring ethnic lines. While they may not have realized it, they had one thing in common: the yoke of Roman numerals. Remarkably, this remaining vestige of the empire served to stagnate the West's economic evolution for almost a thousand years. Roman numerals made basic addition and subtraction cumbersome and the calculation of interest or deprecation nearly impossible. This changed in 1202, when Leonardo Fibonacci introduced Europe to the Hindu-Arabic numeral system and the concept of zero in his treatise, *Liber Abaci* (Book of the Abacus).[19] The son of a Pisan customs official in what is now Bejai, Algeria, Fibonacci was exposed to this rational system of math, and mastered it.[20] But the true genius of his mastery was his presentation of the new theories. Rather than writing a dry collection of arithmetic formulae, he taught concepts by way of real world business examples, such as the computation of interest and used

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[17] LEWIS MANDELL, THE CREDIT CARD INDUSTRY: A HISTORY 13 (Twayne Publ'g 1990).

[18] DEMETRIOS GOFAS, *The Byzantine Law of Interest, in* THE ECONOMIC HISTORY OF BYZANTIUM, 1095, 1096 (Angeliki E. Laiou ed., Dumbarton Oaks 2002).

[19] FERGUSON, *supra* note 2, at 32.

[20] *Id.*

commodity trading as the theme for the entire work.[21] Soon Abacus schools erupted all over northern Italy and their graduates became the first corporate CEOs.[22]

With this new knowledge, a host of complex mathematics was made possible, leading to greater trade, greater volumes of lending and the birth of international banking. But more than that, it created lending structures outside of government or church control, lending not only to those entities, but also to the common trader and merchant.[23] This democratization of lending was an important component in the development of Western economic models.

V. LOSING MY RELIGION

So now, everyone could easily calculate interest but there was a *small* hurdle, most governments adhered to biblical strictures against usury or interest on loans.[24] In fact, Psalm 15 asks "Lord, who shall abide in thy tabernacle?" In response, it is said one of the persons who may abide in the tabernacle is one "that putteth not out his money to usury."[25] Ouch.

To get around issues of morality, the bankers, likely in cahoots with lawyers, simply changed the name of their new lending product from a loan to a "bill of exchange."[26] A merchant would receive their money in the form of a bill of exchange at their local bank.[27] They would present the bill to receive their money at a different bank in a different town, agreeing that they would pay a slightly higher amount than the actual loan.[28] See your Holiness? No interest! It's just a *service* charge.

The salutary effect of the bills of exchange was they removed the difficulty of the use of money, a development we just heralded five paragraphs ago. Lighter than clay tablets, coins were still a burden to carry about in large quantities. As result, trade increased because this private precursor to paper money made transactions easier and faster. No more waiting for a

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21 RODNEY STARK, THE VICTORY OF REASON: HOW CHRISTIANITY LED TO FREEDOM, CAPITALISM, AND WESTERN SUCCESS 108 (Random House 2005).

22 *Id.*

23 WEATHERFORD, *supra* note 10, at 72.

24 *See Leviticus* 25:36-7 and *Ezekiel* 18:13.

25 *See* Psalms 15:5.

26 WEATHERFORD, *supra* note 10, at 73-74.

27 *Id.* at 74.

28 *Id.*

delivery of gold coin, carted on the backs of mules, subject to brigands, pirates or tolls levied by each of the feudal dominions through which your caravan had the misfortune to travel. Weatherford provides an excellent illustration:

> In 1338, a shipment of coins required three weeks to wend its way from Rouen . . . to Avignon . . ., a distance of just over four hundred miles. By contrast, a bill of exchange could be sent in a mere eight days and if it was stolen, the thief could not redeem it. Despite the extra cost of 8 percent to 12 percent, a bill still proved cheaper than the cost of hiring an armed escort for a shipment . . . Bills of exchange helped to free money from its spatial limitations.[29]

Other barriers conquered by bills were the limitation of only lending the supply of coins on hand and reliance on a single currency. This allowed more money to be put into use without the need for the inflationary act of minting more coins. Soon, the bills were exchanged in place of coins, circulating to third, fourth and fifth parties, just like the paper money we know today.[30]

It was not long before government became entwined with the production of paper money. In the United States, the first use of paper money occurred in 1690 in the Commonwealth of Massachusetts who needed to find a way to pay for a boondoggle attempt to capture Quebec City.[31] The paper promised redemption in gold or silver coins and these slips were utilized in trade alongside gold and silver coins.[32] This pre-dated the creation of the British Central bank by four years which, from its outset, issued paper currency backed by redemption in precious metals. As we will see, the existence of a central bank is a necessary prerequisite to the formation of a system of credit.[33] Like bills of exchange, this paper had value because the holder had faith they *could* exchange their paper for metal. As you might expect, convenience aided faith and ensured almost no one cashed in their paper.

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[29] *Id.* at 75.
[30] *Id.*
[31] EVANS & SCHMALENSEE, *supra* note 16, at 28-29.
[32] *Id.*
[33] MARION ARCHIBALD ET. AL., MONEY: A HISTORY, 177 (Jonathan Williams ed., St. Martin's Press 1997).

VI. PAPER TO PLASTIC

By the 1980's, every major government had removed their currencies from a gold or silver standard. Therefore, unlike the 1690's or the 1960's for that matter, our money retains value not because of faith in its backing by gold, but on faith alone; the dollar is worth a dollar because we believe it is.

In the last twenty years, we have gotten even further disconnected from associating our money with anything physical. Old Amil-mirra thought it was pain to lug around that barley contract. In the 21st century, we actually decided paper money was too cumbersome. Thus, five millennia later, Amil-mirra's tablet was replaced by a weightless plastic card. Your money is now digits on a computer or smart phone screen. Remember that business transaction from Rouen to Avignon that took 8 days? It can now be completed with a mouse click which sends invisible, instantaneous transmissions of binary code that passes for money and is completed in an eighth of a second.

VII. GIVE AMERICA SOME CREDIT

But where did credit cards come from? America has had credit since its foundation. Records demonstrate installment credit was being offered by New York furniture retailer Cowperwaite and Sons as far back as 1807.[34] Revolving credit is a somewhat different animal. Its roots are found in the National Banking Act of 1863, which created nationally chartered banks even though the first national credit cards would not be issued for another century. Further centralizing and standardizing the banking system was the creation of the Federal Reserve in 1913. The key component of the Reserve System was the requirement of *all* nationally chartered banks to become members and thereby be regulated by the Fed.[35] Thus, the charge plate was set.

Interestingly, for much of American history, consumer lending was not a part of the portfolio of U.S. banks. The merchants themselves would provide the financing for the purchases and leave to the larger loans to the banks.[36] Credit cards stepped into the shoes of merchant lenders, allowing them to cut costs and risk, putting those on the third-party bank. Thus, "credit cards provided a platform that made borrowing and

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[34] MANDELL, *supra* note 17, at 14.
[35] EVANS & SCHMALENSEE, *supra* note 16, at 28-29.
[36] *Id.* at 51.

lending small amounts of money more efficient."[37]

The modern credit card allegedly began in 1949 when Frank McNamara, president of a credit company, realized he left his wallet at home in the midst of meal out.[38] He called his wife who dutifully arrived with the money.[39] This led to an epiphany of sorts: a club card to pay for restaurant outings so that lack of cash was not a deterrent. Extravagantly naming the initial use of the card the "The First Supper" a legend was born.[40] Unfortunately, such grandiosity tends to diminish the credibility of Diner's Club's origin.

