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INTRODUCTION

The Truth in Lending Act, with accompanying implemental regulations, is designed to provide uniform methods for the disclosure of credit terms by lenders. This affords consumers an opportunity to make informed choices in the selection of credit. The Act represents a congressional response to the public need for the fair and honest appraisal of actual costs of using the funds of another.

In order to secure creditor compliance with its many disclosure

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3. The section of the Truth in Lending Act that delineates the congressional findings and declaration of purpose provides in pertinent part:

   The Congress finds that 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.

requirements, the Truth in Lending Act incorporates a criminal
penalty,\(^*\) as well as administrative\(^*\) and private civil enforcement
provisions.\(^\dagger\) A significant role is envisioned for the private Truth in
Lending litigant in effectuating the purposes of the Act.\(^\dagger\) Specifically,
the consumer litigant assumes the role of a private attorney
general in the enforcement of the disclosure requirements.\(^\dagger\)
Certain problems have arisen, however, with respect to the procedural rela-
tionship between Truth in Lending claims and creditor contract
claims. The characterization of these claims, both as counterclaims
and defenses, conceivably deters the potential prophylactic effect
of private enforcement suits, particularly with respect to class
actions.

This article will describe the role of the private litigant in Truth
in Lending Act enforcement and the elements of a private cause of
action. Secondly, the specific substantive questions raised by the
procedural characterization problem will be examined. The major-
ity and minority positions of the federal counts on this issue will
be analyzed. The analysis will demonstrate that uniform resolution
of this procedural issue in the federal courts is critical to the pri-
vate attorney general concept underlying effective enforcement of
the Truth in Lending Act. Finally, the discussion will focus on the
anomalous Truth in Lending defense cognizable in Illinois which
can operate to foreclose the effective enforcement of a creditor’s
contract claim.

PRIVATE ENFORCEMENT UNDER THE TRUTH IN LENDING ACT

The Consumer as a Private Attorney General

The role of the consumer-plaintiff as a private attorney general
is of paramount importance under the Truth in Lending Act in
effectuating creditor compliance. No independent federal agency
was created to enforce the Act.\(^\dagger\) More importantly, none of the
existing agencies which possess joint responsibility for administra-
tive enforcement of the Act were granted enforcement powers


\(^{8}\) See text accompanying notes 10 through 18 infra.


greater than what they had prior to the Act. Finally the Act's criminal sanctions are applicable to only a narrow class of cases, and involve inherent difficulties in proof. Thus, the limited nature of the administrative and criminal enforcement mechanisms clearly elevates the role of the private consumer litigant in enforcement of the Act.

The importance of private litigation is also evident in the context of the class action. While not originally contemplated by Congress, consumer class actions predicated upon purported truth in lending disclosure violations soon became commonplace. Federal courts, however, began to refuse to grant class certification in many truth in lending actions due in part to concern over the potential for disproportionate liability of a creditor in a class action award. In confronting this situation, Congress tried to balance the potential for disproportionate liability against the positive deterrent effect and the resultant incentive for creditor compliance associated with the threat of class action liability. A compromise was enacted which placed an upper limit on the total

11. Id.
12. Criminal actions and penalties are limited to situations involving "willful and knowing" violations of the Act. In pertinent part the Act provides:

Whoever willfully and knowingly

(1) gives false or inaccurate information or fails to provide information which he is required to disclose under the provisions of this subchapter or any regulation issued thereunder,

(2) uses any chart or table authorized by the Board under section 1606 of this title in such a manner as to consistently understate the annual percentage rate determined under section 1606(a)(1)(A) of this title, or

(3) otherwise fails to comply with any requirement imposed under this subchapter, shall be fined not more than $5,000 or imprisoned not more than one year, or both.

14. For a discussion of the problems created by the Truth in Lending class action prior to the 1974 congressional amendments, see Comment, The Truth In Lending Class Action, 40 Albany L. Rev. 753 (1976); Note, Class Actions Under the Truth in Lending Act, 83 Yale L.J. 1410 (1974).
17. Id. at 14-15. See also Annual Report To Congress On Truth In Lending For The Year 1972, S. 914, 93d Cong., 1st Sess., reprinted in 119 Cong. Rec. 4596 (1973). This com-
amount of recovery in a truth in lending class action. This action demonstrates congressional recognition and reaffirmation of the significant function private litigation plays as a means of achieving creditor compliance with the terms of the Act.

Key Issues and Elements Relevant to a Truth in Lending Enforcement Action

The Truth in Lending Act requires creditors to comply with all disclosure requirements mandated by the Act and the regulations promulgated thereunder. The Federal Reserve Board is specifically empowered to prescribe regulations to carry out the Act's primary objective of full and fair disclosure of credit terms. Pursuant to this directive, the Board has promulgated a massive collection of regulations, generally known as "Regulation Z," which specifically delineate the language and format required for proper credit disclosure under the Act.

Standing to bring suit under the Truth in Lending Act is automatically conferred upon any consumer who is exposed to a disclo-
Sure violation, so long as he is an obligor on the contract. Moreover, because standardized terminology is regarded as a prerequisite to enlightened comparative credit shopping, there is no standing requirement of deception, reliance or misunderstanding on the part of a plaintiff. In short, a plaintiff is not required to sustain any damage, or to actually make a misinformed credit choice. Instead, the law presumes that violations of the Act have injured the consumer by frustrating the full and fair disclosure objective.

The individual plaintiff or plaintiff-class has a minimal burden of proof in establishing a Truth in Lending violation. Because the Act is intended to be liberally construed, lenders are required to adhere precisely to the law and particularly to Regulation Z.


The law enables multiple obligors to file suit on the same credit instrument and individually recover. For example, a husband and wife who sign as joint obligors would both be able to sue and each could individually recover the statutory penalty. The legislative history reveals that Congress requires only one disclosure statement for joint obligors simply to reduce paperwork. “For example, if two people (e.g. husband and wife) are the obligors only one copy . . . would need to be furnished.” H.R. REP. No. 1040, 90th Cong., 1st Sess. (1967), reprinted in [1968] U.S. CODE CONG. & ADMIN. NEWS, 1962, 1984. There is no indication that Congress intended to limit the liability of each lender to a single obligor. Smith v. No. 2 Galesburg Crown Finance Corp., 615 F.2d 407, 416 (7th Cir. 1980); Mirabel v. General Motors Acceptance Corp., 537 F.2d 871, 882-83 (7th Cir. 1976); Allen v. Beneficial Finance Co., 531 F.2d 797, 805-06 (7th Cir. 1976).