At this time, the Diner's Club card was made out of paper, not plastic. In my extensive study of 1950's and early 1960's culture, I've watched at least three seasons of *Mad Men*, it does not seem it was customary for Don Draper to jam paper cards in his pocket, hoping they wouldn't get mangled. In other words, the card, like Frank's cash, would still be in his wallet and he would still have to answer to Mrs. Frank. Further research proved my instincts were correct: Diner's Club was not even the first revolving account credit card.

Credit, no pun intended, goes to the venerable department store, Bloomingdale's. In 1938, the store introduced what it called a permanent budget account which allowed customers the option of not paying off their bill every month, aggregating total purchases into a single sum that could be paid over time at the cost of interest charges.[41] Previous forms of credit, such as installment payments and charge cards may not have required payment at the time of purchase. However, the retailer did expect full payment over six months or, with a charge card, payment in full when billed at the end of the month.

This led to stores having credit managers who were scolds and moralizers, reducing interest in patronizing certain retailers due to embarrassment.[42] It was presumed wives, who generally frequented these department stores, needed to be stopped from their spendthrift ways, so that the haranguing credit manager

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[37] *Id.*

[38] DINERS CLUB INTERNATIONAL, www.dinersclubus.com/home/about/dinersclub/story?nav=left (last visited Sept. 26, 2013).

[39] *Id.*

[40] *Id.*

[41] LOUIS HYMAN, BORROW: THE AMERICAN WAY OF DEBT 104 (Vintage Books, 2012).

[42] *Id.* at 99-104.

acted *in loco husbandis.*[43] Contrary to this conceit, personal experience has shown overspending is an equal opportunity issue.

Now that we know the origin of revolving credit, let us return to Diner's Club. In fairness, while it may not have been the first revolving charge account, it was the first effort to forge a universal card. Your Bloomie's account only worked at Bloomie's. McNamara's goal was to have his card operate at any restaurant anywhere in the world. To that end, McNamara started out recruiting restaurants and giving cards to select individuals so that, by 1951 there were 42,000 members who paid $18.00 a year for membership.[44] Under the agreement, a member restaurant paid 7% of the cardholder's bill to Diner's Club.[45] What was the restaurant owner getting out of this transaction? The owner believed that by accepting Diner's Club cards, they would attract new business.[46] At the end of 1951, Diner's Club made $60,000 in pre-tax income.[47] By 1958, after absorbing a competitor and moving into hotels and car rentals, gross profits topped $40 million.[48]

This expansion concerned American Express. Famously known as the issuer of traveler's cheques, Amex saw Diner's Club as a danger to its travel related business. As a result, it entered the credit card field in 1958, buying up other Diner's Club competitors to even the playing field as the premier high-end traveler's club.[49] They charged a higher membership fee, to suggest it was more prestigious, but lured merchants to its banner by offering a merchant rate 2% lower than Diner's Club.[50]

But we are still not quite at our modern credit card. Indisputably, Diner's Club and Amex were universal cards but their business was not consumer loans, it was travel and dining. The first bank to issue a general use credit card was Bank of America to its customers in California, beginning in 1958.[51] Initially, merchants were reluctant to sign agreements to accept this card but Bank of America made it hard to refuse when the

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[43] *Id.* at 102.
[44] EVANS & SCHMALENSEE, *supra* note 16, at 54.
[45] MANDELL, *supra* note 17, at 3.
[46] *Id.*
[47] EVANS & SCHMALENSEE, *supra* note 16, at 54.
[48] EVANS & SCHMALENSEE, *supra* note 16, at 54.
[49] EVANS & SCHMALENSEE, *supra* note 16, at 58.
[50] *Id.* at 59.
[51] *Id.* at 57.

bank mass issued the card to some 60,000 area residents.[52] By the spring of 1959, the number of participating merchants rose from 800 to 25,000.[53] After losses of $45 million in 1960 due to a host of issues, it turned its first profit in 1961.[54]

The year 1958 saw Chase Manhattan enter the credit card field. It hastily exited the field when selling its credit card division to American Express in 1962.[55] Seven years later, Chase repurchased the division and joined with Bank of America, which had begun marketing its credit card as BankAmericard.[56] Despite this bi-coastal union, both cards were regional, limited to California and New York respectively whereas, at this stage, both Diner's Club and Amex were global players in their specialized area of travel and entertainment.[57] However, bank cards had the potential for explosive growth, they could attract a broad range of merchants and utilized a different business model: no membership fees and earning revenue strictly from merchant fees and finance charges.

In 1966, BankAmericard's in-state rivals, United California Bank, Wells Fargo, Crocker National Bank and the Bank of California, united to form the Interbank Card. Interbank Card's name changed to Mastercharge in 1969, and by 1979, was known as Mastercard.[58] Likewise, in 1970, BankAmericard re-incorporated as National BankAmericard. Four years later, the card became accepted outside the U.S., and in light of its now international reach, it renamed itself Visa in 1976.[59]

As the two card networks expanded, they each attempted to woo other banks: BankAmericard using a franchise system and Interbank by offering cooperative opportunities.[60] Of the two options, more banks preferred Interbank's system because under Interbank's system, the bank marketed a jointly owned brand rather than sublimating their identity to BankAmericard.[61] In this

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[52] *Id.*
[53] *Id.*
[54] *Id.* at 57.
[55] *Id.* at 60.
[56] *Id.*
[57] *Id.*
[58] MASTERCARD, http://www.mastercard.com/corporate/ourcompany/about-us.html (last visited Sept. 26, 2013).
[59] VISA, Corporate.visa.com/about-visa/our-business/history-of-visa.shtml (last visited Sept. 18, 2013).
[60] EVANS & SCHMALENSEE, *supra* note 16, at 64.
[61] *Id.*

way, Interbank member banks could still harbor their own dreams of national expansion if interstate banking requirements were lifted.[62]

However, under either system, members were required to sign exclusivity agreements. For example, if a bank signed with Visa, it was barred from offering Mastercard products.[63] This practice subjected Visa to anti-trust concerns, which will be discussed later in greater detail.[64] Notwithstanding this cutthroat marketing, Visa and Mastercard actually *cooperated* to create uniform operational standards for this emerging credit card system.[65]

Refusing to be subordinate to their growing competitors, regional banks tried to create competing bank networks for their own card.[66] For example, in Illinois, five banks created the Midwest Bank Card, which eventually comprised a network of 600 banks in Illinois, Indiana and Michigan.[67] Despite these efforts, the regional partnerships lacked expertise, and individual banks reluctantly began aligning with the two growing powers.[68]

This had a salutary effect of hastening standardization of credit practice due to Visa's and Mastercard's previous coordination on the architecture of the system; interoperability became a foundation of the modern card system.[69]

VIII. THE DEATH OF A SALESMAN

The birth of a national system of credit changed the landscape of credit altogether. In the past, stores had issued the credit. After the success of Bloomingdale's model, other department stores in the post-war era followed suit.[70] Yet, in the space of a generation, an entirely new model was overtaking the world of consumer credit. As seen by the previous section, banks, formerly unconcerned with small-scale consumer lending, were suddenly very interested in this line of business.