25. Smith v. Chapman, 614 F.2d 968, 971 (5th Cir. 1980).


28. Smith v. Chapman, 614 F.2d 968, 971 (5th Cir. 1980).


31. Smith v. No. 2 Galesburg Crown Finance Corp., 615 F.2d 407 (7th Cir. 1980); Smith
that is required of the plaintiff is a showing that the loan or credit instrument failed to comply with the disclosure requirements of the statute or the regulations promulgated thereunder.\(^{38}\)

The issue of compliance is measured by an objective standard.\(^{33}\) Allegations of substantial compliance or meaningful disclosure are weighed objectively against the regulatory requirements.\(^{34}\) Strict adherence is required and minor deviations are not excused.\(^{38}\)

Neither the lender's good faith, nonliability under state law, nor reasonableness of conduct are relevant to a determination under the Act.\(^{38}\)

A finding of noncompliance with any aspect of the Act or Regulation Z may result in both criminal\(^{37}\) and civil liability.\(^{38}\) The most significant civil liability provision is section 1640,\(^{38}\) which permits

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32. "Except as otherwise provided in this section, any creditor who fails to comply . . ."


33. Smith v. Chapman, 614 F.2d 968, 971 (5th Cir. 1980).

34. Id. Recently, the United States Supreme Court described meaningful disclosure:

"The concept of meaningful disclosure that animates TILA [the Truth in Lending Act] . . . cannot be applied in the abstract. Meaningful disclosure does not mean more disclosure. Rather, it describes a balance between competing considerations of complete disclosure . . . and the need to avoid . . . informational overload.


35. Smith v. Chapman, 614 F.2d 968, 971 (5th Cir. 1980).


It is possible to seek both statutory damages under § 1640 and rescission under § 1635. Reid v. Liberty Consumer Discount Co., 484 F. Supp. 435 (E.D. Pa. 1980). Section 1635 provides for rescission to make the debtor whole, while § 1640 is a "penalty" provision designed to compel disclosure. Palmer v. Wilson, 502 F.2d 860 (9th Cir. 1974). Although the two remedies are not exclusive, their combined potential for harshness can be averted by the court’s exercise of discretion. Just because both are alleged, the court is still entitled to exercise its "sense of equity" in making awards. Palmer v. Wilson, 502 F.2d 860, 862 (9th Cir. 1974). See also Williams v. Public Finance Corp., 598 F.2d 349 (5th Cir. 1979); Sellers v. Wollman, 510 F.2d 119 (5th Cir. 1975).


§ 1640. Civil liability — Individual or class action for damages; amount of award; factors determining amount of award

(a) Except as otherwise provided in this section, any creditor who fails to comply with any requirement imposed under this part or part D or E of this subchapter with respect to any person is liable to such person in an amount equal to the sum
consumers to bring an action for damages. Damages under this

(1) any actual damage sustained by such person as a result of the failure;
(2)(A)(i) in the case of an individual action twice the amount of any finance charge in connection with the transaction, or (ii) in the case of an individual action relating to a consumer lease under part E of this subchapter, 25 per centum of the total amount of monthly payments under the lease, except that the liability under this subparagraph shall not be less than $100 or greater than $1,000; or
(B) in the case of a class action, such amount as the court may allow, except that as to each member of the class no minimum recovery shall be applicable, and the total recovery in such action shall not be more than the lesser of $500,000 or 1 per centum of the net worth of the creditor; and
(3) in the case of any successful action to enforce the foregoing liability, the costs of the action, together with a reasonable attorney's fee as determined by the court.

In determining the amount of award in any class action, the court shall consider, among other relevant factors, the amount of any actual damages awarded, the frequency and persistence of failures of compliance by the creditor, the resources of the creditor, the number of persons adversely affected, and the extent to which the creditor's failure of compliance was intentional.

Correction of error within fifteen days
(b) A creditor has no liability under this section for any failure to comply with any requirement imposed under this part or part E of this subchapter if within fifteen days after discovering an error, and prior to the institution of an action under this section or the receipt of written notice of the error, the creditor notifies the person concerned of the error and makes whatever adjustments in the appropriate account are necessary to insure that the person will not be required to pay a charge in excess of the amount or percentage rate actually disclosed.

Unintentional violations; bona fide errors
(c) A creditor may not be held liable in any action brought under this section for a violation of this subchapter if the creditor shows by a preponderance of evidence that the violation was not intentional and resulted from a bona fide error notwithstanding the maintenance of procedures reasonably adapted to avoid any such error.

Liability of subsequent assignees of original creditor
(d) Any action which may be brought under this section against the original creditor in any credit transaction involving a security interest in real property may be maintained against any subsequent assignee of the original creditor where the assignee, its subsidiaries, or affiliates were in a continuing business relationship with the original creditor either at the time the credit was extended or at the time of the assignment, unless the assignment was involuntary, or the assignee shows by a preponderance of evidence that it did not have reasonable grounds to believe that the original creditor was engaged in violations of this part, and that it maintained procedures reasonably adapted to apprise it of the existence of any such violations.

Jurisdiction of courts
(e) Any action under this section may be brought in any United States district court, or in any other court of competent jurisdiction, within one year from the date of the occurrence of the violation.

Good faith compliance with rule, regulation, or interpretation of Board or with interpretation or approval of duly authorized official or employee of
section include a statutory penalty computed according to a particular finance charge,\(^4\) and any actual damages\(^4\) sustained by the plaintiff.

The consumer, as a private attorney general, has a clear mandate from Congress and the courts to enforce compliance with the disclosure requirements of the Truth in Lending Act. The enforcement purpose of the Act is enhanced by a relatively simple and straightforward burden of proof. Nevertheless, certain procedural barriers may impede the consumer's ability to ensure full compliance with the Act.

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Federal Reserve System.

(f) No provision of this section or section 1611 of this title imposing any liability shall apply to any act done or omitted in good faith in conformity with any rule, regulation, or interpretation thereof by the Board or in conformity with any interpretation or approval by an official or employee of the Federal Reserve System duly authorized by the Board to issue such interpretations or approvals under such procedures as the Board may prescribe therefor, notwithstanding that after such act or omission has occurred, such rule, regulation, interpretation, or approval is amended, rescinded, or determined by judicial or other authority to be invalid for any reason.

Recovery for multiple failures to disclose

(g) The multiple failure to disclose to any person any information required under this part or part D or E of this subchapter to be disclosed in connection with a single account under an open end consumer credit plan, other single consumer credit sale, consumer loan, consumer lease, or other extension of consumer credit, shall entitle the person to a single recovery under this section but continued failure to disclose after a recovery has been granted shall give rise to rights to additional recoveries.

Offset from amount owed to creditor

(h) A person may not take any action to offset any amount for which a creditor is potentially liable to such person under subsection (a)(2) of this section against any amount owing to such creditor by such person, unless the amount of the creditor's liability to such person has been determined by judgment of a court of competent jurisdiction in an action to which such person was a party.