In the wake of World War II, economic and lending

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[62] *Id.*
[63] EVANS & SCHMALENSEE, *supra* note 16, at 70.
[64] *Id.*
[65] *Id.* at 63.
[66] *Id.*
[67] *Id.*
[68] *Id.* at 64.
[69] *Id.* at 65.
[70] HYMAN, *supra* note 37, at 106.

incentives had changed. Returning soldiers were ready to start families, while generous VA loans promised mortgages on homes with almost no money down.[71] Even non-veterans could enjoy low mortgage costs via FHA loans, bought by Fannie Mae.[72] Between 1944 and 1950, housing construction exploded from 114,000 single family detached homes to 1.7 million.[73] Combined with the creation of the federally subsidized Eisenhower highway system, the predominantly urban landscape became a suburban vista with 60 million people moving to the suburbs by 1980.[74]

Having moved from the city into a larger living space, new homeowners were left with a problem that made retailers salivate: additional rooms to furnish.[75] In furnishing homes, revolving credit gave homeowners the flexibility to buy on credit and pay at their own rate rather than having to exercise miserly saving.[76] From cars to appliances to furnishings, everything could be bought on credit.[77] Religious and social mores about debt had clearly changed: credit and installment lending climbed from $2.6 billion in 1945 to $103.9 billion in 1970.[78] The rise of American economic hegemony out of the devastation of World War II coincided with an increase in wages and optimism, a decline in the fear of credit, and a softening of the so-called Protestant work-ethic.[79]

Therefore, a store that refused to offer credit or favored cash over sales was subject to a competitive disadvantage.[80] Instead, most stores offered such credit, not only as an impetus to buy but also to promote customer loyalty.[81] However, the growth of discount chains like K-Mart and Target ate into the customer base of high-end department stores.[82] They, too, offered credit but with lower margins, they were eager to find someone else to bear the costs and the risk.[83]

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[71] ROBERT D. MANNING, CREDIT CARD NATION: THE CONSEQUENCES OF AMERICA'S ADDICTION TO CREDIT, 37 (Basic Books 2000).
[72] *Id.*
[73] *Id.*
[74] *Id.*
[75] HYMAN, *supra* note 37, at 76.
[76] *Id*. 105-106.
[77] *Id.* 96.
[78] *Id.* at 38.
[79] *Id.* at 34-36.
[80] HYMAN, *supra* note 37, at 106.
[81] *Id*. at 109.
[82] HYMAN, *supra* note 37, at 119.
[83] *Id.* at 139.

The economic downturn of the 1970s further altered the landscape: more shopping than ever occurred at discount rather than department stores.[84] Department store credit was feasible in a booming economy because it was based on quick repayment usually six months or less, somewhat limiting the danger of store borrowing to pay for their customer's purchases while they waited for repayment..[85] However, in the economic downturn, people were unable to afford the higher prices of department stores and turning more strongly to discounters.[86] In order to keep their costs low, discounters did not want to create their own card system nor borrow money (and pay interest on that borrowing) to fund store purchases.[87] As a result, discounters welcomed the advent of third-party credit cards.[88] By the end of the 1970s, most department stores were accepting national brand credit cards.

Logistically, in this new economy, the change made sense. Most purchases were now being done on credit, and the pace was increasing.[89] In the past, retailers provided proprietary cards, in which the retailer was responsible for borrowing money to pay for the customer's purchase, relying on the hope that they would be repaid.[90] Consequently, retailers had more capital tied up in credit loans than in merchandise.[91] Thus, when banks began lending for consumer goods purchases, it made sense for retailers to allow banks to take on that risk rather than assume it themselves.

IX. DEBT CAN BE TAXING. . . EXCEPT WHEN IT'S NOT

The acceptance of credit and accumulation of debt were not simply functions of a changing economy and social mores. Part of the reason for this cultural change was the unforeseen consequences of legislation.

During World War II, the federal government lowered the tax brackets so that the middle class, formerly exempt from taxation, was required to shoulder the burden.[92] Nonetheless, in

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[84] *Id*. at 151.
[85] *Id.* at 139.
[86] *Id.* at 151.
[87] *Id.* at 143.
[88] *Id.* at 140.
[89] EVANS & SCHMALENSEE, *supra* note 16, at 40
[90] *Id.* at 119.
[91] *Id.* at 139.
[92] *Id.* at 123.

making them subject to taxation, the middle class now had access to the same tax deductions utilized by wealthy individuals and businesses.[93]

In 1913, the passage of the Sixteenth Amendment, creating the income tax, allowed for the deduction of *all* interest. In that era, most loans were business loans and, as such, their interest was deductible as a business expense.[94] With the application of the new tax code, an individual's mortgage, credit and installment interest were now deductible as well, giving consumers an incentive to borrow.[95] In addition, the creation of FHA in the 1930s led to the government—subsidized 30 year mortgage, thereby conditioning people to accept what used to be unacceptable: long term debt.[96]

When the Sixteenth Amendment was passed, it was presumed that few individuals would ever pay taxes.[97] Clearly, it was not imagined that laws intended for businesses would eventually be utilized to make a TV purchase seem like a wise tax decision.[98] Likewise, the government planners who saw home construction as the solution to the Depression did not consider it might be a means to change attitudes on long term debt.[99] Nor could the authors of the G.I. Bills that rewarded our soldiers for their service have imagined its impact on the accumulation of consumer debt. Like anything else, many different and seemingly unconnected strands came together to form history, even with something as mundane as a credit card.

X. Dancing Between the Raindrops

While these programs may have helped shape a new consumer viewpoint, what is clear is that no enabling statute created the credit card. Perhaps the most striking aspect of the rise of the credit card is how its legal existence was a consequence of tangentially related laws and cases. Specifically, "[c]onsumer credit has been subject to a large variety of legal controls. . . of

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[93] *Id.*

[94] *Id.*

[95] *Id.* at 124.

[96] *Id.* at 87, 222 (arguing that the 1986 tax reform bill, which removed all interest deductions but mortgage interest, combined with the meteoric rise in home values, is partially to blame for the crash of 2008: consumers took out second mortgages to pay for lavish spending and to pay-off credit cards).

[97] *Id.* at 115.

[98] *Id.*at 116-117.

[99] *Id.*at 89.

general application like the usury laws and . . . bankruptcy, fraud and duress and some of . . . special application like the small loans laws and the Retail Installment Sales Acts."[100] That was about to change.

XI. REGULATION Z

The Truth in Lending Act ("TILA"), passed by congress in 1968, become the first legislation to statutorily address credit cards. The statute states,

> . . .economic stabilization would be enhanced and the competition among the various financial institutions and other firms engaged in the extension of consumer credit would be strengthened by the informed use of credit. The informed use of credit results from an awareness of the cost thereof by consumers. It is the purpose of this subchapter to assure a meaningful disclosure of credit terms so that the consumer will be able to compare more readily the various credit terms available to him and avoid the uninformed use of credit, and to protect the consumer against inaccurate and unfair credit billing and credit card practices.[101]

The regulations implementing the statute are codified at 12 CFR Part 226.[102] Subsection (B) of the addresses open-ended or revolving credit card accounts.[103] Commonly, these regulations are entitled Regulation Z.