The Seventh Circuit has noted that the statutory damages are designed to liquidate "uncertain actual damages," as well as encourage suits to enforce the Act. Smith v. No. 2 Galesburg Crown Finance Corp., 615 F.2d 407, 415 (7th Cir. 1980). Nevertheless, it is clear that a private litigant can pursue both the statutory remedy and a remedy for any actual damages incurred through a § 1640 action. Actual damages, obviously, are not required for a Truth in Lending action. Johnson v. Household Finance Corp., 453 F. Supp. 1327 (S.D. Ill. 1978).
The counterclaim is an integral mechanism to the federal rules’ liberal joinder policy. Counterclaims have their genesis in the common law doctrines of set-off and recoupment. Rule 13 of the Federal Rules of Civil Procedure resembles former Equity Rule 30, which required assertion of counterclaims arising out of the subject matter of the suit. Furthermore, Rule 13 incorporates the philosophy of the earlier rules by discouraging circuitous actions and multiple litigation.

Under Rule 13, a counterclaim is characterized as either compulsory or permissive. A compulsory counterclaim is defined as one which arises out of the same transaction or occurrence that creates the subject matter of the opposing litigant’s claim. An independent basis for federal jurisdiction is not required for a compulsory counterclaim; such a claim automatically falls under the ancillary jurisdiction of the court. If a litigant fails to assert a compulsory counterclaim, he will be foreclosed from bringing the claim in a subsequent independent suit. In contrast, a permissive counter-
claim cannot be entertained by the court unless it independently meets federal jurisdictional prerequisites, and where it is excluded from the federal suit, it will not be barred in later actions.

In determining the status of a counterclaim, the federal courts generally have applied four alternative tests to evaluate whether claims "arise out of the same transaction or occurrence": (1) whether the issues of law and fact are largely the same; (2) whether the doctrine of res judicata would bar a subsequent suit without the compulsory counterclaim rule; (3) whether the same evidence supports both the plaintiff's and the defendant's claims; and, (4) whether there is any logical relationship between the claim and the counterclaim. Of these four standards, the "logical relationship" test is the most frequently applied. This test is favored by the courts because it permits flexibility and realistic appraisal of individual fact situations. Moreover, it is a broad approach which circumvents multiple suits.

In a Truth in Lending Act proceeding, the federal counterclaim mechanism creates significant problems which work to frustrate the enforcement objective of the Act. The problems emanate from the characterization of a counterclaim as compulsory or permissive. The problem is not merely a procedural one, however, since a court's determination of the issue has a significant impact on the availability of a federal forum for the Truth in Lending Act plaintiff, particularly in the class action context. The most troublesome cases involve those counterclaims that flow from the loan or credit instrument which is under attack for allegedly violating the

51. Fed. R. Civ. P. 13(b) provides: "A pleading may state as a counterclaim any claim against an opposing party not arising out of the transaction or occurrence that is the subject matter of the opposing party's claim."


53. Wright & Miller, supra note 43, at § 1420.

54. For a thorough discussion of the merits and disadvantages of each test, see Wright & Miller, supra note 43, at § 1410.


57. See notes 1 through 4 supra and accompanying text.

58. See text accompanying notes 99 and 105, infra.
Act. Potential counterclaims by the lender relating to default, performance or contract validity may become issues in the litigation concerning disclosure violations, and may operate to frustrate enforcement of the Act. The courts have split on the issue of how to characterize the defendant-lender's counterclaim based on varying interpretations of the federal policies underlying counterclaims and the Truth in Lending Act.

The Majority Position: The Permissive Debt Counterclaim

The majority of courts have determined that debt counterclaims are permissive. Accordingly, any such debt counterclaim must have an independent jurisdictional basis before it will be entertained in federal court. This conclusion flows from the conceptual distinctions between the disclosure violation and the contractual obligation.

The Fourth Circuit was the first federal appellate court to grapple with the problems relating to counterclaims in Truth in Lending Act litigation. In Whigham v. Beneficial Finance Company, the court delineated three reasons for finding the lender's debt claim to be permissive. First, the lender's claim was governed by state law and raised issues of law and fact that were separate and distinct from those raised by the Truth in Lending claim. Thus, the claims did not share any of the joint characteristics required

59. See notes 61 and 78 infra and accompanying text.
60. See notes 63 and 86 infra and accompanying text.
62. See note 61 supra and accompanying text.
63. Basham v. Finance American Corp., 583 F.2d 918, 928 (7th Cir. 1978) ("The Truth in Lending Act claim is not directed at or an answer to the underlying debt").
64. 599 F.2d 1322 (4th Cir. 1979).
65. Id. at 1324. As the Fourth Circuit stated: "The only question in the borrower's suit is whether the lender made disclosures required by the federal statute and its implementing regulations. The lender's counterclaim, on the other hand, requires the court to determine the contractual rights of the parties in accordance with state law." Id. (citations omitted).
for a finding that the counterclaims were in fact compulsory.\textsuperscript{66} Second, proof of each claim required different pieces of evidence and would inject a myriad of unrelated concerns into the Truth in Lending proceeding.\textsuperscript{67} Thus, the debt counterclaim posed potential issues that exceeded the scope of the proof required for the Truth in Lending claim.\textsuperscript{68} Furthermore, the court felt that the potential for confusion and complexity was antagonistic to the congressional intent to provide the consumer with easy access to the courts to pursue enforcement of the Act. The straight-forward prima facie case delineated by congress in the Act indicated an intent to permit the consumer to achieve enforcement easily. Finally, the Truth in Lending claim and the debt claim were not considered to be logically related,\textsuperscript{69} even though they emanated from the same credit instrument.\textsuperscript{70} Unlike the debt claim, the Truth in Lending claim did not arise from the contractual obligation.\textsuperscript{71} Furthermore, because the debt collection claim was not of federal origin, it was felt that it should not be used as a manipulative tactic to impede Truth in Lending Act enforcement.\textsuperscript{72}

\textsuperscript{66} Id. at 1323.
\textsuperscript{67} Id. at 1324. \textit{See also} Agostine v. Sidcon Corp., 69 F.R.D. 437 (E.D. Pa. 1975). While only the loan instrument will be necessary to prove the Truth in Lending claim the lender will have to prove default. Moreover, the lender's claim can be challenged via standard contract defenses and may involve such concerns as performance, warranty, consideration and other contract issues. Also, the proof of default may raise collateral matters concerning negotiable instruments and security interests. \textit{See, e.g.}, Hinkle v. Rock Springs Nat'l Bank, 538 F.2d 295, 297 (10th Cir. 1976); Jones v. Goodyear Tire & Rubber Co., 73 F.R.D. 577, 579 (E.D. La. 1976).