Okay, I know you are asking the same question I did. Why are they called Regulation Z? While I can assure you it does not authorize creation or citizenship for zombies, there is no explanation. Even the internet has no surmise on the origin of the name other than an anonymous poster at Ask.com who claims it is named Regulation Z because Z is the 26th letter of the alphabet and these regulations were the 26th set of regulations dealing with home mortgage financing and lending practices.[104] I am not sure if I buy this, given that the citation in the Code of Federal

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[100] HOMER KRIPKE, *Consumer Credit Regulation: A Creditor-Oriented Viewpoint*, 68 COLUM. L. REV. 445, 445 (1968).

[101] Consumer Protection Act, 15 U.S.C. §1601 (1968).

[102] Truth in Lending Act, 12 C.F.R. § 226.1 (2011).

[103] *Id.*

[104] ASK.COM, http://www.ask.com/question/why-is-it-called-regulation-z (last visited Sept. 28, 2013).

Regulation is 12 C.F.R. §226, not §26. Instead, considering the dry nature of the reading, perhaps "Z" refers to their anti-insomniac applications.

Regardless of the source of its name, these rules would serve as the primary backbone governing credit card issuers until the 2009 Credit Card Accountability, Responsibility and Disclosure Act (CARD).[105] Under TILA, the Federal Reserve served as the body to promulgate and administer the rules to the credit card industry. As of July, 2011, under the Dodd-Frank Wall Street Reform and Consumer Protection Act, TILA's general rule making authority was transferred to the Consumer Financial Protection Bureau, an entity created by the same act.[106]

XII. IN ANTI-TRUST WE TRUST

Anti-trust laws also impacted the nature of the credit cards we know today. As noted above, the terms of Visa's agreements forbade Mastercard issuing banks from issuing Visa cards or handling transactions with Visa merchants.[107] In 1971, Worthen Bank and Trust attempted to associate with both Visa and Mastercard, but when Visa chose to enforce its exclusivity agreement, the bank filed an antitrust lawsuit against Visa.[108] The case settled eventually, but Worthen's action sparked similar challenges to the Visa agreement from its competitors. As a result, in 1974, Visa sought a business clearance review from the Department of Justice for its practices.[109] When the Department declined to hold that Visa's exclusivity agreement was not a violation of anti-trust laws, Visa removed all restrictions against Visa members also offering Master Card products, thereby ushering in the practice of dual acceptance.[110]

However, Visa's membership agreement still maintained exclusivity agreements against other issuers. In 1989, Sears sought membership in Visa, a request Visa refused, going so far as to enact a membership rule that denied Visa membership to

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105 123 STAT. 1734 Public Law 111-24-May 22, 2009, www.gpo.gov/fdsys/pkg/PLAW-111publ24/pdf/PLAW-111publ24.pdf (amending the Truth in Lending Act).

106 http://www.federalreserve.gov/newsevents/press/bcreg/20110201a.htm Press Release February 1, 2011.

107 EVANS & SCHMALENSEE, *supra* note 16, at 70.

108 Worthen Bank and Trust Co. v. Nat'l BankAmericard Inc., 485 F.2d 119 (8th Cir. 1973).

109 EVANS & SCHMALENSEE, *supra* note 16, at 277.

110 *Id.* at 278.

anyone issuing Discover or American Express cards.[111]

In an effort to bypass that by-law, a Sears' subsidiary, SCFC ILC acquired Mountain West, a small Utah thrift institution which possessed membership in Visa. When the small thrift which had 5,800 Visa accounts suddenly ordered 1.5 million Visa cards to start a new "Prime Option" credit card, Visa refused.[112] Mountain West sued for an injunction to force approval of the delivery of the 1.5 million cards, which was granted in district court. Visa appealed and overturned the order, remanding the case for further proceeding. [113] Eventually, a final determination was reached in 1994 when the 10th Circuit found Visa committed no anti-trust violation because the by-law did not bar Sears from access to the credit card market.[114] Given Sears owned Discover, there was no evidence Sears could only produce the Prime Option Card with Visa's help or that exclusion from a joint venture with Visa prevented issuing the new card as a Discover product.[115]

In 1996, Wal-Mart, in a class action where it was joined by rival Sears and nearly five million other retailers, sued Visa and Mastercard for violations of anti-trust laws on the grounds that it was illegal to require retailers who accepted a Visa debit card to also accept Visa credit cards.[116] Seven years later, the case settled for approximately $2.5 billion dollars and with Visa and Mastercard agreeing to allow merchants to take debit cards without being required to take credit cards.[117]

Yet, even in the wake of Wal-Mart's class action, the concept of Visa/Mastercard duality remained unchallenged Finally, in 2003, these practices were found to violate the law.[118] The Second Circuit dismissed arguments that the exclusionary rules were necessary to promote cohesion between Visa and Mastercard and that "in any event the anticompetitive effects outweigh the procompetitive."[119]

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[111] SCFC ILC, Inc. v. Visa, 936 F.2d 1096, 1097 (10th Cir. 1991).

[112] *Id*. at 1098.

[113] *Id.*

[114] SCFL ILC, Inc. v. Visa USA, Inc., 36 F.3d 958, 971 (10th Cir 1994).

[115] *Id.*; *In Re Visa Check/Master Money Antitrust* Litigation, 96 CV 5238.

[116] EVANS & SCHMALENSEE, *supra* note 16, at 267.

[117] *Id.* at 267.

[118] United States v. Visa U.S.A., Inc., 163 F. Supp. 322, 340–42 (S.D.N.Y. 2001), *aff'd*, 344 F.3d 229 (2d Cir. 2003).

[119] *Id.* at 243; *See generally*, K. Craig Wildfang et al., *The Persistence of Anti-Trust Controversey and Litigation in Credit Card Networks, 73* ANTITRUST LAW 675 (studying the interaction of credit cards and anti-trust

Most recently, Mastercard, Visa and some of the larger banks settled another class action suit, involving about 7 million U.S. merchants, a case centered on claims that the defendants unlawfully conspired to fix swipe fees for merchants.[120] The settlement was reached on behalf of a class of roughly 7 million U.S. merchants who accept Visa and MasterCard credit cards and debit cards.[121] In the settlement, Visa agreed to pay some $4.4 billion and Mastercard $790 million.[122] Both parties also agreed to reduce swipe fees, fees paid by merchants to issuers for each card use, while they retool their rules on such transactions. In addition, retailers could now impose a surcharge for use of credit cards (presumably assessed on the consumer) subject to caps and disclosures.[123]

XIII. A PLAGUE OF PLASTIC

We have already examined the first consumer protection rules, Regulation Z, promulgated in the wake of the passage of TILA in 1968. Two years later, Illinois banks can be credited with the dubious distinction of being the reason for the next set of federal and state legislation drafted to protect consumers.[124]

As mentioned above, when credit card networks began to emerge, regional banks attempted to create their own networks by getting cards to consumers whether they asked for them or not..[125] Sadly, the axiom against keeping up with the Joneses is a cautionary tale for banks as well as consumers.

In 1966, Marine Midland Bank had tested two ways of exhorting customer interest in its card: sending credit card applications to some customers and actual cards to others.[126] To

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laws).

[120] JAMES O'TOOLE, *Visa MasterCard Settle Antitrust Case*, CNNMONEY (July 14, 2012), http://money.cnn.com/2012/07/13/news/companies/visa-mastercard-settlement/index.htm. discussing *In Re Payment Card Interchange Fee and Merchant Discount Antitrust Litigation,* 05 MD 1720, United States District Court, Eastern District of New York.

[121] *Id.*

[122] *Id.*

[123] *Id.*

[124] SEAN VANATTA, *The Great Chicago Christmas Credit Card Fiasco of 1966: Echoes*, BLOOMBERG (Dec. 24, 2012 5:30 PM), http://www.bloomberg.com/news/2012-12-24/the-great-chicago-christmas-credit-card-fiasco-of-1966-echoes.html.

[125] HYMAN, *supra* note 37, at 156.

[126] *Id.*

ensure an accurate measure, they controlled the distribution, ensuring that the recipients in both groups were similarly placed in terms of income and worth.[127] In total, 33,357 applications were sent versus 731 credit cards.[128] While the disparity in cards versus applications was enormous, the response was entirely reversed: only 0.7% of the applications were returned while 19% of the cards sent in the mail were used within 60 days; in other words, cards had a response rate 27 times the response of applications.[129] Not surprisingly, Marine Midland began direct mailing their cards.[130] Even if the cards were never used, the bank was able to sell merchants on how many cards were technically in the hands of potential customers.[131] Marine Midland was not alone. As noted earlier, an Illinois dominated Midwest banking coalition was determined to form a rival credit card network.[132] In their myopic focus on getting cards to their customers before anyone else did, they spawned a mass mailing strategy of Biblical proportions, issuing *five million cards in a single month*.[133]

The initial threshold was low: Any customer without bad credit would get a card.[134] But their effort was not limited simply to customers. [135] Under the Illinois Constitution of 1870, branch banking was banned. The only lessening of that restriction was made in 1967, which permitted a drive- in facility within 1500 feet of the main bank.[136] This geographical limitation led to the purchase of mailing lists of persons who owned stock, had expensive cars, membership in certain organizations or clubs, business owners. . . you get the picture.[137]

Unfortunately, no one coordinated this process to eliminate persons who might appear on more than one of those lists.[138] A businessman with a new car purchase, stock and a

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[127] *Id.*
[128] *Id.*
[129] *Id.* at 156-57.
[130] *Id.* at 157.
[131] *Id.*
[132] EVANS AND SCHMALENSEE, supra note 16, at 63.
[133] Hyman, *supra* note 37, at 158.
[134] *Id.* at 159.
[135] *Id.*
[136] ILLINOIS DEPARTMENT OF FINANCIAL & PROFESSIONAL REGULATION, http://www.idfpr.com/Banks/cbt/STATS/BR-HIST.ASP (last visited Sept. 28, 2013).
[137] HYMAN, *supra* note 37, at 159.
[138] *Id.*

prestigious club membership received seven cards on the same day while another received eighteen cards, including one for each of his three boys, aged nine to thirteen.[139] At the same time, a woman received cards from two separate banks; unfortunately, she had been dead five months.[140] As if giving credit to the dead were not enough, babies and small children also received cards in the mail.[141] Federal Reserve Board member Andrew F. Brimmer explained this at a congressional hearing: "Babies with sizable savings accounts—frequently opened by grandparents—could not be distinguished from adults."[142]

If you think that this could not get worse, it does. You see, the banks also *publicized* that they were mailing these cards at the holiday season so that post-office temps, criminals and perhaps the neighbor you didn't like, pilfered your mail and post box.[143] Enterprising criminals also knew the adage "location, location, location" applied even in crookery, targeting multifamily homes and apartments where they knew they could collect the most plastic.[144] Lacking the activation protocols we have today, a simple forged signature started the spending spree. Bloomberg estimates losses ranged between $6 million to $12 million, or $43 million to $85 million in 2012 dollars.[145]

This led to federal law addressing the subject and the Credit Card Liability Act in Illinois, which states:

> No person in whose name a credit card is issued without his having requested or applied for the card or for the extension of the credit or establishment of a charge account which that card evidences is liable to the issuer of the card for any purchases made or other amounts owing by a use of that card from which he or a member of his family or household derive no benefit unless he has indicated his acceptance of the card by signing or

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[139] *Id.*

[140] SEAN VANATTA SUPRA NOTE 122:, *The Great Chicago Christmas Credit Card Fiasco of 1966: Echoes*, BLOOMBERG (Dec. 24, 2012 5:30 PM), http://www.bloomberg.com/news/2012-12-24/the-great-chicago-christmas-credit-card-fiasco-of-1966-echoes.html. (While Bloomberg's author thinks this strange, Chicago has long allowed the dead vote so why not give them credit cards?).

[141] *Id.*

[142] *Id.*

[143] *Id.*

[144] *Id.*

[145] *Id.*

> using the card or by permitting or authorizing use of the card by another. A mere failure to destroy or return an unsolicited card is not such an indication.[146]

Regarding collection actions filed in such instances, the law required:

> When an action is brought by an issuer against the person named on the card, the burden of proving the request, application, authorization, permission, use or benefit as set forth in Section 1 hereof shall be upon plaintiff if put in issue by defendant. In the event of judgment for defendant, the court shall allow defendant a reasonable attorney's fee, to be taxed as costs.[147]

As to liability, the Act held:

> Notwithstanding that a person in whose name a credit card has been issued has requested or applied for such card or has indicated his acceptance of an unsolicited credit card, as provided in Section 1 hereof, such person shall not be liable to the issuer unless the card issuer has given notice to such person of his potential liability, on the card or within two years preceding such use, and has provided such person with an addressed notification requiring no postage to be paid by such person which may be mailed in the event of the loss, theft, or possible unauthorized use of the credit card, and such person shall not be liable for any amount in excess of the applicable amount hereinafter set forth. . .[148]

For those who were subject to fraud from the shotgun mailing, the statute limited liability in such actions. If the card had no signature pane, liability was limited to $ 25.00 and those with a signature panel to $50.00. Wisely, the practice was banned entirely by the Unsolicited Credit Card Act of 1977.[149]

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[146] Credit Card Liability Act, 815 Ill. Comp. Stat. 145/0.01 (2013).
[147] Credit Card Liability Act, § 145/1.
[148] Credit Card Liability Act, § 145/2.
[149] Credit Card Liability Act, § 150/1.

XIV. AND NOW. . . THE SUPREMES

The earliest case in the modern credit card era attempting to discern the nature of the credit card contract took place in 1954. It did not involve consumers or collections but was a regulatory action. A company called Master Charge (presumably no relation to what eventually became Master Card) appealed a ruling that found Master Charge was denied a permit to issue capital stock because it had not procured a license as a lender under the Small Loan Law.[150] To Master Charge, what it was doing was nothing like a loan because it was not delivering money. Under their business plan, for a charge of $ 5.00 per year, it issued cards to persons deemed to be good credit risks, which entitled them to purchase, on credit, merchandise or service at stores, hotels and restaurants listed in its booklet. At the point of sale, the cardholder would sign an invoice and Master Charge would agree to purchase, without recourse, at a discount from 6 to 10 percent any of the invoices the listed retailer chose to sell and assign to it. Master Charge would bill the cardholder for the face amount of the invoices and the cardholder will pay the same.[151] Master Charge insisted that a loan of money is a contract by which one delivers a sum of money to another, and the latter agrees to return at a future time a sum equivalent to that which he borrowed.[152] Thereby, a law that could apply only to loans of money was not intended to apply to loans of credit.