\textsuperscript{69} Whigham v. Beneficial Finance Co., 599 F.2d 1322, 1324 (4th Cir. 1979).

\textsuperscript{70} \textit{Id. But see} Carter v. Public Finance Corp., 73 F.R.D. 488, 495 (N.D. Ala. 1977) (claims' joint origin from same credit instrument alone is sufficient to supply nexus required under Fed. R. Civ. P. 13(a)).

\textsuperscript{71} Whigham v. Beneficial Finance Co., 599 F.2d 1322, 1324 (4th Cir. 1979). Rather, the Truth in Lending claim flows from the Act's disclosure requirements and enforces those requirements by invoking a statutory penalty. \textit{Id. See also} Grey v. European Health Spas, Inc., 428 F. Supp. 841, 847-48 (D. Conn. 1977).

\textsuperscript{72} \textit{Id.} Courts have also recognized the distinct objectives of the two types of claims. Even though they originate in the same instrument, the claims devolve into issues that are fundamentally different. The Truth in Lending disclosure claim is grounded in federal law, whereas the debt counterclaim will be governed by state law.

On a purely transactional level, such a [logical] relationship obviously exists: both claim and counterclaim arise out of a singular occurrence . . . But in these circumstances, I do not consider the presence of transactional identity alone sufficient to establish, for compulsory counterclaim purposes, a logical relationship between plaintiff's claim and defendant's counterclaim . . . I find that the respective claims are "offshoots" of the same basic transaction, but not the "same basic con-
The Fourth Circuit's position can be supported for other reasons as well. By holding that the debt claim is permissive, a potential problem concerning the right to a jury can be circumvented from the outset of the litigation. It is doubtful that a Truth in Lending plaintiff is entitled to a jury trial. In contrast, a defendant could demand a jury trial to determine the merits of a debt counterclaim. The plaintiff would be entitled to a separate trial to avoid prejudice. Consequently, the objective of judicial economy would be defeated under these circumstances.

In jurisdictions which deem counterclaims to be permissive lenders often urge courts to change their position on the counterclaim issue by raising the spectre of res judicata. Res judicata, however, will only bar a lender's subsequent debt claim if the claim is deemed to be compulsory. The strongest support for the majority view is found in its appropriate solicitude for the objectives sought to be enforced by the Truth in Lending Act. The exclusion of debt counterclaims in the Truth in Lending Act proceeding not only eliminates potentially cumbersome litigation, but also eliminates the potential deterrent effect of these claims. Although debtors are not relieved of contract liability, they do not have to battle the issue contemporaneously with the disclosure violation. The enforcement role of the consumer-plaintiff is buttressed, and the objectives of the Act are closer at hand. By holding the debt counterclaim permissive, the federal policies underlying the Truth in Lending Act are best served.

73. See Jones v. Goodyear Tire & Rubber Co., 73 F.R.D. 577, 580 (E.D. La. 1976). Actions under the Act have been considered to be sui generis and covered by the right to jury trial at law. Id.

The equity jurisdiction of the court is invited when rescission is sought under 15 U.S.C. § 1635. Because the § 1635 rescission remedy may be joined with a § 1640 statutory penalty action, it seems apparent that this is not an action at law. See note 38, supra.

74. See Plant v. Blazer Financial Services, Inc., 598 F.2d 1357, 1362 (5th Cir. 1979).

75. See note 99 supra.


77. This is consonant with the rule that the Truth in Lending Act should be liberally construed so as to achieve its remedial purpose. See Mirabel v. General Motors Acceptance Corp., 537 F.2d 871 (7th Cir. 1976); Sellers v. Woolman, 510 F.2d 119, 122 (5th Cir. 1975); Eby v. Reb Realty, Inc., 495 F.2d 646, 650 (9th Cir. 1974).
The Minority View: The Compulsory Debt Counterclaim

A minority of the courts have determined that the lender's debt counterclaim is compulsory within the meaning of Federal Rule 13. In determining whether the counterclaims arise out of the same "transaction or occurrence," these courts have applied a strict analysis and interpretation of Rule 13 to find that the Truth in Lending Act claim and the debt counterclaim do in fact arise from the same credit instrument. Thus, because of the joint origin, the two claims are so "logically related" that any counterclaim based on the underlying debt must be considered compulsory.

This strict interpretation allegedly effectuates the liberal joinder policy of the federal rules for three reasons. First, the two claims will involve common issues of proof, since the Truth in Lending action will require introduction of the loan or credit instrument. Second, the counterclaim will require only minimal additional proof of default. Finally, the compulsory counterclaim is specifi-
cally designed to provide complete relief to the defendant who is involuntarily brought into federal court. Thus, a court's simultaneous adjudication of the debt claim with the Truth in Lending Act claim eliminates wasteful litigation and promotes judicial economy.

Proponents of the minority view posit that not only is their approach consistent with the policy underlying the federal rules on joinder, but also that the Truth in Lending Act supports the conclusion that the debt counterclaim should be deemed compulsory. It is urged that because the Act was designed to afford "even-handed treatment" to debtors and creditors, it should not be used to foreclose a creditor from pursuing a claim on the credit instrument. Unless the creditor is permitted to assert his claim in the Lending Act adjudication, it is argued that he may be prejudiced by a finding of a disclosure violation. Moreover, since both state and federal courts have jurisdiction over Truth in Lending claims, it is argued that there is a presumption that Congress intended the debt counterclaim to be adjudicated with the disclosure claim. A contrary analysis would always permit a plaintiff to


84. Plant v. Financial Services, Inc., 598 F.2d 1357, 1364 (5th Cir. 1979); Revere Copper & Brass, Inc. v. Aetna Cas. & Sur. Co., 426 F.2d 709, 715.

Defendant's affirmative assertion of a compulsory counterclaim will not waive his objections to personal jurisdiction or venue. In contrast, the assertion of permissive counterclaims will waive those objections. WRIGHT & MILLER, supra note 43, at § 1409 at 39.


86. Id. at 1364.


The court in Bolden held that the plaintiffs' Truth in Lending Act claim is closely related to a state fraudulent advertising violation, thus making the exercise of pendant jurisdiction proper. Similarly, the court noted that the state counterclaim is "logically related." Because the plaintiff had interjected state issues into the litigation, he should not be heard to assert that the defendant's state claim is attenuated. Id. at 620-21.

88. Plant v. Financial Services, Inc., 598 F.2d 1357, 1364 (5th Cir. 1979).


90. Plant v. Financial Services, Inc., 598 F.2d 1357, 1364 (5th Cir. 1979) See also Stokes
bring suit in federal court, where the debt claim is out of reach. Proponents argue that Congress did not intend to insulate debtors in federal courts from lender's counterclaims.