The court would not play semantic games. It upheld the commissioner's decision finding that there is no essential difference between a loan and a sale of credit, so Master Charge was required to license under the Small Loans Act.[153]

While not a Supreme Court case, it is a useful preface demonstrating that the primary obstacle to creating a universal card was the assumption that issuers were subject to state law.[154] It would take almost a quarter century for the Supreme Court to review such perceived limitations. Yet, like so much of the credit card's legal history, the fact the case involved a credit card was tangential to the decision.

In *Marquette Nat. Bank of Minneapolis v. First of Omaha Service Corp,* a unanimous court found state usury laws did not

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[150] Master Charge v. Daugherty, 267 P.2d 821, 822 (Cal. Ct. 1954).
[151] Master Charge, 267 P.2d at 822.
[152] *Id.*
[153] *Id.*
[154] EVANS AND SCHAMALENSEE, supra note 32, at 69.

apply to nationally chartered banks.[155] This was First of Omaha's second go-around with this argument, having come out the loser of a similar case in Iowa. While the federal court in that case had refused to enjoin the card program, the Iowa Supreme Court held usury laws were applicable.[156] As a piece of trivia, after this loss, the Omaha hired Robert Bork, Ronald Reagan's failed Supreme Court nominee, to argue the instant case before the Supreme Court.

The First National Bank of Omaha (Omaha Bank) was a nationally chartered bank located in Nebraska.[157] In the war of BankAmericard v. Interbank (Visa) it chose to join the BankAmericard network.[158] Given its proximity to Minnesota, Omaha Bank solicited for new cardholders in Minnesota.[159] The Minnesota cardholders they reenrolled were charged the interest rate permitted by Nebraska law (18%) on unpaid balances.[160] However, this interest rate was in excess of that permitted by Minnesota law (12%).[161] The Marquette National Bank of Minneapolis (Marquette), a Minnesota-chartered national banking association, also enrolled in the BankAmericard plan, brought suit in Minnesota against Omaha Bank to enjoin the operation of Omaha Bank's card until such time it complied with Minnesota's usury law.[162] The trial court rejected Omaha Bank's contention that the National Bank Act preempted Minnesota's usury law.[163] On appeal, Omaha Bank asserted 12 U. S. C. §85 authorized any national banking association to charge on any loan interest at the rate allowed by the laws of the State where the bank is located.[164] The Minnesota Supreme Court reversed and the U.S. Supreme Court granted certiorari.[165]

At the outset, Justice Brennan observed Omaha Bank is a national bank which makes it an instrumentality of the Federal government, created for a public purpose, and as such is necessarily subject to the "paramount authority of the United

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[155] Marquette Nat'l Bank of Minneapolis v. First of Omaha Serv. Corp., 439 U.S. 299, 319 (1978).

[156] Fisher v. First Nat'l Bank of Omaha, 548 F.2d 255, 548 (8th Cir. 1977).

[157] Marquette Nat'l Bank, 439 U.S. at 301.

[158] *Id.* at 302.

[159] *Id.*

[160] *Id.*

[161] *Id.*

[162] *Id.* at 304.

[163] *Id.* at 306.

[164] *Id.*

[165] *Id.* at 307.

States," meaning the interest rate that Omaha Bank could charge is governed by federal law.[166]

Marquette did not disagree Omaha Bank was an entity whose locus was in Nebraska.[167] Instead, it contended that a national bank which systematically solicits Minnesota residents for credit cards to be used in Minnesota merchants must be considered to be 'located' in Minnesota.[168] The court disagreed with this argument as well, holding that the credit extended was granted by Omaha Bank in Nebraska, that the finance charges were assessed by the bank in Omaha, and all payments on unpaid balances are remitted to the bank in Omaha[169] Furthermore, the bank issued its BankAmericards in Omaha,, after credit assessments made by the bank in that city.[170]

Failing that, the bank attempted to argue Omaha Bank's credit card plan adversely affected the marketplace.[171] Justice Thurgood Marshall was particularly interested in learning how Marquette could be at a competitive disadvantage when the competition was charging interest 6% higher than Marquette.[172] When Marquette's attorney insisted on the point, Marshall rhetorically asked if other gas station owners would object if its competitor tripled their price.[173]

When the unanimous court finished writing the decision, I am sure they had no engage in self-congratulation; *Brown v. Board of Education* this was not. To them, and I am sure most legal observers, this was a by-the-numbers application of the supremacy clause. But, in the world of credit cards, it changed everything.

Previously, usury laws limited the development of a national card industry because they limited the bank's ability to market their cards nationally, or as you can see from *Marquette*, regionally due to the differences in rates. Each state would require the issuer to administer an entirely different program.[174]

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[166] Marquette Nat'l Bank of Minneapolis, 439 U.S. at 309 (citing Davis v. Elmira Savings Bank, 161 U.S. 275, 283 (1896)).

[167] *Id.* at 309.

[168] *Id.* at 312.

[169] *Id.* 310-11.

[170] *Id.*

[171] *Id.* at 314.

[172] OYEZ , http://www.oyez.org/cases/1970-1979/1978/1978_77_1265, MP3 transcript of *Marquette Nat'l Bank of Minneapolis v. First of Omaha Serv. Corp.,* oral argument, minute 24:10 to 24:20.

[173] *Id.* at minutes 25:20 to 25:29.

[174] EVANS & SCHMALENSEE, *supra* note 16, at 69.

After *Marquette*, three major changes occurred. First, nationally chartered banks began to move from the state they had chartered in to ones with less restrictive usury laws, such as South Dakota and Delaware.[175] Second, in order to restrain banks from leaving their states, shedding jobs and tax revenue, states began to eliminate their usury caps. For example, New York went from 12% caps to complete elimination of caps except for credit cards, which they allowed to rise to 25%.[176] Finally, with fewer interest rate differentials, banks could now begin true national mass-marketing.[177]

XV. DO YOU HAVE ANY CASE LAW FOR THAT?

On the state level, cases involving credit cards were also running through the system. While certainly not exhaustive or scientific, a search on Lexis in its state court case database from 1901 to the present shows the first opinion on personal liability on credit card was in 1960. In *Union Oil Company v. Lull*,[178] the defendant was sued by Union for $1,454.25 in charges. Unfortunately, the charges were unauthorized and Lull claimed he did not know about the charges until he received his bill on May 26, 1958 at which time he immediately canceled the card by telegram.[179]

The terms of the card, printed on the back, stated the account holder guaranteed payment for services or products rendered "to anyone presenting this card" even if the charges were unauthorized.[180] Lull claimed he was unaware of the liability because the manner by which the terms were conveyed (being on the back of the card) would not lead a cardholder to suspect they were part of a contract.[181]

The court held that Lull's misconception would not allow him to escape liability.[182] This is likely because there was some factual evidence to show Lull knew the card was missing early in May. However, after an extensive review of the case law, while the court said the terms could be applied against Lull, it noted

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175 *Id.*
176 *Id*. at 70.
177 *Id.* at 70.
178 Union Oil Co. of Cal. v. Lull, 349 P.2d 243, 245 (Or. 1960).
179 *Id.* at 246.
180 *Id.* at 247.
181 *Id*. at 249. Id at 246-47.
182 *Id.* at 250.