Effect on the Private Litigant

Denomination of debt counterclaims as compulsory is troublesome for several reasons. First, there is an implicit assumption that the federal court is accomplishing that which a state court would otherwise have power to do. This implies that if the action were filed in a state court, the debt counterclaim would always be compulsory. This is simply not true. For example, in Illinois, where all counterclaims are permissive, the debt counterclaim would not necessarily be asserted in a suit brought in state court under the federal statute. Consequently, the filing of a Truth in Lending action in a state court would not always compel litigation of the debt counterclaim. More fundamentally, it is questionable that

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91. Plant v. Financial Services, Inc., 598 F.2d 1357, 1364 (5th Cir. 1979).
92. Id. Several courts have said that the courts should be wary of permitting "the Truth In Lending Act to be used simply as a means to obtain a federal forum for ordinary debtor-creditor controversies between citizens of the same State." Hughes v. Ford Motor Credit Co., 360 F. Supp. 15, 19 (E. D. Ark. 1973). See also Price v. Franklin Investment Co., 574 F.2d 594, 607 n.29 (D.C. Cir. 1978); Solevo v. Aldens, Inc., 395 F. Supp. 861, 864 (D. Conn. 1975). Notwithstanding this caution, it is unlikely that a debtor will raise the debtor-creditor contract issues as pendant claims. Instead, the creditor will be attempting to interject issues of default by way of counterclaims. The district court can circumvent all the contract issues by holding that the counterclaims are permissive. See discussion infra.
93. There is no doubt the compulsory counterclaim rule is applicable even though the state does not have a comparable requirement. See C. WRIGHT, LAW OF THE FEDERAL COURTS § 79 at n.34 (3d ed. 1976) and citations contained therein. In subsequent litigation states are not at liberty to disregard a claimant's failure to plead his compulsory counterclaim in federal court. Id.
94. Section 38 of the Illinois Civil Practice Act reads in pertinent part:
§ 38. Counterclaims. (1) Subject to rules, any demand by one or more defendants against one or more plaintiffs, or against one or more codefendants, whether in the nature of setoff, recoupment, cross demand or otherwise, and whether in tort or contract, for liquidated or unliquidated damages, or for other relief, may be pleaded as a cross demand in any action, and when so pleaded shall be called a counterclaim.
95. Id.
96. Even where the state provides for compulsory counterclaims, the Truth in Lending claim may not definitionally satisfy the test. Consequently, the contract claim and Truth in Lending claim may not be asserted in the same state suit. At least one federal court has refused to hold that the failure to assert the Truth in Lending claim in the contract action estops assertion later in federal court. Drew v. Flagship First Nat'l Bank, 448 F. Supp. 434, 436-37 (M.D. Fla. 1977). Since this holding, however, the Fifth Circuit has held that the Truth in Lending claim is compulsory under the federal rules. 598 F.2d 1357 (5th Cir. 1979).
Congress ever intended these actions to be tried together. The availability of alternative forums does not provide evidence of a congressional intent that credit claims be tried with the federal Truth in Lending claim. Finally, congressional silence on debt counterclaims does not represent an intent to either include or exclude these claims. Rather, it is more plausible to suggest that this silence is attributable to a perception that the Truth in Lending Act deals with matters outside the contract.


98. More specifically, enforcement actions brought under § 1640 are designed to provide a civil penalty for violations of the Act. Thus, this section is not designed to make the plaintiff whole. Palmer v. Wilson, 502 F.2d 860 (9th Cir. 1974). Thus, unlike § 1635, which permits rescission, the substantive contract claims are not responsive to the original claim in a § 1640 action.

15 U.S.C. § 1635 provides in pertinent part:

(a) Except as otherwise provided in this section, in the case of any consumer credit transaction in which a security interest, including any such interest arising by operation of law, is or will be retained or acquired in any real property which is used or is expected to be used as the residence of the person to whom credit is extended, the obligor shall have the right to rescind the transaction until midnight of the third business day following the consummation of the transaction or the delivery of the disclosures required under this section and all other material disclosures required under this part, whichever is later, by notifying the creditor, in accordance with regulations of the Board, of his intention to do so. The creditor shall clearly and conspicuously disclose, in accordance with regulations of the Board, to any obligor in a transaction subject to this section the rights of the obligor under this section. The creditor shall also provide, in accordance with regulations of the Board, an adequate opportunity to the obligor to exercise his right to rescind any transaction subject to this section.

(b) When an obligor exercises his right to rescind under subsection (a) of this section, he is not liable for any finance or other charge, and any security interest given by the obligor, including any such interest arising by operation of law, becomes void upon such a rescission. Within ten days after receipt of a notice of rescission, the creditor shall return to the obligor any money or property given as earnest money, downpayment, or otherwise, and shall take any action necessary or appropriate to reflect the termination of any security interest created under the transaction. If the creditor has delivered any property to the obligor, the obligor may retain possession of it. Upon the performance of the creditor's obligation under this section, the obligor shall tender the property to the creditor, except that if return of the property in kind would be impracticable or inequitable, the obligor shall tender its reasonable value. Tender shall be made at the location of the property or at the residence of the obligor, at the option of the obligor. If the creditor does not take possession of the property within ten days after tender by the obligor, ownership of the property vests in the obligor without obligation on
Even though the counterclaim issue is technically a matter of procedure, resolution of the issue has a significant impact on the availability of a federal forum for Truth in Lending violations. Thus, the counterclaim issue has substantive implications as well. The potential involvement of compulsory contract claims may have a chilling effect upon the private plaintiff's decision to bring suit. Because these actions concern consumer transactions it is possible that the aggrieved consumer is delinquent in his obligations. Ironically, the reason for a potential plaintiff’s delinquency may in fact be the deceptive credit practices of the creditor. The potential default recovery could, however, exceed the Truth in Lending Act award. Consequently, the consumer may be reluctant to bring suit for a statutory recovery when the end result might be a more substantial judgment being entered on the default. Thus, the incentive to bring an enforcement suit under the Act is defused.

There is no dispute that the Act is not designed to circumvent or vindicate a borrower’s debt liability. The problem is, however, that the private attorney general mechanism fails if the plaintiff is reluctant to bring a disclosure action. Although section 1640 is not designed to create a windfall for the plaintiff, the mechanism probably cannot succeed if the consumer-plaintiff risks both the

his part to pay for it.

99.  Conceivably, a middle course of action is possible. If a counterclaim can be shown to prejudice the opposing party, the court could order separate trials under Federal Rules 13(i) and 42(b). Separate judgments under Federal Rule 54(b) could be entered. This does very little, however, to alleviate the confusion presented by compulsory counterclaims. In fact, it would only further open the court's door to litigation of state claims that lack an independent jurisdictional basis.


This is a particularly difficult problem in class actions, where class members' maximum recovery may only be a few dollars. Id. In Carter, the court acknowledged that the presence of counterclaims exposed class members to greater liability than the statutory award. Nevertheless, the court found the counterclaims compulsory and noted that the class members would probably never bring suit individually because of the potential contract liability. Thus, they should not be permitted to circumvent the contract liability in a class action.


103.  Basham v. Finance America Corp., 583 F.2d 918, 928 (7th Cir. 1978) (“The design of the Truth in Lending Act was to provide protection to consumers by affording them meaningful disclosure and thereby an opportunity to shop for credit. It was not designed, nor should it be used to thwart the valid claims of creditors”).

104.  See generally Sellers v. Wollman, 510 F.2d 119, 122 (5th Cir. 1975).
entry of a judgment for default and the set-off of any statutory award.

Class Action Implications

The resolution of the counterclaim issue has the most significant impact in the context of the class action. Although the Act permits class recovery, the decision to certify a class action is committed to the court's discretion. In accordance with Rule 23, the federal court must make findings concerning numerosity of the class, commonality of issues, typicality of claims and adequacy of the class representatives. Additionally, the court must determine whether the class action is a superior method of adjudication by determining whether common issues of law or fact predominate over individual issues. In making this determination, four considerations must be weighed by the court: (1) the possible interest of individual control; (2) existing individual litigation; (3) the effects of concentrating the litigation and, (4) class management and administration. In addition to these pragmatic considerations, the court must also be mindful of the scope and purpose of the underlying Truth in Lending legislation. Where courts have characterized debt claims as compulsory counterclaims, the presence of those

106. Rule 23 of the Federal Rules of Civil Procedure provides in pertinent part: (a) Prerequisites to a Class Action. One or more members of a class may sue or be sued as representative parties on behalf of all only if (1) the class is so numerous that joinder of all members is impracticable, (2) there are questions of law or fact common to the class, (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and (4) the representative parties will fairly and adequately protect the interests of the class. (b) Class Actions Maintainable. An action may be maintained as a class action if the prerequisites of subdivision (a) are satisfied, and in addition: . . .(3) the court finds that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy. The matters pertinent to the findings include: (A) the interest of members of the class in individually controlling the prosecution or defense of separate action; (B) the extent and nature of any litigation concerning the controversy already commenced by or against members of the class; (C) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; (D) the difficulties likely to be encountered in the management of a class action.
107. Id.
110. Id.
claims in the lawsuit has been fatal to class certification.\textsuperscript{111}

The debt counterclaim often is viewed as antagonistic to the underlying objectives of class actions. For example, it may be found that where there are creditor counterclaims, the class proceedings will degenerate into a collection of minitrials, where individual contract claims and defenses dominate.\textsuperscript{112} Thus, the basic class certification requirement that issues of law and fact predominate will not be met. Additionally, it has been urged that if any representative party is in default, the claims and defenses of that party will not typify the claims and defenses of the class.\textsuperscript{113} In fact, although motives for bringing a class suit under the Act are generally not questioned,\textsuperscript{114} concern has been voiced about the motives of a debtor in default who initiates a class action.\textsuperscript{115}

\textsuperscript{111} See Carter v. Public Finance Corp., 73 F.R.D. 488, 492 (N.D. Ala. 1977). ("The majority of Truth in Lending cases considering the issue . . . have determined that the presence of such counterclaims renders, or may render, the class action inferior to other methods of adjudication.")

One court has indicated that findings of compulsory counterclaims are no more than a facade. "It may be suspected that district court opinions to the contrary were mere shibboleths upon which to rest a determination that a class action was not to be maintained because of difficulties likely to be encountered in its management." Jacklitch v. Redstone Federal Credit Union, 463 F. Supp. 1134, 1136 n.1 (N.D. Ala. 1979).


\textsuperscript{113} Whether a party adequately represents the remainder of the class is ordinarily a question of fact which must be decided in accordance with the facts of each case. Sussman v. Lincoln American Corp., 561 F.2d 86, 90 (7th Cir. 1977); Lirtzman v. Spiegel, Inc., 493 F. Supp. 1029, 1032 (N.D. Ill. 1980).


In support of their motions, the defendants have filed certain affidavits which state that the gross potential class is in excess of 1,000 persons, that this plaintiff had defaulted upon her contract, and that approximately 80 persons from the total class are in default. It thus appears that this plaintiff's interests would parallel those of only a nominal percentage of the class as a whole, namely, those persons who are, like herself, in default. It is obvious that the claims and defenses of this plaintiff are not typical of those of the alleged class as a whole.

A question of motivation must also bear upon this issue. Affidavits and documentary evidence submitted with the motions would indicate that the 1\% of net worth limit imposed by the Act upon class recovery would reduce the prorata recovery of each class member to a sum of $7.00 to $8.00. Thus, this plaintiff, by adopting the class action format, has elected to waive, not only herself, but, potentially, for each member of the class, 92\% to 93\% of the statutory minimum penalty to which each is entitled under the Act. It would be improper to speculate upon this plaintiff's motivation in electing the class action format of suit. Yet it would be more grossly improper to certify this plaintiff as a representative of the whole class. It is necessary to note the possibility that the class action device may have been adopted by this plaintiff as a lever which, hopefully, might alleviate her
Moreover, because individual statutory recovery usually exceeds the potential recovery available in a class action,\textsuperscript{116} there is some authority that the class mechanism is not superior to individual adjudications.\textsuperscript{117} This conclusion is faulty for two reasons. First, it expressly ignores the clear congressional intent that class actions be used as a potent enforcement tool whenever possible.\textsuperscript{118} Second, it assumes that the class members would individually bring suit if the class were not certified.\textsuperscript{119} This assumption imputes a greater level of awareness and sophistication to consumers than probably exists.\textsuperscript{120} Further, it defeats the class action objective of encouraging an action to be brought on behalf of a large number of people who would not bring suit on their own initiative.\textsuperscript{121}

Lender counterclaims may present significant administrative problems for an effective class action.\textsuperscript{122} The nature of the expanded case and issues presented obviously threatens judicial efficiency. Also, many potential class members may wish to opt out because of the counterclaims. Consequently, the resulting res

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\textsuperscript{116} Section 1640(a)(2) does not clearly state that a class representative bringing suit waives his right to an individual recovery. If a right to an individual recovery exists, there is arguably an "inherent conflict" between the plaintiff and other members of the class because the plaintiff stands to recover a much larger award. Perry v. Beneficial Finance Co., 81 F.R.D. 490, 495-96 (W.D.N.Y. 1979). In response to this argument, it has been held that plaintiff waives any right to an individual recovery by bringing a class action. Goldman v. First Nat'l Bank, 532 F.2d 10 (7th Cir.), cert. denied, 429 U.S. 870 (1976); Perry v. Beneficial Finance Co., 81 F.R.D. 490, 496 (W.D.N.Y. 1979). See also Bantolina v. Aloha Motors, Inc., 419 F. Supp. 1116 (D. Hawaii 1976). If this right is waived, then the representative plaintiff's interests are coextensive with the remainder of the class. See Perry v. Beneficial Finance Co., 81 F.R.D. 490, 496 (W.D.N.Y. 1979).