Union's right to recover under the guaranty agreement for unauthorized purchases was conditioned on Union's exercise of reasonable care in making inquiries as to the identity of the purchaser.[183] As this was a cross-country gas buying spree, the court was essentially requiring Union to produce cashiers to testify from each station where the card was used. I'm guessing Lull won Part II.

In contrast, another identity theft liability case, filed subsequent to the TILA and Regulation Z had a different outcome. In *Nat'l Commercial Bank & Trust Co. V. Malik*,[184] the bank sued the owner of a store for an act of good customer service. A customer accidently left a credit card at the defendant's store.[185] The storeowner found it and immediately notified the customer who promised to retrieve the card in six days.[186] The defendant's employee agreed to hold the card until then.[187] Thereafter, the card was used to make $3,304.01 in unauthorized charges.[188]

The bank did not sue their customer, choosing instead to sue the storeowner, claiming he had wrongfully allowed the card to fall into possession of an unauthorized user, that the cardholder had assigned their claims against the storeowner to the bank, that the loss of the card was occasioned by the owner's negligence and breach of an alleged bailment of the card.[189]

Relying almost exclusively on TILA, the court noted the Act places the burden of proof on the issuer to demonstrate they provided notice of the potential liability of unauthorized use to the cardholder.[190] In looking to the allegations of the complaint, the court noted it did not allege compliance with the notice provisions of TILA.[191] Indeed, notice to merchants is not a part of TILA, rendering it impossible for the bank to make such a claim.[192]

With the bank arguing it stepped into the cardholder's shoes via an assignment, the court analyzed the rest of the

183 *Id.* at 253.
184 Nat'l Commercial Bank & Trust Co. v. Malik, 72 Misc. 2d 865, 865 (N.Y. Sup. Ct. 1972).
185 *Id.* at 866.
186 *Id.*
187 *Id.*
188 *Id.*
189 *Id.*
190 *Id.* at 867.
191 *Id.*
192 *Id.* at 866-67 (the court cited the notice provisions found in TILA).

allegations under that theory.[193] According to basic assignment law, an assignee receives the same rights as the assignor.[194] In looking at the dictates of TILA, the court properly noted the cardholders who lost the card would have had no liability to pay for the unauthorized uses.[195] Consequently, they would have suffered no damages.[196] Therefore, "the claims of the plaintiff assignee. . . are therefore claims without damages."[197]

The first Illinois case examining credit cards appears to be a criminal matter: *People v. Roberts.*[198] It is notable for Robert's defense which led to an interesting formulation of the credit card contract. In this case, Roberts was convicted of forgery for purchasing $3.00 worth of gas with a credit card.[199] The forgery claim was based on the signed sales slip.[200] He appealed.[201]

While admitting he was not the authorized user of the card and that the signature on the slip was not that of the authorized user, he asserted the signature was only a deceptive practice, not forgery and that the slip was not an instrument capable of defrauding another, language that was a statutory requirement.[202] Roberts claimed the sales slip, *combined with the credit card itself*, may constitute a document but the failure to allege the existence of a credit card account was fatal to the indictment.[203] The court disagreed, utilizing the reasoning similar to a later civil case, *Garber v. Harris Trust*, holding the credit card itself simply establishes a line of credit exist while the sales slip, like a check, purports to make use of the credit.[204]

XVI. THE NATURE OF THE CREDIT CARD

As the credit card was beginning to gain popularity, legal scholars were attempting to use familiar common law notions of contract and the commercial code to analyze the credit card contract. As early as 1960, the California Law Review tried,

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193 *Id.* at 867.
194 *Id.*
195 *Id.*
196 *Id.*
197 *Id.*
198 People v. Roberts, 27 Ill. App. 3d 489, 490 (3d Dist. 1975).
199 *Id.* at 490.
200 *Id.*
201 *Id.*
202 *Id.* at 491-92.
203 *Id.* at 492.
204 *Id.*

without success, to fit itself into the existing legal framework of letters of credit or credit offered by the seller itself.[205] As the article's title makes clear, the involvement of a third-party lender to consumer purchases confounded the legal scholars. As previously discussed, bank lending for consumer purchases, was unknown, both from a business or legal perspective. With some pride, it can be said that Illinois courts were first to answer the riddle posed in the California Law Review. That is, Illinois formulated the almost universally accepted definition of the credit card contract.

In *Garber v. Harris Trust*, the plaintiff received notice of the card issuer's intent to modify the terms of his account.[206] Garber sued, representing a class, asserting the credit card contract was formed when the card was issued so that the issuers could not unilaterally change the terms without new consideration.[207] Harris and other banks in the class maintained issuance of the card was merely a standing offer to extend credit.[208] One needed to use the card before there was a contract.[209] Therefore, the issuers could modify the terms at will without new consideration.

The court agreed the card itself was a standing offer, which meant each *use* of the card is a separate contract governed by the terms and conditions in place at the time of each use.[210] Because the card is only an offer, the issuer could modify the terms at will.[211]

In dismissing Garber's claim that issuers were bound to honor the same terms forever, the court reviewed a basic concept of contract law: consideration.[212] Garber asserted providing credit information and submitting to a credit check constituted consideration.[213] The court found for a performance or a return promise to constitute consideration, it must be bargained for.[214] When you apply for credit, there is no bargaining: if you wanted

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205 DONALD H. MAFFLY AND ALEX C. MCDONALD, *The Tripartite Credit Card Transaction: A Legal Infant*, 48 CAL. L. REV. 459, 461 (1960).

206 Garber v. Harris Trust & Sav. Bank, 432 N.E.2d 1309, 1310 (Ill. App. 1982).

207 *Id.*

208 *Id.* at 1311.

209 *Id.*

210 *Id.* at 1312.

211 *Id.*

212 *Id.* at 1313.

213 *Id.*

214 *Id.*

the card, you had to submit to those checks.

The court also found there was no mutuality of obligations.[215] If you never use the card, you were not subject to the terms.[216] Likewise, if the consumer never makes a charge, the issuer does not have to perform its duties under the contract.[217] With this understanding, the terms, if they were a contract, had no effective termination date.[218] As such, the cardholder agreement was a contract of indefinite duration which, by its nature, was terminable or modifiable at will under long standing contract law.[219]

In fact, the court held modifications could also have a *retroactive* effect on balances accrued under the old terms.[220] Any unpaid balances would be subject to the new terms, but only if the cardholder uses the card after modifications were sent.[221] By using the card, the cardholder essentially "refinanced his existing balance under new arrangement."[222]

Garber was decided almost a quarter century ago. Notwithstanding its age, *Garber* has come to be known nationally as the most reasonable explanation of the formation of a credit card contract.[223] Indeed, its reasoning provided the basis of several recent Illinois decisions involving credit card complaint pleading standards: *Portfolio Acquisitions v. Feltman, Asset Acceptance v. Tyler* and *Razor Capital v. Antaal.*[224]

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[215] *Id.*

[216] *Id.*

[217] *Id.*

[218] *Id.* at 1313-14.