\textsuperscript{119} Ironically, the court in \textit{Carter} noted:

These class members would probably find themselves exposed to much greater liability on the counterclaim than they would ever stand to recover from the defendant in the class action, and probably would never choose to bring individual actions. For this reason the court does not believe a class action is in interest of the class members, who would probably be better off by individually controlling their suits.

73 F.R.D. at 491. Since the court admits they would not likely bring individual suits, it is difficult to perceive the putative benefit of denying class certification to permit them to control the suits they will never bring.

\textsuperscript{120} Watkins v. Simmons & Clark, Inc., 618 F.2d 398, 404 (6th Cir. 1980).


\textsuperscript{122} Id. at 493. See also Alpert v. United States Industry, Inc., 59 F.R.D. 491 (C.D. Cal. 1973).
The judicata effect of the primary action requires that notice be given to these individual class members. Moreover, defaulting class members might not appreciate the risk of entry of a judgment which could exceed any potential recovery against them. Thus, unless the notice is explicit, the class members will be bound by both the small Truth in Lending award as well as the contract adjudication.

Similarly, defaulting class members who are cognizant of the potential risks involved where a counterclaim is deemed compulsory may also seek to opt out. As a result, significant numbers of the class who have legitimate claims will be excluded, and the superiority of the class mechanism thereby defeated. There is great irony in this result. The same courts that consider the policies of the compulsory counterclaim to be paramount to the policies of the Truth in Lending Act, circuitously hold that the true policies of the Act cannot be served when compulsory counterclaims force members out of the class. It is even more ironic that the liberal joinder policy which underlies the counterclaim analysis is a basis for denial of class certification. Despite explicit congressional intent to encourage use of the class action device in Truth in Lending disclosure actions, the liberal joinder policy requiring the court to bring in several debt counterclaims supersedes this congressional mandate for joinder of consumers with identical Truth in Lending Act claims.

Some courts have tried to soften the harsh result wrought by the existence of compulsory counterclaims in class actions. One ap-

123. In addition, one court notes that the contracts may require the debtor to pay court costs and attorney's fees. Carter v. Public Finance Corp., 73 F.R.D. 488, 491 (N.D. Ala. 1977). Thus, the judgment entered on the contract would exceed the statutory award. Moreover, despite the provision for attorney's fees under the Act, the debtor might be assessed at least a proportionate share of the fees.


126. Id.

127. The court in George noted that 'concededly, adherence to the literal command of Rule 13(a) here cuts against achievement of "efficiency" by defeating a class adjudication of other common issues.' 81 F.R.D. at 6. Nevertheless, the court found the mandate of Rule 13(a) more compelling and held the counterclaims were compulsory. Id.

128. In addition to the approaches delineated in the text, two other solutions have been used. One court has held that "unnamed" class members are not opposing parties within the meaning of Rule 13. Thus, despite the compulsory character of the claims, the parties are not opposing. Assertion of the claim therefore would not be mandated by the rule. See Donson Stores, Inc., v. American Bakeries Co., 58 F.R.D. 485, 489 (S.D.N.Y. 1973). One other court has simply held that the presence of compulsory counterclaims is an insufficient
proach is to treat potential counterclaims as claims which affect only the remedy to be awarded, not the underlying liability.¹²⁹ Thus, the question of whether a specific class member will be awarded damages is determined by the validity of outstanding debt counterclaims.¹³⁰ Even though the remedies among class members might vary under this approach, common issues of law and fact would still predominate in the determination of liability.¹³¹ This analysis results in a bifurcated proceeding, involving a general liability stage and a separate remedy stage to ascertain individual relief. This approach has been criticized as only circumventing, rather than confronting, the confusion caused by compulsory counterclaims.¹³²

A second technique that has been used to tone down the harsh result in class actions is to exclude defaulting members of the class, or create a subclass. This approach operates on the theory that half a class is better than no class at all.¹³³ Where a class involves only a few defaulting members, the potency of the enforcement action is not lost. If, however, a significant segment of the class is in default and is excluded, the litigation will be deflated.¹³⁴ Moreover, compulsory counterclaims could still be asserted against individual class members and thereby be a basis for denial of class certification¹³⁵ on the ground of lack of commonality.¹³⁶

¹³² 131. Id.
¹³³ 132. George v. Beneficial Finance Co., 81 F.R.D. 4, 7 (N.D. Tex. 1977) ("Nothing is gained from allowing the suit to proceed as a class action knowing full well that the 'damage phase' of the case would be totally unmanageable.")
¹³⁵ 134. George v. Beneficial Finance Co., 81 F.R.D. 4 (N.D. Tex. 1977). The court points out that the congressional objective is disclosure. Compliance is achieved by the class action mechanism which joins a large number of people together to enforce the Act. If a significant portion of a potential class is excluded, the potency of the class action device obviously is lost. Id. at 7.
¹³⁶ Additionally, it should be noted that the time for "default" poses additional management problems. Class members may be defaulting and curing default at varying times. Even if the time for default is fixed, members who default or cure default after that date will be improperly excluded from or included in the class. Id. Moreover, if the class representative is in default, the continued viability of the action is dependent upon the initiative of other class members. Similarly, subclassing presents significant problems, since commonality of issues is still required.
¹³⁷ Id.
¹³⁸ Id.
The characterization of a debt counterclaim as compulsory may be the death knell for many class action suits. The counterclaim issue thus strikes at the very heart of the decision to certify a class action. Consequently, the consumer-plaintiff may lose one of the most potent enforcement tools for ensuring compliance with the Truth in Lending Act.

**Further Implications of the Counterclaim Issue: The Illinois Position**

The importance of uniformity in the federal forum in characterizing creditor claims in Truth in Lending Act enforcement proceedings is further demonstrated by the potential conflict which exists between the Seventh Circuit and Illinois state courts. The Seventh Circuit has endorsed the majority position on creditor contract claims, deeming them to be permissive counterclaims. The court has therefore recognized the complete independence of the Truth in Lending disclosure suit from the underlying contract action. There is some authority in the state courts, however, that a Truth in Lending Act violation could be a complete defense to a creditor contract claim. The effect of this position is to leave the creditor without a remedy.

The Seventh Circuit adopted the permissive counterclaim position in *Valencia v. Anderson Brothers Ford*. The court reviewed the positions taken by the Fifth and Fourth Circuits on the issue of counterclaims in the Truth in Lending context. Cognizant of previous holdings that the immediacy of the connection between claims does not automatically satisfy the "logical relationship" test, the court noted that the "sole connection" between the Truth in Lending Act claim and the contract claims was the initial execution of the loan instrument. The court noted that requiring a joint trial of claims emanating from this instrument would not achieve the advantages sought by the compulsory counterclaim rule. Thus, adopting the Fourth Circuit's analysis, the court declined to hold the debt counterclaims compulsory. Instead, it found that the enforcement objectives of the Truth in Lending Act were better served by denoting these claims permissive.

The debt counterclaim will rarely, if ever, satisfy independent

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137. 617 F.2d 1278 (7th Cir. 1980).
138. Id. at 1291.
139. See notes 82 through 85 supra.
jurisdictional grounds. Therefore the effect of the court’s characterization of the claim as permissive is that the lender’s remedy will be in the state forum. It is critical to the lender that the state court recognize the limited and independent nature of the Truth in Lending proceeding and not permit that action to have any effect on the debt action. Prior to the Seventh Circuit’s pronouncement in Valencia, however, one Illinois appellate court suggested that a Truth in Lending disclosure violation could be treated as a complete defense to a subsequent contract suit by the lender. The court noted that Illinois has long recognized the rule that a valid defense to contract enforcement exists where the contract is illegal under federal or Illinois law. Since it is not necessary that the relevant federal statute declare the contract void or unenforceable, the illegality defense could be based on a statutory violation. Thus, the court concluded that violations of the Truth in Lending Act or Regulation Z are grounds for asserting the defense of illegality in the lender’s suit.

The recognition of a contract defense for violations of the Truth in Lending Act creates a real quandary for the lender. For example, if an Illinois borrower, or class of borrowers, sues an Illinois lender in federal court, the lender’s counterclaim will be deemed permissive. Consequently, the lender will be expected to bring his debt claims in state court. When the lender brings suit in state court, the Illinois borrower can assert that violations of the Truth in Lending Act rendered the contract illegal and hence unenforceable.

142. Id.
143. It is unclear whether Grayling extended the defense to statutory violations of federal or state law. 53 Ill. App. 3d at 613, 368 N.E.2d at 1059. In American Buyers Club v. Zuber, 57 Ill. App. 3d 899, 373 N.E.2d 786 (1978), the court noted that “[i]t is unnecessary for us to consider whether violations of the [Illinois] act preclude enforcement of a contract although we can find no authority . . .” 57 Ill. App. 3d at 904, 373 N.E.2d at 790. The Zuber court also noted that a federal statutory violation would render the contract void. Id. at 903, 373 N.E.2d at 790.

In Piatcheck v. Fairview Reliable Loan, Inc., 474 F. Supp. 622 (S.D. Ill. 1970), this issue was further confused. There, the federal district court read Zuber as having concluded that Truth in Lending violations would not render an underlying contract unenforceable. 474 F. Supp. at 626. This reading of Zuber is inaccurate, because the Zuber decision directly addressed only the violations of the Illinois statute. Ironically, while the district court in Piatcheck stated that Grayling should be limited to its facts, it did not hesitate to rely upon Grayling. The court relied upon Grayling to support the proposition that because Truth in Lending claims can serve as a defense in a state contract action, they arise from the same transaction as debt claims on the underlying contract. Therefore, the court found that the latter, when asserted as counterclaims in federal court, should be considered compulsory.
able. The Supreme Court of Illinois has not passed upon this legal
catch 22.

The Superior Court of Pennsylvania, however, has considered
the defensive assertion of the Truth in Lending claim. In House-
hold Consumer Discount Co. v. Vespagnani,144 the defendant as-
serted that the defense of recoupment should be an available
means of asserting his Truth in Lending claim. If allowed to do so,
any statutory penalty awarded the defendant debtor would dimin-
ish the lender’s contract recovery. The court unequivocally stated
that the Truth in Lending claim can never provide a defense to an
action on the debt.146

The Pennsylvania position reflects an enlightened view. The
Truth in Lending Act was not designed to reach substantive con-
tact issues.146 Just as those issues are inappropriate in the coun-
terclaim analysis, they are also an inappropriate basis for a con-
tact defense. The Act expressly states that except in narrow
circumstances it does not affect the validity or enforceability of
any contract under state or federal law. Further, civil penalties
outlined in section 1640 are not designed to give a borrower the
benefit of his bargain. These statutory damage provisions bear no
relationship to any theory of contractual recovery. The Act’s pur-
pose, to ensure full and fair credit disclosure, therefore should not
be subverted by permitting substantive contract matters to be
raised.

CONCLUSION

The Truth in Lending Act was enacted as a prophylactic mea-
sure to secure full and fair credit disclosure. Through standardized
credit terms, the consumer is able to make informed credit deci-
sions. The purposes of the Act are achieved through various en-
fforcement mechanisms, the most important of which is the con-

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145. Id. at 356, 387 A.2d at 97.
146. Analogously, a creditor cannot “offset” debts which have been reduced to judgment
in state court. Although § 1640(h) provides that no offset may be obtained unless a court of
competent jurisdiction has entered judgment on the debt, this reference is to creditors’
debts. See note 39 supra. The purpose of this provision was to require that a debtor reduce
a lender’s liability to judgment under the Act before offsetting against the balance owed
1977) (“A debtor attempts to evade payment on a note by deducting the Act’s penalty from
his payment without a judicial determination of the liability of the lender.”). See Reid v.
sumer as "private attorney general." In this capacity, either as a class or as individuals, the credit industry is policed and compliance with the Act is encouraged.

The purposes of the Act should not be distorted by procedural mechanisms which dilute the private enforcement mechanism. Suits arising under the Act have no logical relationship to lenders' potential contract counterclaims. Consequently, individual and class actions should not be summarily defeated in federal court by counterclaims involving contract issues. The majority of courts have recognized the important function of private enforcement actions, and the separability of disclosure violations from contract issues. Thus, the majority rule excludes these state contract issues from Truth in Lending actions filed in federal court. A minority of courts persist in characterizing these counterclaims as compulsory. Because this defeats many Truth in Lending disclosure actions, neither the liberal joinder policies of the federal rules nor the policies of the Act are served.

The Seventh Circuit has recognized the complete independence of the Truth in Lending disclosure suit from underlying contract claims. It is apparent, however, that the Illinois appellate courts have not drawn the same distinction. The erection of a contract defense in state court equally subverts the underlying purpose of the Truth in Lending Act. Moreover, it can effectively deny the lender a forum for his contract or debt claim. At the earliest opportunity the Illinois courts should join their federal counterparts and correct this situation.