[219] *Id.* at 1314.

[220] *Id.*

[221] *Id.* at 1315.

[222] *Id.* (citing *Beck v. First National Bank* (Minn 1978) 270 N.W.2d 281)

[223] *See* Sharp Elecs. Corp. v. Deutsche Fin. Servs. Corp., 216 F.3d 388, 394 (4th Cir. 2000); Ramirez v. Palisades Collection LLC, (250 F.R.D. 366 (N.D.Ill. 2008); Parkis v. Arrow Fin. Servs., LLC, No. 07 C 410, 2008 WL 94798, 1 (N.D. Ill.2008); Schoppert v. CCTC Int'l, Inc., 972 F. Supp. 444, 447 (N.D. Ill. 1997); Jenkins v. Gen. Collection Co., 538 F. Supp. 2d 1165, 1174 (D. Neb. 2008); Taylor v. First N. Am. Nat'l Bank, 325 F. Supp. 2d 1304, 1313 (M.D. Ala. 2004); Grasso v. First USA Bank, 713 A.2d 304, 309 (Del. Super. 1998); *In re* Viva, 414 B.R. 301, 306 (Bankr. E.D. Tenn. 2008).

[224] Portfolio Acquisitions, L.L.C. v. Feltman, 909 N.E.2d 876 (Ill. App. 3d 2009); Asset Acceptance LLC v. Tyler, 966 N.E.2d 1039 (Ill. App.. 3d. 2012) and Razor Capital v. Antaal, 972 N.E.2d 1238 (Ill. App. 2d 2012).

XVII. THE BIGGEST UNINTENDED CONSEQUENCE OF THEM ALL

Whether or not one believes former Vice President Al Gore, it may be said with some confidence that *Garber* made e-commerce possible. By focusing on the act of using the card, not a physical signature, it enabled us to enter an era where we need not leave home to engage in trade. The impact of e-commerce is such that the phrase Black Friday is stated synonymously with its modern counterpart Cyber Monday, even if 'cyber' has fallen out of favor as the adjective de jour to describe on-line activities.

In 1999, William M. Daley, then head of the Commerce Department, in a report on the new phenomenon of e-commerce, stated its promise was a "future with more opportunity for all Americans."[225] This statement was made even as the report noted e-commerce accounted for less than 1% of the economy.[226] Daley was not far off. In 2012, worldwide e-commerce sales accounted for $1 trillion dollars in sales.[227] In the U.S. alone, $364 billion in sales were recorded.[228]

The internet as we know it, with portable access via a mobile device possessing more computing power than the computers in existence in 1999, would not have occurred without the creation of the credit card and the cashless society. Government, in this instance, encouraged its growth with the passage of the Electronic Signatures in Global and National Commerce Act, cleverly going under the acronym of ESIGN.[229] The stated purpose of which was to facilitate the use of electronic records and signatures in interstate and foreign commerce by ensuring the validity and legal effect of contracts entered into electronically.

As you recall in *Marquette*, some twenty-five years before E-Sign was passed, made clear national banks were not bound by state laws regarding usury. Seeing the potential of e-commerce,

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[225] WILLIAM M. DALEY, THE EMERGING DIGITAL ECONOMY II (Jeffrey Mayer ed. U.S. Dept. of Commerce, June 1999).

[226] *Id.*

[227] EMARKETER *Ecommerce Sales Topped 1 Trillion for the First Time in 2012* (Feb. 5, 2013), http://www.emarketer.com/Article/Ecommerce-Sales-Topped-1-Trillion-First-Time-2012/1009649.

[228] *Id.*

[229] Electronic Signatures in Global and National Commerce Act, 15 U.S.C. § 7001 (2000). It received the acronym E-Sign in http://www.sec.gov/rules/interp/33-7985.htm.

Congress avoided any lag in states amending their laws by ESIGN explicitly pre-empted state laws to impose uniformity regarding electronic transactions.[230] The statute also provides that should a state enact the Uniform Electronic Transactions Act (EUTA) a model state law,[231] any deviation was limited to state statutes meeting certain conditions.[232] It specifically forbade states from adopting EUTA with modifications to force non-electronic delivery methods for documents or to enact laws giving greater weight to physical documents over electronic forms.[233] Accordingly, Illinois passed the Illinois' Electronic Commerce Security Act, eliminating physical signatures in all statutes save those that met the limited exceptions found within ESIGN.[234]

XVIII. CONCLUSION

Our story began with the understanding that commerce and credit have been intertwined since before recorded time. Despite the passage of thousands of years, Aristotle's concept of creditors being something unnatural has persisted. Credit cards, now regulated more strongly by the CFPB and the Card Act, have been called a drug by some and worse by others. These extreme views do not help discussions on the causes of our current financial problems.

Unfortunately, we as humans, suffer what Alan Greenspan presciently described as "irrational exuberance." By that he meant we always seek ways to get rich quickly despite ample centuries of evidence. In the 17th century, it was the Dutch and tulips (yes, that is not a typo).[235] A century later, it was the French and the "Mississippi Company" in which the government invested so much, it crippled the French economy for a decades.[236] Around the same time, England had to work through

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[230] Electronic Signatures in Global and National Commerce Act, 15 U.S.C. § 7002 (2000).

[231] *Id.*

[232] *Id.*

[233] Electronic Signatures in Global and National Commerce Act, 15 U.S.C. § 7002 (2000).

[234] Electronic Commerce Security Act, 5 Ill. Comp. Stat. § 175/1-105 (1999).

[235] This unusual investment choice is discussed in detail in MIKE DASH, TULIPOMANIA : THE STORY OF THE WORLD'S MOST COVETED FLOWER & THE EXTRAORDINARY PASSIONS IT AROUSED (Random House 2001).

[236] FERGUSON, *supra* note 1, at 139-58.

the South Seas crash.[237] For us, it has been the stock market crash of 1929, which precipitated the Depression, and more recently the tech-stock bubble and our most recent real estate bubble.

What makes such bubbles possible in the incredible interconnectivity of the world economy? Without realizing it, this interconnectivity touches each of us personally. If you have a 401(k), it is very likely you are investing in a bank that issues credit cards and want that 401(k) to grow. Growth in stock value requires profitability and sales, meaning, the bank needs more credit card customers and more credit card purchases. While no one likes collection attorneys, if we want the costs of borrowing to be low and stock prices to remain high, we need creditors and their attorneys to recover these losses. If done ethically and with an understanding of the consumer's circumstances, some good can come of these efforts, both for the creditor and for the consumer, as they may, over time, eliminate debt and restore their credit.

Like anything in life, credit cards can be a boon or, in the wrong circumstances, be a great evil. It is likely that our natural fear and distrust of credit has much to do with the instinctive fear that a change in circumstances can lead to financial ruin. Almost like the post-war era, in the real estate boom, many of us may have shed our instinct to plan for the worst. The economy changes every day and new vehicles of lending and loaning will always be with us, stepping just ahead of regulation or a true understanding of the consequences. In the end, it is we, as citizens and consumers, who must make informed personal choices and political selections to insure against the turbulence of the modern economy.

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[237] *Id.* at 158.